FPI QUARTERLY UPDATE

India's tax and regulatory developments on foreign portfolio investors

January 2026 to March 2026

BUDGET UPDATES

Key Tax Proposals under Finance Act, 2026 impacting FPIs

The Finance Bill, 2026, presented on 1 February 2026, proposed several changes relevant to FPIs.

It was enacted by the President's ascent on 30 March 2026 and shall be applicable from 1 April 2026.

Key proposals include:

- Taxation of buyback proceeds as capital gains instead of dividend income at the following rates:
  - 12.5% for long-term capital gains
  - 20% for short-term capital gains
- For promoters, an additional tax of 30% is proposed on such gains over and above the normal tax. In case of promoter companies, the tax rate on such gains is proposed to be 22%.
- Individual Persons Resident Outside India (PROI) will be permitted to invest in equity instruments of listed Indian companies through the Portfolio Investment Scheme. It is also proposed to increase the investment limit for an individual PROI under this scheme from 5% to 10% and aggregate limit from 10% to 24%.
- The amendment to the GST law to treat the activities of Intermediaries (like stockbrokers) in India to FPIs as 'export of services', resulting in no application of GST on service cost, thereby reduction in cost of investment to FPIs. The GST relief in case of such FPIs will offset the increase in STT on futures and options.

The Finance Act, 2026 has introduced revisions in Securities Transaction Tax (STT) rates applicable to certain transactions in securities, particularly derivatives. Key changes include:

Type of Transaction	Current STT Rates*	Proposed STT Rates*
Sale of option	0.1	0.15
Sale of option (where option is exercised)	0.125	0.15
Sale of Futures	0.02	0.05

** In percentage*

Tax incentives for International Financial Service Centre (IFSC) units (w.e.f. tax year 2026-27)

- Currently, IFSC units, including fund management entities, are eligible for deduction of 100% of business income for 10 consecutive years out of 15 years.
- It is proposed to extend the deduction period to 20 consecutive years out of 25 years.
- It is further proposed that the business income of these units from IFSC after the expiry of 20 years will be taxed at the rate of 15%.

These proposals mark a significant shift in taxation of buyback transactions and derivatives, impacting structuring and return expectations for FPIs. The ability to claim treaty benefits on buyback gains provides potential tax optimisation opportunities.

Amendments in relation to provisions of Income-Tax Return (ITR)

Currently, an updated ITR cannot be filed if it results in a loss position. It was proposed to allow the filing of updated ITR when such ITR reduces the loss originally reported in ITR.

Also, presently, an updated ITR cannot be filed once reassessment proceedings have been initiated. It was proposed to allow taxpayers to file an updated ITR even after a reassessment notice has been issued.

In such cases, additional income-tax payable is to be increased by 10% of the tax and interest due. Further, additional income tax paid in the said updated ITR will not attract penalty.

Present	Proposed
Within 9 months from the end of the relevant tax year	Within 12 months from the end of the relevant tax year

Note: In the Income-tax Act, 2025, the terms 'Assessment Year' and 'Previous Year' are replaced with 'Tax year' defined as the period from 1 April to 31 March.

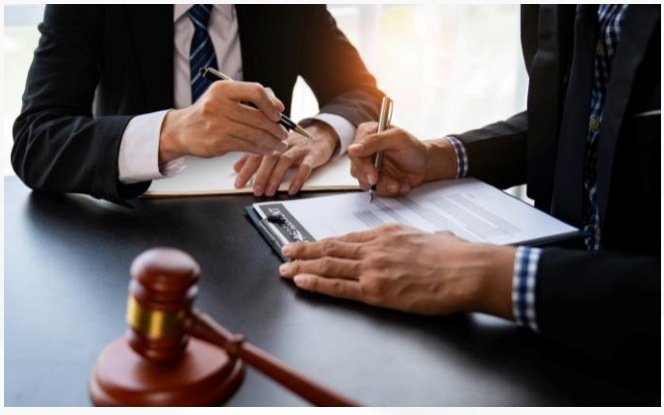
Income-tax Rules, 2026

The Central Board of Direct Taxes (CBDT) has released Income-tax Rules, 2026 aimed at simplifying and rationalising the existing rules framework.

Key changes include:

- Reduction in the number of rules and forms
- Additional disclosures in Form 10F (treaty claims)
- Enhanced reporting requirements for international taxation
- Requirement of IFSCA inputs for GAAR invocation in IFSC cases

The proposed changes may increase documentation requirements for FPIs claiming treaty benefits, particularly through enhanced Form 10F disclosures and reporting standardisation.



TAX UPDATES

India–France DTAA Amended through Signing of Protocol

The CBDT, vide press release dated 23 February 2026, announced that India and France have signed an Amending Protocol to the India–France Double Taxation Avoidance Convention (DTAC).

The Protocol introduces several key changes:

- Capital Gains Taxation: Full taxing rights on capital gains from the sale of shares are now allocated to the source country (i.e., where the company is resident).
- Removal of MFN Clause: The Protocol deletes the Most-Favoured-Nation (MFN) clause, thereby resolving long-standing interpretational issues.
- Dividend Taxation: Introduction of a split tax rate - 5% where shareholding is at least 10%, and 15% in other cases.
- Fees for Technical Services (FTS): Definition aligned with the India–US DTAA, incorporating the "make available" principle.
- Permanent Establishment (PE): Expanded to include Service PE provisions.
- Exchange of Information & Tax Recovery: Strengthened provisions, including assistance in the collection of taxes and alignment with BEPS MLI standards.

The Protocol will come into effect upon completion of ratification procedures in both countries.

Particulars	Earlier Position (Pre-Protocol)	Revised Position (Post-Protocol)
Capital Gains (Sale of Shares)	Taxing rights generally with the country of residence under Article 13 (except specific cases like immovable property rich entities).	Source-based taxation (India) for gains from the sale of shares.
MFN Clause	MFN clause allowed import of beneficial provisions from treaties with OECD countries (subject to interpretation disputes).	MFN clause removed, eliminating interpretational ambiguity.
Dividend Taxation	No clear concessional split; generally 10%/15% applied.	5% (≥10% shareholding) and 15% (others) introduced.
Fees for Technical Services (FTS)	No "make available" condition; broader scope of taxation.	FTS taxable only if "make available" condition satisfied.
Permanent Establishment (PE)	No explicit Service PE clause in the treaty.	Service PE introduced, expanding PE scope.
Exchange of Information (EOI)	Standard OECD-based EOI provisions.	Enhanced EOI aligned with BEPS / global standards.
Assistance in Tax Collection	Limited/ absent provisions for tax recovery assistance.	Mutual assistance in the collection of taxes introduced/ strengthened.
Alignment with BEPS/ MLI	Not fully aligned with the latest BEPS framework.	Aligned with BEPS recommendations and MLI standards.

This development is significant for French FPIs and investment structures, as it shifts taxing rights on capital gains to India, removes reliance on MFN benefits, and introduces clearer treaty provisions aligned with global standards.

CBDT Prescribes Procedure for Notification and Compliance of Sovereign Wealth Funds (SWFs)

The CBDT, vide circular dated 30 March 2026[1], has prescribed the application and compliance framework for Sovereign Wealth Funds (SWFs) seeking tax exemption under the Income-tax Act, 2025.

Key provisions include:

- Exemption Framework: Eligible SWFs can claim exemption on dividend, interest, specified income and long-term capital gains from investments in notified infrastructure sectors, subject to conditions such as minimum holding period of 3 years.
- Application Process: SWFs seeking notification are required to file Form I with the CBDT for approval.
- Ongoing Compliance:
  - Filing of income-tax return along with audit report
  - Submission of quarterly statements (Form II) within one month from the end of each quarter for investments made
  - Existing SWFs: Funds already notified under section 10(23FE) are not required to reapply but must comply with quarterly reporting requirements.
  - Effective Date: Applicable from 1 April 2026 onwards.

This circular introduces a structured compliance and reporting regime for SWFs, which may be relevant for government-backed foreign investors operating through FPI or similar structures investing in infrastructure assets in India.

[1] Circular No. 03 of 2026

REGULATORY UPDATES – SEBI

SEBI Board Meeting – Key Decisions Impacting FPIs

The Securities and Exchange Board of India (SEBI), vide press release dated 23 March 2026 (PR No. 18/2026), announced key decisions taken in its Board meeting covering multiple regulatory areas, including measures directly relevant for Foreign Portfolio Investors (FPIs).

A significant development is the approval of a framework to permit net settlement of funds for FPI transactions in the cash market. Currently, FPIs are required to settle trades on a gross basis, leading to higher funding requirements and foreign exchange costs. Under the revised framework, FPIs will be allowed to net off pay-in and pay-out obligations for outright transactions within a settlement cycle, while securities settlement will continue on a gross basis. This measure is expected to reduce funding costs, improve capital efficiency and enhance operational ease, particularly during high-volume events such as index rebalancing. The framework is proposed to be implemented by 31 December 2026.

Further, SEBI has introduced ease-of-doing-business measures for Alternative Investment Funds (AIFs) by allowing retention of liquidation proceeds beyond fund tenure in specified circumstances, such as pending tax or litigation matters, and by introducing the concept of "inoperative funds" with reduced compliance requirements. This may be relevant for FPIs investing through AIF structures, as it provides greater flexibility in fund wind-down and reduces compliance burden where no active investment activity remains.

The Board has also approved measures to enhance flexibility for InvITs and REITs, including permitting continued holding of SPVs after concession expiry, expanded investment avenues for temporary surplus funds, and relaxation in borrowing conditions. Additionally, amendments to the 'fit and proper person' criteria for intermediaries aim to balance regulatory oversight with ease of doing business by rationalising disqualification triggers and procedural requirements.

Overall, the decisions reflect SEBI's continued focus on improving market efficiency, reducing compliance burden, and facilitating ease of doing business. The introduction of net settlement for FPIs, in particular, is a significant operational reform expected to enhance liquidity management and reduce transaction costs for foreign investors.

SEBI Master Circular for Issue of Capital and Disclosure Requirements (ICDR Regulations)

The Securities and Exchange Board of India (SEBI) vide Master Circular (last updated February 09, 2026)[2] has updated and consolidated all circulars issued under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018.

The Master Circular incorporates all relevant circulars issued up to 31 December 2025 and serves as a comprehensive reference document governing public issues, rights issues, qualified institutional placements (QIPs) and other capital raising mechanisms.

Key areas covered include:

- Disclosure requirements in offer documents (DRHP/RHP)
- Streamlining of rights issue processes and ASBA/UPI mechanisms
- Timelines for listing and allotment in public issues
- Framework for QIPs and issuance of specified securities
- Compensation mechanisms for retail investors
- Industry standards for KPI disclosures

From an FPI perspective, this Master Circular is highly relevant as it governs primary market issuances in which FPIs participate as Qualified Institutional Buyers (QIBs). The consolidation enhances clarity on issuance processes, disclosures and timelines, thereby facilitating informed investment decisions. FPIs may particularly benefit from improved transparency in offer documents and streamlined application mechanisms, while also aligning their participation strategies with evolving regulatory requirements in primary market transactions.

SEBI Master Circular for Listing Obligations and Disclosure Requirements (LODR)

The Securities and Exchange Board of India (SEBI) vide Master Circular (last updated 30 January 2026)[3] has consolidated all circulars issued under the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

The Master Circular incorporates circulars issued up to 30 December 2025 and provides a comprehensive framework for disclosure and governance by listed entities.

Key areas covered include:

- Periodic and event-based disclosures by listed entities
- Financial reporting and audit-related requirements
- Related party transaction disclosures
- Corporate governance and board evaluation norms
- Minimum public shareholding requirements
- ESG and sustainability reporting (BRSR)

From an FPI perspective, this circular is highly relevant as it governs the disclosure and governance framework of listed companies in which FPIs invest. Enhanced disclosure standards, including ESG reporting and event-based disclosures, improve transparency, enable better risk assessment and support informed investment decisions. FPIs may also benefit from strengthened corporate governance norms and timely dissemination of material information.

[2] HO/49/14/14(2)2026-CFD-POD2/I/4518/2026
[3] HO/49/14/14(7)2025-CFD-POD2/I/3762/2026

SWAGAT-FI Framework for FPIs and FVCIs

SEBI vide circular dated 16 January 2026[4] has introduced the *Single Window Automatic and Generalised Access for Trusted Foreign Investors (SWAGAT-FI)* framework by modifying the FPI Master Circular.

The framework aims to simplify onboarding and compliance requirements for certain categories of regulated foreign investors.

Key features include:

- Eligibility extended to government entities, regulated mutual funds/ unit trusts, insurance companies and pension funds
- Introduction of a "single window" framework enabling unified registration and investment experience
- Relaxation of certain KYC and documentation requirements
- Extension of registration validity to 10 years for SWAGAT-Fis
- Simplified renewal requirements, including reduced reporting obligations

The circular also provides unified investment accounts across FPI, FVCI and other permitted routes.

From an FPI perspective, this is a significant regulatory development, as it materially simplifies entry, compliance and operational requirements for eligible institutional investors. The introduction of a single-window mechanism and longer registration validity is expected to enhance the ease of doing business, reduce compliance burden and potentially increase foreign participation in Indian markets.

Introduction of Closing Auction Session (CAS) in Equity Cash Segment

SEBI vide circular dated 16 January 2026[5] has introduced a **Closing Auction Session (CAS)** mechanism in the equity cash segment.

Key features include:

- Introduction of a 20-minute closing auction session (3:15 PM to 3:35 PM)
- Determination of closing price based on equilibrium price instead of VWAP
- Applicability initially to securities with derivatives contracts (phased implementation)
- Alignment of derivatives settlement pricing with CAS-based closing prices
- Price band of ±3% during CAS and defined order matching mechanisms

From an FPI perspective, this is a market structure change with direct trading impact. FPIs, particularly institutional investors and passive funds, may benefit from improved price discovery, deeper liquidity at close, and reduced tracking error. However, it may also require adjustments to execution strategies, especially for large trades and index-linked investments.

Digital Signature Certificate (DSC) Integration for FPI Registration

SEBI vide press release dated 08 January 2026[6] has introduced enhanced Digital Signature Certificate (DSC) functionality within the Common Application Form (CAF) portal for FPI registration.

Key features include:

- Integration of DSC application and FPI registration into a single unified process
- Ability for applicants to obtain DSC directly through the CAF portal
- Streamlining of onboarding and documentation processes
- Availability of detailed process flows and guidance on the India Market Access Portal

From an FPI perspective, this circular is operationally significant, as it simplifies and digitises the onboarding process. The integration reduces procedural friction, improves efficiency and supports faster registration timelines for FPIs entering the Indian market.

Revised Norms for Third-Party Reviewer for Green Debt Securities

The Securities and Exchange Board of India (SEBI) vide circular dated 27 February 2026[7] has revised the norms governing the appointment of independent third-party reviewers or certifiers for green debt securities. The circular mandates that issuers appoint an independent reviewer to ensure that the issuance complies with the prescribed definition and framework for green debt securities. The reviewer is required to be independent of the issuer and its management, possess relevant expertise in ESG instruments, and be remunerated in a manner that avoids conflicts of interest.

The scope of such review includes verification of the use of proceeds, evaluation of project selection criteria, and overall compliance with ESG requirements. The revised framework also aligns the requirements for green debt securities with the broader regulatory framework applicable to ESG debt instruments.

This circular is relevant from an FPI perspective, particularly for investors allocating capital to ESG or green debt instruments in India. It enhances the credibility, transparency, and standardisation of such investments, thereby strengthening investor confidence and facilitating better due diligence.

[4] HO/19/34/14(5)2025-AFD-POD2/I/2703/2026
[5] HO/47/11/11(3)2025-MRD-POD2/I/2765/2026
[6] 03/2026
[7] HO/17/11/24(1)2026-DDHS-POD1/I/5967/2026

Creation / Invocation of Pledge of Securities

The Securities and Exchange Board of India (SEBI) vide circular dated 05 February 2026[8] has introduced amendments to the framework governing the creation and invocation of pledge of securities through the depository system. The circular aligns the pledge framework with the provisions of the Indian Contract Act, 1872 by requiring the pledgee to provide reasonable notice to the pledger prior to the sale of pledged securities. It also introduces standardisation in the format of pledge request forms and mandates that depositories provide intimation to both pledger and pledgee upon invocation of pledge, with the pledgee being recorded as the beneficial owner.

These changes aim to enhance legal clarity, procedural consistency, and investor protection in pledged securities transactions.

From an FPI standpoint, the circular is relevant for entities involved in collateralised transactions, margin funding, or securities lending arrangements. It strengthens the enforceability of pledge rights, improves transparency in the invocation process, and reduces potential disputes between counterparties.

Categorisation and Rationalisation of Mutual Fund Schemes

The Securities and Exchange Board of India (SEBI) vide circular dated 26 February 2026[9] has revised the categorisation and rationalisation framework for mutual fund schemes. The circular introduces a comprehensive restructuring of scheme classifications across equity, debt, hybrid, lifecycle, and other categories, along with detailed scheme characteristics and uniform descriptions. It also introduces portfolio overlap limits, particularly capping overlap in certain scheme categories, and mandates periodic disclosure of such overlap to enhance transparency.

Further, the circular discontinues solution-oriented schemes, standardises naming conventions to ensure schemes remain "true-to-label," and requires mutual funds to align existing schemes with the revised framework within a prescribed timeline.

From an FPI perspective, this circular has moderate relevance, especially for investors accessing Indian markets through mutual fund structures. The revised framework enhances transparency, improves comparability across schemes, and reduces the risk of overlapping exposures, thereby aiding more informed investment decisions. In this regard, SEBI has issued multiple guidelines which have been stated as follows:

- The Securities and Exchange Board of India (SEBI) vide circular dated 04 March 2026[10] has prescribed detailed guidelines governing custodians pursuant to amendments in the SEBI (Custodian) Regulations, 1996. The circular introduces a comprehensive framework covering segregation of activities, governance standards, risk management practices, outsourcing norms, and infrastructure requirements.
- The Securities and Exchange Board of India (SEBI) vide circular dated 06 March 2026[11] has introduced a voluntary lock-in (debit freeze) facility for mutual fund investors. Under this framework, investors are provided an option to freeze debit transactions in their mutual fund folios, ensuring that no units can be redeemed or transferred until the freeze is lifted. The facility will be made available through the MF Central platform and will be applicable to both demat and non-demat holdings, subject to KYC compliance.
- The Securities and Exchange Board of India (SEBI) vide circular dated 13 March 2026[12] has specified conditions governing borrowing by mutual funds, particularly intraday borrowings. The circular clarifies that mutual funds may undertake intraday borrowings to address timing mismatches in redemption payouts, subject to strict conditions.
- The Securities and Exchange Board of India (SEBI) vide circular dated 25 March 2026[13] has issued an addendum to the earlier circular on borrowing by mutual funds. The circular defers the implementation of guidelines relating to intraday borrowings to 15 July 2026, in order to address operational challenges faced by asset management companies.

[8] HO/47/14/12(1)2026-MRD-POD2/I/4229/2026
[9] HO/24/13/15(2)2026-IMD-RAC4/I/5764/2026
[10] HO/19/(1)2025-AFD-FPICELL/I/5928/2026
[11] HO/24/12/12(5)2026-IMD-SEC-1/I/6373/2026
[12] HO/(92)2026-IMD-POD-2/I/6961/2026
[13] HO/(92)2026-IMD-POD-2/I/7885/2026

REGULATORY UPDATES – IFSCA

One-time Window for Extension of Validity of Placement Memorandum (PPM)

The International Financial Services Centres Authority (IFSCA) vide circular dated 27 January 2026[14] has introduced a one-time window to extend the validity of Placement Memorandum (PPM) for Venture Capital Schemes and Restricted Schemes under the IFSCA (Fund Management) Regulations, 2025.

Key features include:

- One-time window of 3 months to apply for extension of expired or soon-to-expire PPMs
- Extension of validity by an additional 6 months upon approval
- Applicable to both schemes that have not commenced investments and those that have commenced but not achieved minimum corpus
- Requirement to re-file PPM with no material changes in key aspects such as investment strategy, structure and objectives
- Payment of 50% of fresh filing fees for the extension

From an FPI perspective, this circular is relevant for FPIs investing through IFSC-based fund structures, particularly in venture capital and restricted schemes. The extension provides flexibility in fundraising timelines, which may support smoother capital deployment and reduce fund launch risks in volatile market conditions.

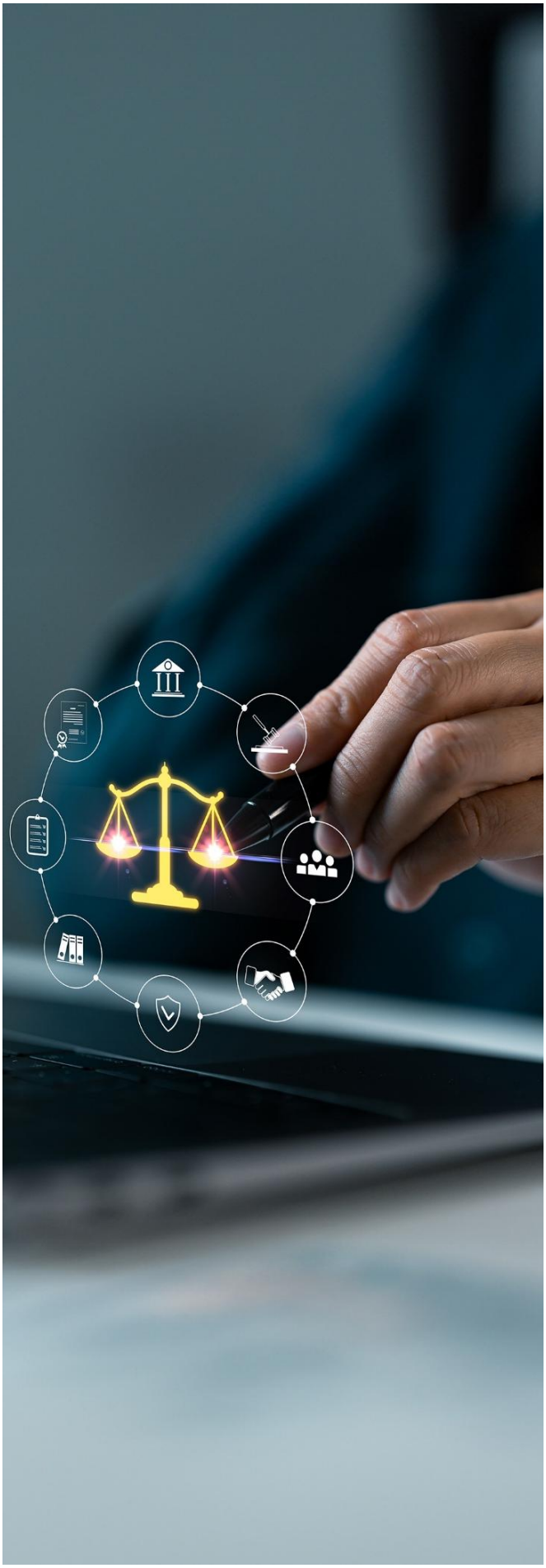
Procedure and Clarification on Third-Party Fund Management Arrangements

IFSCA vide circular dated 16 January 2026[15] has clarified the procedure for filing scheme applications under Third-Party Fund Management arrangements.

Key provisions include:

- Mandatory submission of detailed documentation relating to third-party fund managers, including registration, governance structure and UBO details
- Requirement to disclose investment track record, strategy and assets under management
- Declaration and undertaking for compliance with regulatory provisions
- Mandatory filing through IFSCA Single Window IT System (SWIT)

From an FPI perspective, this circular is relevant for global asset managers and FPIs using IFSC fund platforms, as it formalises due diligence and disclosure requirements in third-party fund management structures. The enhanced transparency and regulatory oversight may strengthen investor confidence but could also increase documentation and compliance requirements.



[14] IFSCA-IF-10PR/1/2023- Capital Markets/27012026
[15] IFSCA/AIF/218/2025-Capital Markets

REGULATORY UPDATES – RBI

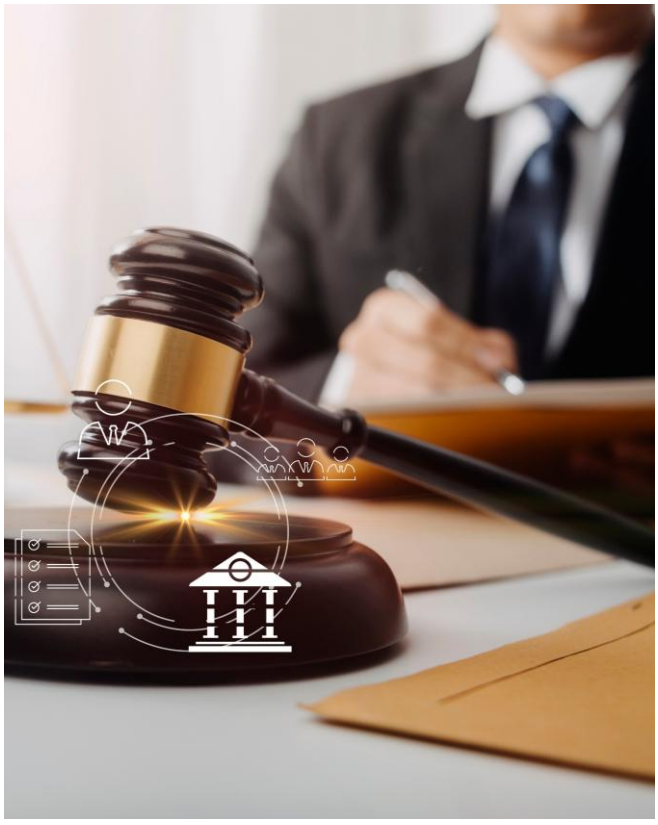
Rationalisation of Voluntary Retention Route (VRR) Framework

The Reserve Bank of India (RBI), vide circular dated 06 February 2026[16], has introduced key changes to the Voluntary Retention Route (VRR) framework for Foreign Portfolio Investors (FPIs) investing in debt instruments.

The circular provides that investment limits under the VRR shall now be subsumed within the overall investment limits applicable to FPIs under the General Route. Accordingly, investments in Central Government Securities (including Treasury Bills), State Government Securities and corporate debt instruments made under VRR will be counted within the respective limits prescribed under the General Route.

Further, FPIs that had committed to retention periods longer than the minimum stipulated period are now permitted to exit the VRR (fully or partially) after completion of the minimum retention period, thereby providing additional flexibility in managing their investment portfolios. The revised framework will be effective from 1 April 2026, and all existing VRR investments will be migrated to the General Route limits.

This development simplifies the regulatory framework governing FPI debt investments by removing the distinction between VRR and General Route limits, thereby improving the fungibility of investments and enhancing operational flexibility. The relaxation in exit conditions further allows FPIs to dynamically manage liquidity and portfolio allocation.



RECENT JURISPRUDENCE

Supreme Court Holds Mauritius-based Investment Entities Not Eligible for DTAA Benefits on Indirect Transfer; Upholds Denial of Treaty Relief in Tiger Global Case

The taxpayers, Tiger Global International II Holdings[17] (along with affiliated entities), were Mauritius-based investment companies holding valid Tax Residency Certificates (TRCs) and registered as global business entities. The taxpayers held shares in a Singapore company, which in turn derived substantial value from assets located in India (Flipkart group).

- During the relevant period, the taxpayers transferred shares of the Singapore entity to a third-party investor (Walmart group) and claimed exemption from capital gains tax in India under Article 13 of the India–Mauritius DTAA, contending that such gains were taxable only in Mauritius.
- The Indian tax authorities denied nil withholding certificate and contended that the transaction constituted an indirect transfer of Indian assets, taxable in India under Section 9(1)(i) of the Income-tax Act, 1961. The matter was referred to the Authority for Advance Rulings (AAR), which rejected the application on the ground that the transaction was prima facie designed for tax avoidance.
- The Delhi High Court reversed the AAR ruling and held that the taxpayers were entitled to DTAA benefits, noting the existence of TRCs, economic substance in Mauritius, and applicability of grandfathering provisions under the treaty.
- On appeal, the Supreme Court examined the interplay between domestic tax law, DTAA provisions, GAAR framework, and judicial anti-avoidance principles. The Court analysed legislative developments post Vodafone ruling, including the introduction of indirect transfer provisions, GAAR, and amendments to the India–Mauritius DTAA.
- The Supreme Court held that a Tax Residency Certificate (TRC) is not conclusive proof for claiming treaty benefits, and that tax authorities are entitled to examine the substance of the transaction, including control, management and commercial purpose. It observed that Circular No. 789 does not prevent scrutiny in cases involving potential treaty abuse.
- The Court emphasised that GAAR and judicial anti-avoidance principles can override treaty benefits, and that transactions lacking commercial substance or structured primarily for tax avoidance may be denied treaty protection.
- On facts, the Court upheld the findings of the AAR that the taxpayers' structure lacked sufficient commercial substance, and that the arrangement was designed to obtain treaty benefits. It noted that control and decision-making were not effectively exercised in Mauritius, and the entities functioned as part of a broader investment structure.

[16] A.P. (DIR Series) Circular No. 21
[17] Civil Appeal No. 262 OF 2026

- The Supreme Court further held that the transaction was not protected by grandfathering provisions, as GAAR principles permit examination of the overall arrangement, and not merely the date of investment.
- Accordingly, the Court upheld that the gains arising from the transfer of shares of the Singapore company (deriving value from Indian assets) were taxable in India, and the taxpayers were not entitled to claim exemption under the India–Mauritius DTAA.

Delhi Income Tax Appellate Tribunal (ITAT) Holds Gains from Stock Derivatives Not Taxable in India under India–Mauritius DTAA

The taxpayer, Estee India Fund[18], is a Mauritius-based investment fund registered as a Category II Foreign Portfolio Investor (FPI) with SEBI. During the relevant assessment year, the taxpayer engaged in trading of Futures and Options (F&O) in both currency derivatives and stock derivatives, maintaining a hedged portfolio strategy.

- The taxpayer claimed that gains arising from such derivative transactions were not taxable in India in accordance with Article 13 of the India–Mauritius Double Taxation Avoidance Agreement (DTAA), contending that such gains fall under Article 13(4) and are taxable only in the country of residence (Mauritius).
- The Assessing Officer accepted that gains from currency derivatives were not taxable in India; however, gains arising from stock derivatives were treated as capital gains from shares and taxed under Article 13(3A) of the DTAA. The tax authorities argued that since derivatives derive value from underlying shares, such transactions are akin to trading in shares.
- The Delhi ITAT examined the nature of derivatives vis-à-vis shares and held that the approach adopted by the tax authorities was fundamentally flawed. The Tribunal observed that derivatives and shares are distinct financial instruments, even though derivatives may derive their value from underlying shares. Derivatives represent contractual rights and obligations and do not confer ownership or shareholder rights.
- The Tribunal referred to the definition of "shares" under the Companies Act, 2013 and the definition of "securities" under the Securities Contracts (Regulation) Act, 1956, noting that derivatives are specifically included within the broader category of securities and are not equivalent to shares. Accordingly, derivatives constitute a separate class of assets.
- The ITAT further relied on judicial precedents, including Vanguard Funds Public Ltd. and Sigma Global Fund, to reiterate that assets deriving value from underlying shares cannot be equated with shares themselves. It emphasised that a derivative contract is an independent financial instrument that can be traded without actual ownership of the underlying asset.
- On interpretation of the DTAA, the Tribunal held that Article 13(3A) specifically applies only to gains arising from alienation of shares, and does not extend to derivative instruments. Consequently, gains from derivatives fall within the residual clause under Article 13(4), which provides that gains from assets not specifically covered shall be taxable only in the country of residence.
- Accordingly, the ITAT held that gains arising from stock derivative transactions are not taxable in India and are taxable only in Mauritius under Article 13(4) of the DTAA, and thus allowed the taxpayer's claim for exemption.

[18] ITA NO.1955 (DEL) OF 2025

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169
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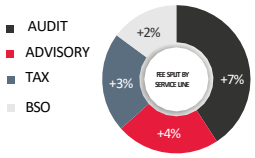
GROWTH BY SERVICE LINE



GROWTH BY REGION

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