



**Software Finance & Tax Executives Council**

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March 12, 2013

**Via Email**

Hon. Devin Nunes  
Chairman  
Subcommittee on Trade  
Committee on Ways and Means  
United States House of Representatives  
1102 Longworth House Office Building  
Washington, DC 20515

**Re: Letter for the Record:  
Hearing on U.S.-India Trade Relations: Opportunities and Challenges**

Dear Chairman Nunes:

This letter conveys the views of the Software Finance and Tax Executives Council (SoFTEC) with respect to your hearing tomorrow on U.S.-India Trade Relations: Opportunities and Challenges. U.S. based multinational software companies have long enjoyed robust trade with customers and have a strong record of making substantial investments in India. However, recent tax legislation and administrative policies in India have erected significant non-tariff barriers that create uncertainty and threaten to retard the previously robust trade with and investment in India by software companies. We ask that this letter be made a part of the record of the hearing.

SoFTEC is a trade association providing software industry focused public policy advocacy in the areas of tax, finance and accounting. SoFTEC represents the leading developers of software and is the voice of the industry on tax issues. Many SoFTEC members have customer, employees and facilities in India and it thus has an interest in providing its views on the subject matter of the hearing.

In particular, SoFTEC is concerned that recent retroactive legislative changes to the tax laws of India make it exceedingly difficult for software companies to determine their tax obligations to India for current and prior years. Those legislative changes also throw into doubt the efficacy of cases decided by the courts of India, which undermine the rule of law further exacerbating the difficulty in predicting how the Indian tax laws will be applied to foreign software businesses. These retroactive legislative changes also attempt to unilaterally change recognized interpretations of standard terms used in bilateral tax treaties, changes that are inconsistent with established treaty interpretations, which lead to extensive double taxation of profits earned in India by U.S.-based companies. Last, SoFTEC is concerned that the

mechanisms for resolving tax disputes with the Indian government are inadequate and ineffective, resulting in expensive and time-consuming controversies and double taxation. .

## **1. Retroactive Legislative Changes and Tax Treaty Interpretation:**

Last year, in Finance Bill 2012, the Indian legislature approved numerous changes to its Income Tax Act, some provisions of which would retroactively change the tax law of India as far back as 1962. Many of these changes are directed at how the Indian tax authorities are to interpret bilateral income tax treaties, including a treaty with the United States ratified in 1989.

As applied to software, the definition accepted around the world of the term “royalty,” as evidenced by the OECD and UN model tax conventions, generally only includes payments for the right to make copies of software and distribute them to the public. The term “royalty” does not include payments for the right to use software copies. There are many cases decided by the courts in India that follow this interpretation. Finance Bill 2012 departed from this internationally accepted definition of the term “royalty” by including within the definition payments for the right to “use” software. The Bill also purported to make this new interpretation retroactive to 1976. This different interpretation is leading to disputes between software companies, the U.S. tax authorities, and the tax authorities of India over whether payments of tax based on India’s expansive interpretation of the definition of “royalty” is eligible for a U.S. tax credit, leading to double taxation.

Many of the tax provisions of Finance Bill 2012 are retroactive to the dates of enactment of the Income Tax Act (1962) or amendments thereto. The tenor of these retroactive provisions is to upset past and future decisions by the Indian courts. These provisions even go so far as to reverse court decisions with respect to the very taxpayers who secured the decisions. These provisions essentially deprive all taxpayers, foreign and domestic alike, of judicial review of tax assessments asserted by Indian tax authorities. The inability to obtain meaningful judicial review of tax assessments seriously undermines taxpayer confidence in the rule of law in India, creating significant financial uncertainty and impeding their ability to trade with India.

India has a significant number of bilateral tax treaties containing provisions Finance Bill 2012 purports to modify by defining terms for tax treaty purposes. SoFTEC believes the appropriate process for defining terms contained in bilateral tax treaties is consultation with the treaty counterparty. Unilaterally defining terms in a bilateral tax treaty erodes confidence by taxpayers and treaty counterparties that the treaty will be respected. Tax treaties are supposed to provide certainty for taxpayers and reduce the risk of double taxation. The provisions in Finance Bill 2012 relating to tax treaty interpretation promote uncertainty.

The tax provisions of Finance Bill 2012 promote opacity and unpredictability in the Indian tax law with the effects of deterring foreign investment and making software and information products more expensive for India’s consumers.

## **2. Tax Dispute Resolution:**

Many multinational taxpayers with operations in India face protracted tax disputes with Indian tax authorities and view the process for resolving those disputes as “broken.” Many of

these disputes center around so-called “transfer pricing” which is a process for allocating business profits between countries, with the taxpayer exposed to double taxation when two countries lay claim to the right to impose tax on the same profits. Usually, such disputes are worked out in negotiations between what is known as the “competent authority” of each country. In the United States, the competent authority is the Deputy Commissioner (International) of the Internal Revenue Service. The government of India has a similar post within its tax authority.

Many times, a business will attempt to negotiate what is known as a “bilateral advance pricing agreement” which provides certainty over how their profits will be split between two countries and avoid transfer pricing disputes. However, the U.S. Competent Authority refuses to engage in bilateral advance pricing agreements with India because of a large backlog of double tax cases with India that have proven difficult to resolve. Indian competent authority appears to be negotiating double taxation cases not based on the facts and circumstances of the each case, but based on policy and revenue targets.

The backlog of tax disputes also is a problem. Some U.S. software companies have more cases pending in India than they do in the rest of the world, some of which date from the 1996 tax year. There is an estimated 60,000 cases in the pipeline. For the assessment year 2009-10, more than 12,000 tax evasion cases were launched, while only 600 were resolved. One U.S. software company has 17 cases pending in the Indian courts and 61 cases in appeals with the administration. The length of time these complex cases take to resolve and the inability to trust that a favorable court decision will be honored by the tax administrators or not retroactively overturned by the legislature only leads to needless expense and greater uncertainty.

The U.S. tax treaty with India dates to 1989 and contains no mechanism for binding arbitration of tax disputes. Should the U.S. and India undertake negotiations over revisions to the treaty, the U.S. negotiators should insist on inclusion of an alternative dispute resolution procedure to more efficiently and expeditiously resolve tax disputes. Specifically, any revised tax treaty between the United States and India should include a provision for mandatory binding arbitration of income tax disputes.

**Conclusion:**

SoFTEC thanks the Chairman for the opportunity to present these views with respect to the Hearing on U.S.-India Trade Relations: Opportunities and Challenges. Please contact the undersigned at (202) 486-3725 or [mnebergall@softwarefinance.org](mailto:mnebergall@softwarefinance.org) with regard to any questions or for more information.

Respectfully submitted,



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