Australian Government
Australian Taxation Office

Taxation Ruling compendium – TR 2026/2

Relying on this Compendium

This Compendium of comments summarises and provides responses to submissions received during public and targeted consultation on draft TR 2024/D1 *Income tax: royalties – character of payments in respect of software and intellectual property rights*. It is intended to promote transparency and explain how stakeholder feedback was considered in finalising the document only.

It is not a publication that has been approved to allow you to rely on it for any purpose and is not intended to provide you with advice or guidance, nor does it set out the ATO's general administrative practice. Therefore, this Compendium does not provide protection from primary tax, penalties or interest for any taxpayer that purports to rely on any views expressed in it.

Consultation period: 17 January 2024 to 1 March 2024

We thank all submitters for their time and contributions.

Summary of issues raised and responses

Issue 1 – insufficient guidance

Paragraph or section of draft product

Not applicable – relevant to document usability

Issue raised

TR 2024/D1 does not provide taxpayers with sufficient guidance to enable accurate self-assessment of whether their software arrangement will be subject to royalty withholding tax.

The purpose of public rulings is to provide certainty to taxpayers on the ATO view and make it easier to comply, yet the view in the draft Ruling will be challenging to apply in practice. The ATO says that the conclusion is based on specific facts and circumstances; this will provide little comfort to taxpayers who need to apply the ATO guidance.

ATO response

The Ruling focuses on setting out the principles that should be applied in working out whether a payment is a royalty. We recognise that the Ruling deals with only one element of a royalty withholding tax liability. How the law applies is necessarily dependent upon the facts and circumstances of each software intermediation arrangement; although there may be many similarities, they are not universally the same.

The Ruling sets out the ATO view on the characterisation of payments made under a 'software intermediation arrangement', which focuses on the tax consequences for software intermediaries making the payment. The rights granted to, or used by, a software intermediary are unlikely to be the same as those granted to or used by an end-user. Notably, the Ruling does not cover the character of payments made directly from an end-user to the owner or licensee of the intellectual property (IP), or payments to a software intermediary acting as agent for the owner or licensee of the IP.

Outcome

Clarified

Issue 2 – approach taken is too broad

Paragraph or section of draft product

Not applicable – relevant to document scope

Issue raised

The draft Ruling can be applied broadly. For example, under the proposed view, distribution arrangements involving physical copies, digital downloads and software-as-a-service (SaaS) can give rise to a royalty which would be subject to Australian withholding tax. Arrangements such as this are not limited to businesses in the technology sector.

The Commissioner's views in the draft Ruling appears to extend beyond related parties and could technically apply to arrangements entered into between unrelated parties.

ATO response

The focus of the Ruling is on software intermediaries, not end-users.

Outcome

No change

Issue 3 – simple use

Paragraph or section of draft product

Not applicable – relevant to document scope

Issue raised

The lack of comments in the draft Ruling on whether payments for the 'simple use' of software by end-users are royalties subject to withholding tax could potentially cause confusion over whether simple uses of software by end-users give rise to any royalty withholding tax obligations. This could create an unforeseen compliance burden for these users, including individuals and small business.

ATO response

We have not reintroduced any reference to simple use because we do not think it is relevant to the characterisation question considered by the Ruling. The term 'simple use' is not found in the standard tax treaty definition of 'royalty', nor in the domestic tax law definition. Nor is it a term that is relevant to Australian copyright law. Further, the term was used in Taxation Ruling TR 93/12 *Income tax: computer software* (now withdrawn) in relation to end-users of software whereas this Ruling focuses on software intermediaries.

Under draft Practical Compliance Guideline PCG 2026/D4 *Royalty characterisation of payments relating to intermediation or distribution arrangements – ATO compliance approach*, which outlines our compliance approach, it is proposed that payments by end-users of software that fall within the green zone will be categorised as low risk.

Outcome

No change

Issue 4 – reliance on prior rulings

Paragraph or section of draft product

Not applicable – relevant to ruling commencement

Issue raised

The Commissioner should make clear the circumstances in which taxpayers can be considered to have ‘appropriately relied upon’ TR 93/12 and how that may be evidenced in practice. Where the Commissioner cannot provide this necessary guidance, the Commissioner should alter the date of effect such that the final Ruling has prospective application only.

ATO response

We reaffirm our position that TR 93/12 will continue to apply to periods prior to its withdrawal (25 June 2021), to the extent that it has been appropriately applied by taxpayers (see paragraph 38 of the final Ruling). The appropriateness or otherwise of that reliance will itself depend on facts and circumstances.

Outcome

No change

Issue 5 – date of effect

Paragraph or section of draft product

Not applicable –relevant to ruling commencement

Issues raised

The following issues were raised in relation to the date of effect of the final Ruling:

- The changes in the draft Ruling from TR 93/12 and draft Taxation Ruling TR 2021/D4 *Income tax: royalties - character of receipts in respect of software* (now withdrawn) are significant, and the Commissioner’s propositions have not yet been tested before a court. A more extensive consultation period should have been allowed before putting it in effect.
- The final Ruling should offer a transition period during which taxpayers can make necessary adjustments regarding their present arrangements.
- The final Ruling should apply prospectively only after its publication. TR 93/12 should otherwise apply. This position is in accordance with the Commissioner’s views in Law Administration Practice Statement PS LA 2011/27 *Determining whether the ATO's views of the law should be applied prospectively only*.

- The final Ruling should apply only to new arrangements entered into after the date of its issue. The law provides that to the extent a public ruling is withdrawn, it 'continues to apply to schemes to which it applied that had begun to be carried out before the withdrawal …'. The ATO should clarify how this provision applies to taxpayers relying on TR 93/12.
- The draft Ruling states that it will not apply to taxpayers to the extent it conflicts with the terms of settlement of a dispute agreed to before the date of issue. The final Ruling should also clarify that prior undertakings entered through collaborative processes, such as advance pricing arrangements, should also be respected.

ATO response

The Ruling applies to payments made both prior to and after the date of issue. We have made this decision because, in their totality, the principles in the Ruling represent how we have sought to apply the law as a longstanding practice. This Ruling does not represent a change of view, although it does set out how we think that view applies to different facts such as new modes of providing software and different software intermediation arrangements.

The application of the royalty withholding tax provisions themselves depend upon the timing of the payment of the royalty, and not when a particular contract was entered into.

Our compliance work has been consistent overall with the position set out in the Ruling (and also with the draft Ruling, and the prior draft, Taxation Ruling TR 2021/D4 *Income tax: royalties – character of receipts in respect of software*). See also PCG 2026/D4.

Outcome

No change

Issue 6 – structure

Paragraph or section of draft product

Paragraphs 20 to 22, 23 to 41 and 116 to 117

Issue raised

It is unclear whether the following constitute a Ruling:

- paragraphs 20 to 22, which are a statement of the Commissioner's views on the significance of the decision in *International Business Machines Corporation v Commissioner of Taxation* [2011] FCA 335 (*IBM Corporation*)

- the 2 scenarios given in paragraphs 23 to 41 and paragraphs 116 and 117 which are built on untested conclusions of intellectual property law and do not reflect significant variations in software business model fact patterns.

The expression ’of this Ruling’ is used several times in the ‘Ruling’ part of the document to refer to material in the Appendix, which is not a Ruling.

ATO response

There is a clear delineation of the legally binding part of the final Ruling (up to and including paragraph 38) and the non-binding Explanation. In particular, Part 2 of Appendix 1 to the Ruling contains an explanation of provisions of the *Copyright Act 1968* (Copyright Act) that may be relevant in ascertaining whether there is the use of, or right to use, any copyright on the facts of any particular case. As noted at the beginning of Appendix 1 to the Ruling, the Explanation does not form part of a binding public ruling.

Outcome

No change

Issue 7 – definitions

Paragraph or section of draft product

Definitions

7.1 – software arrangement

Issue raised

The term ‘software arrangement’ is broad and should be changed to ‘software *distribution* arrangement’ to make clear the final Ruling is intended to apply to arrangements involving the distribution of software and not the use of software in the distribution of goods and services.

In the definition of ‘software arrangement’, the phrase ‘for the right to be in a position’ may be better expressed as ‘which enable it’. There is no singular ‘right’ which creates such an outcome.

ATO response

The final Ruling uses a tightened definition of ‘software intermediation arrangement’ (the term replacing ‘software arrangement’), consistent with the focus of the Ruling being software intermediaries (sometimes referred to as distributors) and not end-users.

7.2 – distributor

Issue raised

The definition of 'distributor' in the draft Ruling is broad and can create uncertainty, particularly in the context of software rights that may be considered 'embedded' in tangible products sold through an Australian member of the taxpayer's group. The definition of 'distributor' should specifically exclude end-users who are using software for the carrying on of their usual business to provide certainty.

It should be made clear in the final Ruling that the definition of a 'distributor' does not include an entity in a corporate group in this circumstance. Consequently, the ATO should ensure that the definitions used for a number of copyright concepts, such as 'reproduction right' and 'authorisation right' do not inadvertently give rise to the same issue.

ATO response

Whether an arrangement is a 'software intermediation arrangement' needs to be considered on a case-by-case basis, and with a careful examination of the agreement between the parties. This was the approach taken in *IBM Corporation*, and is consistent with the approach taken by the High Court in *Commissioner of Taxation v PepsiCo Inc & Anor* [2025] HCA 30 (*PepsiCo*).

Whether an entity is engaged in the sale of software that is 'embedded' in tangible products does not alter the approach to characterisation of any payments that entity makes for the purchase, or distribution, of those tangible products. The storage medium of software is not determinative of the characterisation of any payment. Similarly, whether the entity is a member of a corporate group does not determine the character of any payment made. The character of a payment depends upon whether it is 'for' any IP rights used or granted, or falls within another element of the royalty definition.

7.3 – software and computer games

Issue raised

The definition of 'software' in the glossary, and in the context of paragraph 126 (referring to paragraphs 130 to 174 of the draft Ruling), indicates that the term 'software' actually refers to 'computer program'. The definition of 'computer program' in the Copyright Act is broad. Copyright may not subsist in everything captured in this definition of 'computer program'.

It is not clear in the draft Ruling how the Commissioner classifies 'computer games', although it appears the Commissioner considers them 'computer programs'. However, existing case law (*Galaxy Electronics Pty Ltd v Sega Enterprises Ltd* & *Anor; Gottlieb Enterprises Pty Ltd v Sega Enterprises Ltd & Anor* [1997] FCA 403, per Lockhart, Wilcox and Lindgren JJ) has considered computer games to be cinematograph films for the purposes of the Copyright Act, rather than 'computer programs'.

ATO response

Some minor changes to certain definitions have been made for clarity. The final Ruling does not define ‘software’ (at paragraph 7) but a description of it continues as part of the Explanation (see paragraph 97).The definition of ‘computer program’ contained in Table 1 of the draft Ruling is reproduced verbatim from section 10 of the Copyright Act. This is retained in the final Ruling.

Scenario 3 of the draft Ruling, regarding distribution of physical copies of computer games, has not been retained in the final Ruling, given the publication of PCG 2026/D4. PCG 2026/D4 outlines our proposed compliance approach to identifying whether any part of a cross-border payment made to a non-resident is a royalty and subject to withholding tax.

Outcome

Clarified

Issue 8 – interpretation of the Copyright Act

Paragraph or section of draft product

Not applicable – relevant to document scope

Issues raised

The following issues were raised in relation to statements about Australian copyright law in the draft Ruling:

- The rules about public rulings do not allow the Commissioner to make a public ruling about the Copyright Act. The Commissioner’s extensive views on copyright and IP rights are unlikely to be binding.
- The ATO’s view on whether payments are royalties rely heavily on a liberal interpretation of copyright law and intellectual property law.
- Comments in the draft Ruling may be contestable and the Commissioner should carefully consider the comments provided by experts in this area of law.
- The tax analysis is based on incorrect assumptions or misunderstandings about the operation of Australian copyright laws, which would affect the legitimacy of the Ruling were it to be finalised in its current form.
- The ATO should release any advice it has obtained on copyright law which would be similar to the ATO publishing Counsel advice on section 254T of the *Corporations Act 2001* when Taxation Ruling TR 2012/5 *Income tax: section 254T of the Corporations Act 2001 and the assessment and franking of dividends paid from 28 June 2010* was published.

ATO response

The discussion about how we see principles of copyright and IP rights is contained in the Explanation section of the Ruling and does not form part of the binding public ruling. However, we have included 2 examples in the binding section, where the application of Australian copyright law forms part of the facts underpinning the conclusion that is binding on us.

The 'liberal interpretation' referred to in the draft Ruling is a quote that references the approach to interpreting the Copyright Act applied by the High Court in *University of NSW v Moorhouse* [1975] HCA 26. It has been retained in the Ruling.

We consider that the copyright law principles discussed in the Explanation part of the Ruling is sufficiently supported by the case law referenced therein, and are willing to test our position in the courts.

Outcome

No change

Issue 9 – relevance of infringement

Paragraph or section of draft product

Scenario 1 – performance of contract requires use of copyright rights

Issue raised

A more appropriate approach to take in the final Ruling is to determine whether the Australian distributor would be infringing the copyright of the owner, but for the rights granted (either documented or implied) by the copyright holder. This would also take into consideration the various defences under the Copyright Act to copyright infringement.

Any payment the Australian distributor makes to the copyright holder is for the software supplied or contractual services provided by the copyright holder. No payment is made for the exploitation of the underlying copyrights in the software.

The view expressed under Scenario 1 of the draft Ruling is that Operational Business Australia Pty Ltd (OBA) authorises end-users to make internal copies, which is a consequence of OBA having the right to authorise reproduction of the software. However, making internal copies of computer programs for normal use and study of the programs or backup are permitted acts under sections 47B and 47C of the Copyright Act.

Permitted acts are user rights and have to be differentiated from copyrights. These permitted acts are non-infringing and are a defence the user has against any allegation of infringement.

Where a particular act is a permitted act, the copyright owner does not have any exclusive right to the same. Accordingly, any payment for such permitted acts or to authorise those acts cannot be for the use of copyright.

ATO response

Use of, or the right to use, copyright is not determined by ascertaining whether the use would otherwise be an infringement of the copyright. Our view is that the term ‘copyright’ is a reference to any exclusive right of the copyright owner in a work to which Australian copyright law applies.

For example, as noted in paragraph 170 of the draft Ruling, it does not matter whether an act authorised would be an infringement of the copyright, nor if it was specifically excluded from constituting an infringement.

The right to authorise the doing of an exclusive right of a copyright owner is evidence of a use of, or grant of, copyright. It does not matter whether the act authorised would be an infringement of the copyright, nor if it was specifically excluded from constituting an infringement.

The exclusive rights of a copyright owner are not necessarily limited to those specified in section 31 of the Copyright Act. The exclusive rights of the owner of copyright are set out inclusively at paragraph 99 of the final Ruling and has regard to subsection 13(2) of the Copyright Act.

Outcome

No change

Issue 10 – cloud services and communication right

Paragraph or section of draft product

Paragraphs 142 to 155

Issue raised

The ATO’s position is too broad and appears to adopt a catch-all approach to treat software distribution models such as cloud-based models as involving both use of the ‘communication’ right and the ‘reproduction’ right.

Paragraphs 142 to 144 of the draft Ruling fail to recognise variations in the facts of SaaS models as in many cases there will not be a download of software, and there will not then be a communication for the purposes of the Copyright Act.

It is not typically the case that a communication of software occurs simply through end-user receipt of SaaS services. By contrast, when software is offered to end-users under a digital download model, it is more likely that a communication will occur (at the point when the software is itself transmitted to end-users for download on their device).

There is no basis under Australian copyright law to suggest that the reseller makes a 'joint' communication when it has no technical ability to do so.

Reference to paragraphs 147 and 149 of the draft Ruling to the decision in *Roadshow Films Pty Limited v iiNet Limited* [2011] FCAFC 23 (*Roadshow*) does not acknowledge that *Roadshow* involved the transmission and reconstruction of parts of a copyright work. In many SaaS models there is no actual transmission of source code nor object code to the end-user. *Roadshow* therefore does not support the position that an intermediary who does not decide the content uploaded to a website is also the maker of the communication of that content, where they only provide access of that content to an end-user.

There is no payment for the use of any copyright which subsists in the SaaS, by either the distributor or by the end-user. Distributors of SaaS solutions typically do not enter into a licence with end-users. Specifying terms of use or access alone does not equate to a licence or to determining the content of the underlying service or any communication in respect of that service.

The Commissioner is requested to provide further guidance regarding what 'control' the terms of the end-user licence agreement would need to exert for a distributor to be considered to be determining the content of the communication.

ATO response

We remain of the view that providing a cloud service may involve making software available online, even though the software would not necessarily be available for download by members the public.

Outcome

No change

Issue 11 – authorisation

Paragraph or section of draft product

Paragraphs 163 to 174

Issue raised

Paragraph 174 of the draft Ruling states:

> … this act of sublicensing will generally constitute the authorisation of an act that is the exclusive right of the copyright owner.

Generalised statements such as these will not be true for a significant number of taxpayers.

Paragraphs 163 to 174 of the draft Ruling do not recognise that authorisation in this context must be the authorisation of an act which is the right of the copyright owner.

The authorisation right has no application to an act done by the copyright owner, as they cannot infringe their own copyright. Any purported authorisation of such an act would not be an act comprised in the copyright. Further, the licensee would have no basis for preventing the copyright owner supplying the works, particularly where the distribution agreement is non-exclusive. There is therefore no 'use' of copyright.

It is incorrect for the draft Ruling to characterise authorisation as a separate, exclusive and independent right, equivalent to the core copyright rights of section 31 of the Copyright Act. The concept of 'authorisation' should be confined in its application of the infringement context in which it was originally introduced.

ATO response

We agree that software intermediation arrangements need to be considered on a case-by-case basis. Depending upon the facts, the performance of a software intermediator's contractual obligations may involve the use of one or more copyright rights, including by way of communication and authorisation.

We are of the view that authorisation of an exclusive act comprised in the copyright is itself an exclusive right of the copyright owner. Greater detail is provided in the final Ruling regarding authorisation of an act comprised in the copyright: see paragraphs 115 to 133.

We acknowledge that the leading cases on authorisation concern infringement actions. It is not clear how the courts would apply principles from those infringement cases to determine the scope of the authorisation right.

Outcome

No change

Issue 12 – publication right

Paragraph or section of draft product

Not applicable – relevant to document scope

Issue raised

The draft Ruling describes copyright rights by referring to the exclusive acts of a copyright owner in section 31 of Copyright Act, though inexplicably, it omits the right to publish from that list.

ATO response

The right to publish in subparagraph 31(1)(a)(ii) of the Copyright Act may be relevant in the context of software intermediation arrangements depending on specific facts and circumstances. Paragraph 99 of the final Ruling reflects this.

Outcome

Clarified

Issue 13 – commercial rental arrangement

Paragraph or section of draft product

Paragraphs 157 to 162

Issue raised

The Commissioner is requested to provide further guidance on the specific features of a software distribution arrangement which he considers may result in that arrangement constituting a commercial rental arrangement.

The typical delivery model for a SaaS solution does not have the necessary features to constitute a 'commercial rental arrangement' in respect of software under subsection 30A(2) of the Copyright Act.

The Australian distributor or reseller is not entering into a commercial rental arrangement because it is not returning the software to the IP owner and does not have any access to the software being provided.

Even if a commercial rental arrangement could arise in a SaaS or digital download scenario, it would be incorrect to characterise a distributor who merely resells the SaaS service or downloadable software as exercising the right to enter into a commercial rental arrangement, given only the supplier ‘makes [the SaaS or downloadable software] available’ to end-users in that scenario.

In Scenario 2, the draft Ruling rightly identifies that when a recurring subscription is payable by end-users for the use of the software and not an outright sale, there is a commercial rental arrangement with respect to the software.

Where the distributor has obtained the use of the rental right from the copyright owner, the consideration paid by the distributor is for the use of the rental right, which is one of the exclusive acts of the copyright owner under section 31 of the Copyright Act, and consequently, should be characterised as royalty.

ATO response

We think it is less likely that a ‘commercial rental arrangement’ will be found in the kinds of software intermediation arrangements contemplated. Accordingly, the discussion on commercial commercial rental arrangements has been removed in the final Ruling.

Outcome

Position amended

Issue 14 – access control technological protection measures

Paragraph or section of draft product

Paragraphs 23 to 41

Issue raised

In Scenarios 1 and 2 of the draft Ruling, it is specifically stated that the relevant software is subject to access control technological protection measures (ACTPMs), but it is not clear what the implications of this are and further guidance should be provided on this point.

In the draft Ruling, use of ACTPMs seems conflated with aspects of authorisation. Such measures may be implemented by overseas companies to suit the international market for the software. Where an Australian distributor has no standing to sue a person for circumventing such measures, it is not a right the Australian distributor has, nor is paying for.

It is incorrect to characterise the Copyright Act as protecting a ‘right of’ copyright owners to ‘control access’ to a work (as paragraph 131 of the draft Ruling suggests), such that a distributor’s act of granting access to a work via an ACTPM should constitute a relevant use of copyright.

Technological protection measures prevent piracy and unauthorised access to copyright works and these provisions of Australian copyright law provide copyright owners with a cause of action against persons who seek to circumvent such measures. These provisions do not constitute a separate monopoly 'right of access' to copyrighted works.

ATO response

Paragraphs 138 to 146 of the final Ruling clarifies the discussion of ACTPMs.

Outcome

Clarified

Issue 85 – 'other like property or right' to copyright

Paragraph or section of draft product

Paragraphs 58 to 60

Issue raised

Further clarity is required on what the Commissioner views as 'other like property or rights'.

The ATO is encouraged to limit the scope of the final Ruling to copyright only.

The Commissioner has taken a broad interpretation of the phrase 'other like property or right', citing *Seven Network Limited v Commissioner of Taxation* [2014] FCA 1411 (the first instance decision). This interpretation is not entirely supported by case law as it fails to address the meaning given to the phrase by the Full Court of the Federal Court on appeal (*Commissioner of Taxation v Seven Network Limited* [2016] FCAFC 70).

In its decision, the Full Court was clear that the phrase is to be taken in the context of the words preceding them and that '"Like right" must mean analogous rights – that is, rights of a similar nature' (*Commissioner of Taxation v Seven Network Limited* [2016] FCAFC 70 at [83]).

ATO response

We consider the position adopted in the Ruling to be consistent with the standard tax treaty definition of 'royalty'. The definition of 'royalty' covers more than use, or grant, of copyright and extends to the use of 'other like property or right'. This is consistent with case law.

We are of the view that the expression 'other like right' can extend the operation of a royalty to other categories of intellectual property so long as they are within the nature or class of intellectual property rights: see paragraphs 55 to 58 of the final Ruling.

Outcome

No change

Issue 16 – international copyright

Paragraph or section of draft product

Paragraphs 127 to 129

Issue raised

The message in paragraphs 127 to 129 of the draft Ruling is not clear about its intention to communicate in respect of the interaction between the Copyright Act, section 184 of the Copyrght Act and the *Copyright (International Protection) Regulations 1969*.

ATO response

We have simplified this content to signpost those Regulations: see paragraph 96 of the final Ruling.

Outcome

Clarified

Issue 17 – Australian domestic law interaction with double tax agreements and Organisation for Economic Co-operation and Development guidance

Paragraph or section of draft product

Not applicable – relevant to document scope

Issue raised

The draft Ruling represents a departure from previous practice, accepted industry approach and the Organisation for Economic Co-operation and Development (OECD) consensus expected to ensure stability and certainty in international tax. Australia was a part of the working group that introduced paragraph 14.4 of the OECD Commentary[1] and lodged no reservations.

ATO view of OECD Commentaries is too narrow

The draft Ruling is focused on the wording and potential limitations of paragraph 14.4 but does not appear to consider all relevant sections of the OECD Commentary including paragraphs 12, 13.1, 14 to 14.2, and 14.4, and 17 to 17.4.

The Commissioner's interpretation of paragraph 14.4 is unjustifiably narrow. It ignores the statement at paragraph 14.1 of the OECD Commentary that 'The method of transferring the computer program to the transferee is not relevant'. Electronic distribution models are to be treated the same, and any ancillary or incidental uses of copyright should be disregarded.

Because copyright is not defined in Australia's 'standard' tax treaties, the Commissioner takes the view that 'the term 'copyright' in this Ruling has the same meaning that it has under the Copyright Act for the purposes of the tax treaty and the domestic tax law definition of royalty'. This ignores changes in the OECD Commentary over time.

The draft Ruling assumes the current OECD Commentary applies to all treaties, yet Australian courts have determined that the version of OECD Commentary at the time the particular treaty was signed be applied.

The absence of a *de minimis* principle of 'simple use' or 'incidental use' in the draft Ruling should be explained with a discussion of its history and role including in the 1992 OECD paper 'The Tax Treatment of Software'[2], and inference from paragraphs 14, 17.2 and 17.3 of the OECD Commentary.

The ATO's interpretation in paragraph 185 of the draft Ruling suggests the OECD guidance can only be relied upon where the software is distributed with 'no modifications', imposing a restriction not found in the OECD Commentary itself. This narrow approach risks substantially vitiating paragraph 14.4 in the modern digital economy, where electronic delivery and minor configuration changes are commonplace.

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[1] OECD (2019) *Model Tax Convention on Income and on Capital 2017 (Full Version)*, OECD Publishing, Paris https://doi.org/10.1787/g2g972ee-en.

[2] See OECD (2012) *Model Tax Convention on Income and on Capital 2010 (Full Version)*, Vol. II, OECD Publishing, Paris, https://doi.org/10.1787/9789264175181-en.

Copyright rights are broader than the right to reproduce or modify

A contrary view is that any inference in paragraph 14.4 that payments will only be royalties where the rights to reproduce or modify the software are granted is questionable, as the national copyright laws of many countries include the right to publish as a copyright right.

The United Nations Commentary[3] states that distributor payments are viewed by some members to be in the nature of royalties as the right to distribute is a use of a copyright. This is a valuable economic right of the copyright owner which exists independently of other rights in the copyright.

ATO response

The relevance of the OECD Model Tax Convention Commentary (OECD Commentary) on Article 12 as explained at paragraphs 61 to 70 of the draft Ruling is maintained in the final Ruling (see paragraphs 78 to 86).

The example in paragraph 14.4 of the OECD Commentary on Article 12 depends upon the facts of an arrangement and the application of relevant domestic copyright law of the country from which the payment was made.

The facts contained in the example in paragraph 14.4 of the OECD Commentary on Article 12 place a significant qualification and limitation on its application. The conclusion that the payments are not a royalty is a consequence of the facts that:

- a distribution intermediary is granted the right to distribute 'copies' of the program, that is, copies of the programs are being acquired (but not made) and distributed by the intermediary, rather than a distribution model involving the grant of access to software (such as through a 'cloud')
- the distribution intermediary is not granted the right to reproduce the program, that is, it can be inferred that the manner and form in which the software is distributed does not require reproduction of the program by the intermediary
- the copyright rights acquired by the distribution intermediary are limited to those necessary to distribute copies of the software program
- the distribution intermediary only pays for the acquisition of the software copies and not to exploit any copyright rights in the software.

This is said to lead to the conclusion that the payments by the distribution intermediary are not for the use of, or the right to use, any copyright rights in the software.

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[3] United Nations (2021) *United Nations Model Double Taxation Convention between Developed and Developing Countries*, Commentary on Article 12 (Royalties), https://financing.desa.un.org/document/un-model-double-taxation-convention-between-developed-and-developing-countries-2021, p370.

If these facts are present in an arrangement, we agree that the characterisation of the payment does not differ if the software copies are delivered on tangible media or distributed electronically.

However, these facts are usually not present in modern software intermediation arrangements. It is necessary to analyse carefully the nature of the rights granted or used by the software intermediary because this will affect the characterisation of a payment. We think this is consistent with paragraphs 10.1 and 17.4 of the OECD Commentary.

The question of whether there is a grant or use of copyright (including any other like right) under software intermediation arrangements covered by the final Ruling depends upon the relevant domestic law meaning because copyright is an undefined terms.

Outcome

No change

Issue 18 – other intellectual property rights used by distributors

Paragraph or section of draft product

Paragraphs 14 and 56

Issue raised

The ATO assumes that Australian distributors would typically have access to other IP rights as part of their arrangements which would need to be examined on a case-by-case basis.

The final Ruling needs to clearly set out whether the inclusions in paragraph 14 of the draft Ruling (which apply to ‘IP’ as opposed to copyright or copyright in relation to software) will be applied by the Commissioner in characterising payments involving other types of copyright (such as sound recordings or other literary works) or other types of intellectual property.

Paragraph 14 of the draft Ruling opens by referring to ‘The following payments’ but the examples given are not of ‘payments’ as such, but the rights given as consideration for the payments. Suggest replacing the opening words in paragraph 14 of the draft Ruling with ‘Payments for the following’.

In subparagraph 14(c) of the draft Ruling, the first line should read ‘the supply of know-how referred to’. The relevant ‘industrial commercial knowledge or information’ in the treaty is not required to be ‘in relation to an IP right’. If it were in relation to an IP right, it might also fall under subparagraph 14(d).

In subparagraph 14(d) of the draft Ruling, the second occurrence of the word 'supply' is ambiguous as it is not defined in the Ruling. 'IP rights' might be clearer.

Paragraph 56 of the draft Ruling appears to use the expression 'IP right' inconsistently and appears to refer to 2 separate categories, 'IP rights' and 'other like property or rights'.

ATO response

Paragraphs 14 and 56 of the draft Ruling have been clarified in the final Ruling (paragraphs 16 and paragraph 53 respectively).

The definition of 'Intellectual property rights or IP rights' contained in the final Ruling (at paragraph 9) is broader than 'copyright' and aligns with the elements contained in paragraph 3(a) of the 'standard tax treaty definition'. Nonetheless, the scope of the Ruling is on the characterisation of payments made under a software intermediation arrangement, rather than an arrangement that does not involve software.

Outcome

Clarified

Issue 19 – nature of software distributor or intermediary

Paragraph or section of draft product

Not applicable – relevant to document application

Issue raised

The terms of an agreement should be interpreted in their commercial context. In most software arrangements, any rights conferred are minimal and do not amount to copyright use that would otherwise constitute infringement.

Where the true object of the agreement is to confer copyright rights, the provider typically grants those rights without any obligation to supply products or services. Conversely, in distributor transactions, the object is to acquire goods or services, and the supplier must undertake substantive commercial activities, including development and delivery. This distinction in economic activity highlights the difference between a simple copyright licensor and a supplier of digital goods or services.

Is the concept of simple use or incidental use still applicable to end-users, and if so, why isn't the same treatment afforded to distributors?

Why is it that distributors (intermediaries) who may have some additional IP rights beyond simple use for distribution purposes are subject to all payments being royalties compared to no royalty payments by end-users?

ATO response

The rights granted to, or used by, a software intermediary are unlikely to be same as those granted to or used by an end-user, and may include copyright rights, for reasons explained in the Ruling.

In our view, it is commonly the case in a software intermediation arrangement that any IP rights granted are neither separate nor severable from any other rights granted. That is, in taking the whole of the agreement into account, the distribution agreements cannot be performed without use of the IP rights granted. In a situation where the payment is undissectable, the entirety of the consideration will be characterised as a royalty.

Outcome

No change

Issue 20 – examples

Paragraph or section of draft product

Scenarios 1, 2 and 3

Issue raised

The examples in the draft Ruling demonstrate that such matters are extremely fact dependent and that the facts of 2 taxpayers in the impacted industries are rarely identical. As a result, the Scenarios would be better published as some other form of guidance, for example, a practical compliance guideline.

The final Ruling should provide additional examples that consider variations in SaaS business models.

ATO response

The final Ruling contains an additional example (Example 3), which illustrates the application of the principles of when authorisation of an exclusive act comprised in copyright may be exercised. In addition, we have published PCG 2026/D4 to provide guidance about when the ATO may not have cause to apply compliance resources to review a software intermediation arrangement.

Outcome

Position amended

Issue 21 – scenarios 1 and 2

Paragraph or section of draft product

Scenarios 1 and 2

Issue raised

Scenario 1 and Scenario 2 of the draft Ruling do not aid in articulating points of principle given the specificity of the examples chosen. The facts included do not sufficiently support the conclusions reached.

Neither scenario involves a SaaS platform where software is hosted on a server that receives input data via the internet, processes it as requested, and returns results to the user without providing any source or object code. In such cases, no copyright is exercised, and no communication of copyright works occurs to the end-user or the software distributor.

In Scenario 1, any 'power to prevent' conferred to OBA by entering into an end-user licence agreement would be, similar to the High Court decision in *Roadshow Films Pty Ltd v iiNet Ltd* [2012] HCA 16, an indirect contractual power – OBA does not have practical control over the means by which Ireland Enterprises Limited (IEL) communicated software to the end-user.

In Scenario 2, it is ForeignCo (not AusCo) that determines the content of the communication and exercises that communication right. There is not authorisation or communication by AusCo that should justify characterising any payments made by AusCo to ForeignCo as royalties.

ATO response

We consider that, in broad terms, Scenarios 1 and 2 (Examples 1 and 2 in the final Ruling) reflect 2 key approaches to software intermediation models. One is where the local software intermediator is the entity granting the end-user licence (Example 1), and another is where the local software intermediary enters into a contract of sale with an end-user, where the end-user licence itself is granted by an offshore IP owner or licensor (Example 2).

Example 1 outlines 3 distribution mechanisms: electronic download, cloud-based access, and physical copies. While SaaS models may differ in some respects, such as software being accessed remotely without any transfer of code, we think Example 1 still offers useful guidance about our approach on how rights granted and exercised in software intermediation arrangements inform the characterisation of payments.

In both examples, the IP rights required to perform the agreed activities inform the royalty characterisation.

Outcome

Clarified

Issue 22 – scenario 3 – reasonable method of apportionment

Paragraph or section of draft product

Scenario 3

Issue raised

Scenario 3 of the draft Ruling attempts to demonstrate an example of a distribution arrangement with a combination of services. This example lacks detail and sufficient rationale justifying its position.

Scenario 3 should be updated in the final Ruling, as it would be more helpful to taxpayers where it instead considered an arrangement involving only non-physical products.

Scenario 3 does not explain why the ATO considers the majority of consideration attributable to the IP rights; any example similar would need to explain the circumstances under which apportionment is required and a better factual statement as to how apportionment shares are determined.

ATO response

Scenario 3 from the draft Ruling has not been retained in the final Ruling. We consider that adequate guidance is provided on this matter in PCG 2026/D4, which outlines our compliance approach to identifying whether any part of a cross-border payment made to a non-resident is a royalty and subject to withholding tax.

Outcome

Position amended

Issue 23 – lack of apportionment guidelines

Paragraph or section of draft product

Not applicable – relevant to document usability

Issue raised

The draft Ruling considers the whole of a payment can constitute a royalty in some cases. But in most cases, the apportionment of the software distributor's payment to the use of the copyright or other IP would be a low percentage and would rarely, if ever, be 100% of the payment.

No guidance is provided by the ATO for apportionment and businesses are left with significant uncertainty.

The appropriate approach to apportionment involves valuing the particular rights granted and apportioning based on those values.

It is unclear whether the basis of apportionment is a 'market valuation' exercise (as opposed to some other exercise which involves determining relative value) and the basis of the ATO's conclusion in Scenario 3 of the draft Ruling that the IP rights are the more valuable rights is also unclear.

Further guidance and examples should be provided in the final Ruling with methodologies that might be used to determine a fair and reasonable apportionment and where no apportionment is required.

ATO response

The applicability and suitability of any apportionment method depends on first determining the true character of the payment. Apportionment will not be required in all cases. In our view, software intermediation arrangements commonly grant IP rights that are neither separate nor severable from other rights. Taking the agreement as a whole, the commercial bargain cannot be performed without using the granted IP rights. In such cases, the entire consideration is characterised as a royalty.

Scenario 3 of the draft Ruling, regarding distribution of physical copies of computer games, has not been retained in the final Ruling, given the publication of PCG 2026/D4. PCG 2026/D4 emphasises that determining the appropriate apportionment methodology to ascertain a reasonable royalty will depend on the particular facts and circumstances of the arrangement. While it is not within the scope of PCG 2026/D4 to prescribe any particular approach, the draft Guideline sets out, under the green and yellow zones, our risk assessment approach as to when we will further examine the quantum of your royalty.

Outcome

Clarified

Issue 24 – burden of proof

Paragraph or section of draft product

Not applicable – relevant to ruling analysis

Issue raised

Under the draft Ruling, it is left to the taxpayer to disprove that the entire payment is a royalty. This significantly increases the burden on taxpayers, even where the payment is not considered a royalty under the draft Ruling. There is an onerous burden on taxpayers to prove that IP rights are separable from other valuable distribution rights.

ATO response

Whether a software intermediary's entire payment constitutes a royalty depends on its proper characterisation. That characterisation, and any need for apportionment, turns on what the payment is objectively for. This depends upon the particular facts and circumstances, with the terms of the agreement being the starting point.

The Ruling should be read in conjunction with PCG 2026/D4.

Outcome

No change

Issue 25 – potential disputes

Paragraph or section of draft product

Not applicable – relevant to document analysis and commencement

Issue raised

The proposed apportionment approach in the draft Ruling and applying the final Ruling retrospectively may lead to an increase in tax disputes which will likely take many years to resolve.

ATO response

The Ruling seeks to clarify our view of the definition of royalties having regard to Australian domestic law and sets out the potential copyright issues that we have seen arise in software intermediation arrangements. This is intended to provide certainty about the tax consequences of their arrangements.

Ultimately, clarification may be obtained through the courts.

Outcome

No change

Issue 26 – meaning of 'sufficiently connected with' in relation to undissected amounts paid

Paragraph or section of draft product

Paragraph 18

Issue raised

When does the whole payment amount to a royalty where not all the things paid for are royalties?

It seems, in paragraph 18 of the draft Ruling, the ATO is asserting a new test to require a sufficient connection, rather than inseparability of the bundle of things paid for, with an undissected sum in an attempt to characterise the whole of the sum as a 'royalty' where only some of the things paid for meet the definition of 'royalty'. If that is the case, it does not appear any legislative or case law basis has been provided to substantiate this new test.

ATO response

Rather than establishing a fixed rule, paragraph 18 of the draft Ruling indicates that where a payment covers multiple elements (each relating to aspects of the royalty definition) and no clear basis for separation is evident, it is reasonable to initially treat the whole amount as a royalty unless evidence suggests otherwise. It does not mandate that all such payments will always be characterised as royalties.

This is an application of longstanding principles of apportionment that depends on the facts. *IBM Corporation* is one example of this. The final Ruling refers to apportionment principles at paragraph 17.

Outcome

No change

Issue 27 – consideration for

Paragraph or section of draft product

Paragraph 16

Issue raised

We agree with paragraph 16 of the draft Ruling – '"consideration" is what moves the payment and is something of value given in exchange for it'. However, the ATO analysis is inaccurate – what moves the payment for resale of tangible products are the products, the same should be the case for digital software.

Title does not pass in cases of sales of digital content, but that fact does not prevent a conclusion that sales of copies of content are equivalent for tax purposes to sales of other copyrighted articles in tangible form. Similarly, for the contracting and subcontracting of services, the fact that no title to goods passes is not relevant.

ATO response

The final Ruling reflects the High Court decision in *PepsiCo*, particularly in relation to the meaning of the terms 'consideration' and 'for' in identifying the 'purpose, basis or condition' of the payment. This is ultimately a question of fact, and the agreement between the parties is important to the characterisation of the payment.

Outcome

Clarified

Issue 28 – goods and services tax concepts of supply and 'consideration for'

Paragraph or section of draft product

Paragraphs 89 to 102

Issue raised

Principles from the goods and services tax (GST) law are not relevant to the assessment of ‘consideration for’, and applying GST concepts to assist in characterising the arrangement is misguided, particularly when the history and context of the royalty definition is considered.

The supply from the distributor to its customer is more accurately characterised as the supply of a promise to deliver fully developed SaaS service. In a SaaS context, although the specific facts must be considered in each case, a distributor is generally paying the owner or licensee of the copyright (as the case may be) for fully developed services on the expectation that their customer will obtain end-user use of the services. There is no payment for the use of any copyright which subsists in the SaaS, by either the distributor or by the end-user (that is, the end customer). A customer is paying for a fully developed copyrighted article, not any access to the copyright.

Paragraph 89 of the draft Ruling does not acknowledge the significant factual variation that exists in ‘distribution’ arrangements.

The precise consequence of paragraphs 90 to 102 of the draft Ruling is not spelled out. There seems to be an implication that the distributor may somehow be taken to have done acts reserved to (and in these cases actually done by) the copyright holder (the licensor).

ATO response

The Ruling does not rely on GST cases for what ‘consideration for’ means, given the High Court decision in *PepsiCo*.

Outcome

Clarified

Issue 29 – application of *IBM Corporation* and *PepsiCo*

Paragraph or section of draft product

Paragraphs 20 to 22 and 103 to 117

Issue raised

The draft Ruling canvasses the potential for apportionment but does not set out any principle from, or the relevance of, *IBM Corporation*.

Conclusions put forward in paragraphs 20 to 22 and 103 to 117 of the draft Ruling are not explicit in the decision in *IBM Corporation* regarding apportionment. The *IBM Corporation* judgment means that in cases where the consideration is not simply and expressly for the use of, or grant of, IP rights, apportionment remains appropriate.

Paragraph 74 of the draft Ruling would seem to be based on the decision in *PepsiCo* and as such the final Ruling should be further delayed pending the *PepsiCo* appeal and the likely proceedings in relation to Coca Cola.

ATO response

The Ruling reflects the High Court decision in *PepsiCo*, which has provided some clarity in the law. We will review this Ruling if a later decision affects those principles.

The *IBM Corporation* decision provides that the whole agreement is to be taken into account in characterising the payment. The language of the agreement is important in establishing what the payments were for; we think it is consistent with authority that any implied terms must also be taken into account. The focus of the agreement on intellectual property rights compared to any standalone distribution rights indicated that the payment was for IP rights.

IBM Corporation is still good law, and was not overruled by the High Court in *PepsiCo*. *IBM Corporation* is an example of the application of longstanding principles of apportionment. The final Ruling refers to apportionment principles at paragraph 17.

Outcome

Clarified

Issue 30 – alignment of ATO view with other competent authorities

Paragraph or section of draft product

Not applicable – relevant to document scope

Issue raised

The Commissioner's unilateral approach has the potential for material disputes (especially if there are no foreign tax credit entitlements) and may result in material compliance and financial burden for taxpayers requiring mutual agreement procedures to resolve double taxation.

The draft Ruling conflicts with that of major trading partners, including the United States of America (US). The US software regulations codify a copyright rights-based analysis that is substantially similar to the analysis described in the OECD Commentary. The United States Treasury also clarified that the U.S. software regulations are based on the principle that copyright law should be a factor in classifying transactions for tax purposes but should not be determinative.

As the US Internal Revenue Service does not consider the payments received by IP owners or licensors to be royalties, there will likely be double taxation (as foreign tax credits not available to apply as a result).

ATO response

We are unaware of specific circumstances of a denial of foreign tax credits or double taxation in practice. We note that the 1998 US Regulations on Classification of Certain Transactions Involving Computer Programs[4], while guided by copyright law principles in determining whether a copyright right or copyrighted article has been transferred, intentionally departed from a strict reliance on copyright law.

Clarification of law via the Australian court processes is an option available to obtain certainty on the correctness of our view. One benefit may be ascertaining the correct application of Australian law before any mutual agreement procedure.

Outcome

No change

Issue 31 – economic cost of ATO position

Paragraph or section of draft product

Not applicable – relevant to document scope

Issue raised

Other countries will follow suit and the collective tax on the global profits will make it significantly costlier to run a software distribution business.

Royalty characterisation, as outlined in the draft Ruling, is likely to increase the costs of Australian businesses and ultimately Australian customers. Australian businesses operating as offshore vendors instead would seek contractual gross-ups of any royalty withholding tax payable which would impact third-party resellers, distributors and integrators of offshore vendor software.

The draft Ruling leaves gaps for uncertainty in relation to the supply and use of digital technology in the Australian economy and can potentially jeopardise the competitiveness of Australian businesses.

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[4] Internal Revenue Service (1998) *Classification of Certain Transactions Involving Computer Programs*, *Federal Register*, 63(191), pp. 52971-52984, https://www.federalregister.gov/documents/1998/10/02/98-26475/classification-of-certain-transactions-involving-computer-programs

Australian distributors are likely to relocate offshore, there will be an increase in the cost of software and related services for consumers in Australia, and there will be limitations on access to valuable technical intellectual property to Australian industry.

ATO response

The Ruling contains our view on the characterisation of payments made under a 'software intermediation arrangement'. Broader economic considerations, including potential global tax developments, impacts on competitiveness, and commercial decisions by software intermediaries, are questions for policymakers and outside the scope of this Ruling.

Outcome

No change

Issue 32 9– penalties and interest

Paragraph or section of draft product

Not applicable – relevant to document scope

Issue raised

The application of penalties and interest ultimately turns on the specific facts and circumstances, however it would be helpful for the final Ruling (or a separate product) to include guiding principles or relevant factors on this question.

The Commissioner's approach to penalties and interest should also reflect the uncertainty in this complex area of tax law that has been compounded by the delay of the Commissioner in providing finalised guidance.

ATO response

Application of administrative penalties for failure to withhold and any general interest charge that may accrue is outside the scope of this Ruling, and is dependent on the unique facts and circumstances of each case.

The application or remission of penalties and general interest charge will be done in accordance with the legislation and taking due account of ATO policy.

Outcome

No change

Issue 33 – tangible goods

Paragraph or section of draft product

Not applicable – relevant to document scope

Issue raised

Construing any tangible technology product (which almost necessarily will have a software element) as the equivalent of a CD-ROM or USB memory stick unnecessarily invites the potential for widespread uncertainty for taxpayers.

The distribution of tangible products other than pure storage media or computing devices that host software that is also sold independently of such devices should be excluded from the scope of the final Ruling.

ATO response

The Ruling contains our view on the characterisation of payments made under a 'software intermediation arrangement'. We maintain the view that some payments for tangible goods with embedded software can give rise to a royalty: see Part 4 of the Ruling.

The mischaracterisation risk in relation to distribution arrangements involving tangible goods is covered by Taxpayer Alert TA 2018/2 *Mischaracterisation of activities or payments in connection with intangible assets*.

Outcome

No change

Issue 34 – guidance for taxpayers who seek to restructure their arrangements

Paragraph or section of draft product

Not applicable – relevant to document commencement

Issue raised

Taxpayers should have a reasonable period to restructure arrangements impacted by the draft Ruling, provided those arrangements were not reasonably subject to royalty withholding tax under TR 93/12, OECD Commentary, or prevailing practice.

The reasonable period should reflect the time commercially required to implement a restructure, including amending legal agreements, accounting systems, billing processes, and software delivery mechanisms.

The Commissioner should also confirm that anti-avoidance provisions will not apply to tax benefits arising solely from this change. Taxpayers who introduce artificial and convoluted schemes to avoid royalty withholding tax in their new arrangements should not be afforded this protection. If these protections are not provided, the Commissioner should issue guidance on the ATO's approach to taxpayers seeking to restructure to avoid royalty withholding tax.

ATO response

The Ruling applies to periods before and after the date of publication.

The application of the general anti-avoidance provisions to arrangements that we have not seen is beyond the scope of this Ruling.

Outcome

No change

Date of publication: 4 September 2026