



# ***PCG 2025/D4 - Low-risk payments relating to software arrangements - ATO compliance approach***

 This cover sheet is provided for information only. It does not form part of *PCG 2025/D4 - Low-risk payments relating to software arrangements - ATO compliance approach*

 For information about the status of this draft Guideline, see item [4168] on our [Advice under development program](#).



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## **Draft Practical Compliance Guideline**

# **Low-risk payments relating to software arrangements – ATO compliance approach**

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### **📌 Relying on this draft Guideline**

This Practical Compliance Guideline is a draft for consultation purposes only. When the final Guideline issues, it will have the following preamble:

*This Practical Compliance Guideline sets out a practical administration approach to assist taxpayers in complying with relevant tax laws. Provided you follow this Guideline in good faith, the Commissioner will administer the law in accordance with this approach.*

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| <b>Table of Contents</b>                  | <b>Paragraph</b> |
|---|------------------|
| What this draft Guideline is about        | 1                |
| Background                                | 3                |
| <i>Current litigation</i>                 | 5                |
| <b>Date of effect</b>                     | <b>7</b>         |
| Structure of this Guideline               | 8                |
| <b>Our compliance approach</b>            | <b>10</b>        |
| <i>Restructures</i>                       | 16               |
| Our risk assessment approach              | 18               |
| Glossary                                  | 19               |
| <b>SCHEDULE 1 – software arrangements</b> | <b>20</b>        |
| <b>Your comments</b>                      | <b>49</b>        |

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### **What this draft Guideline is about**

1. This draft Guideline<sup>1</sup> provides certainty about when the ATO will not review software arrangements to determine whether any part of a cross-border payment made to a non-resident is a royalty and subject to withholding tax (royalty risk).
2. This Guideline provides clarity on arrangements that will not attract our attention, thereby providing confidence to, and avoiding unnecessary compliance costs for, in-scope businesses.

### **Background**

3. Draft Taxation Ruling TR 2024/D1 *Income tax: royalties – character of payments in respect of software and intellectual property rights* sets out our interpretative position on

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<sup>1</sup> For readability, all further references to ‘this Guideline’ refer to the Guideline as it will read when finalised.

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when an amount paid under a software arrangement is a royalty and subject to royalty withholding tax. This Guideline should be read together with TR 2024/D1.

4. At a later stage, we may consider expanding this Guideline to publish our broader compliance approach (that is, beyond the low risk zone). We will consult with you if we decide to do so.

### **Current litigation**

5. Finalisation of TR 2024/D1 has been deferred pending the decision of the High Court of the appeal from *PepsiCo, Inc. v Commissioner of Taxation* [2024] FCAFC 86 (*PepsiCo*). Neither TR 2024/D1 nor this Guideline will impact the view of an Australian court. We must apply the law in accordance with Federal or High Court authorities.

6. Following the High Court's decision of the *PepsiCo* appeal, we will review and, as necessary, update TR 2024/D1. If the decision results in material changes to our view, we will undertake further consultation about those changes.

### **Date of effect**

7. When finalised, this draft Guideline is proposed to apply to arrangements entered into both before and after its date of issue.

### **Structure of this Guideline**

8. This Guideline is structured as follows:

- main body – which sets out our compliance approach for royalty risk
- glossary – which provides definitions of terms used in this Guideline
- Schedule 1 – software arrangements – which sets out the risk assessment framework in relation to software.

9. Additional schedules may be included as part of this Guideline in the future.

### **Our compliance approach**

10. This framework allows you to self-assess the compliance risk relating to whether a cross-border payment you make to a non-resident relating to software is a royalty subject to Australian tax.

11. Where no portion of a cross-border payment is expressly stated to be a royalty by the instrument under which it is paid (or, if there is no instrument), that payment is referred to as an 'undissected payment' for the purposes of this Guideline.

12. The risk framework in this Guideline is for risk assessment purposes only. This Guideline does not replace, alter or affect the application of the law. You do not need our input or sign off on your self-assessed risk rating. However, you may be asked to tell us if you have self-assessed your risk rating and what your risk rating is.

13. We will review the use and application of this Guideline over time and may update it to reflect changes to our risk tolerance or add further schedules relating to other kinds of arrangements.

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Table 1: Risk zones

| Risk zone | Description   |
|-----------|---|
| White     | Further risk assessment not required.   |
| Green     | We will not review your arrangement, other than to verify that you meet the requirements of the green zone. |

14. If your arrangement is in the white zone or green zone, we will not have cause to apply our resources to further review it with respect to royalty risk, other than to verify your self-assessment under this Guideline.

15. We may examine your arrangements where you have not self-assessed your risk zone or are unable to provide evidence to explain your self-assessment against our risk assessment framework, regardless of your self-assessed risk zone.

### **Restructures**

16. Regardless of the outcome under the risk assessment framework, if there has been a change to or restructure of your agreements resulting in a reduction or avoidance of Australian royalty withholding tax, we may have cause to apply compliance resources to review your arrangement.

17. Other provisions, including but not limited to Subdivisions 815-B and 815-C of the *Income Tax Assessment Act 1997* and the general anti-avoidance rules in Part IVA of the *Income Tax Assessment Act 1936* (ITAA 1936), may also be relevant. For example, a restructure by a multinational group so that Australian customers contract with an offshore subsidiary (even though activities in connection with the sale continue to be undertaken by an Australian subsidiary) may be a scheme to which Part IVA, including by way of section 177DA of the ITAA 1936, applies.

### **Our risk assessment approach**

18. Our risk assessment framework includes an assessment of your royalty risk based on the risk indicators set out in the Schedule to this Guideline.

### **Glossary**

19. In this Guideline:

- ‘Royalty’ refers to the definition of ‘royalty’ in paragraph 6(1)(a) of the ITAA 1936.
- ‘Intellectual property’ (IP) refers to creations of the mind such as inventions, literary and artistic works, designs, and symbols, names and images used in commerce.<sup>2</sup>
- ‘IP rights’ include (but is not limited to) the use of, or the right to use any copyright, patent, design, model, plan, secret formula or process, trademark, or other like property or right.

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<sup>2</sup> World Intellectual Property Organization (2020), [What is Intellectual Property?](#) [website], accessed 1 May 2025.

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- 'Offshore supplier' has the meaning described in paragraph 22 of this Guideline.
- 'Software' refers to the meaning as defined in TR 2024/D1.
- 'Specified jurisdiction' takes its definition from 'specified countries' in the instructions to the International dealings schedule for the relevant income year.
- 'Undissected payment' has the meaning described in paragraph 11 of this Guideline.
- 'You' or 'your' refers to the payer who makes an undissected payment.
- References to a payment should be taken to include a reference to a credit or payment in any other form, for example, where an amount is reinvested, accumulated, capitalised, carried to any reserve, sinking fund or insurance fund however designated, or otherwise dealt with on behalf of the person who is beneficially entitled to the amount or as the person directs.

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**Commissioner of Taxation**

6 August 2025

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## **SCHEDULE 1 – software arrangements**

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| <b>Table of Contents</b>  | <b>Paragraph</b> |
|---|------------------|
| Scope of this Schedule  | 20               |
| <i>White zone</i>   | 25               |
| <i>Green zone</i>   | 27               |
| <u>Example 1 – internet security software solely acquired for private or domestic use</u> | 28               |
| <u>Example 2 – general administrative software ancillary to a business in Australia</u>   | 32               |
| <u>Example 3 – software copies stored on physical media acquired by a retailer</u>        | 41               |
| <u>Example 4 – washing machines with embedded software</u>                                | 45               |

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### **Scope of this Schedule**

20. This Schedule relates to payments made in relation to software and should be read together with TR 2024/D1, which sets out our interpretative position on when an amount paid under a software arrangement is subject to royalty withholding tax. If we review your arrangement to consider whether an amount should have been withheld from a payment, our position will be in accordance with our views set out in TR 2024/D1.

21. In practice, characterisation of a payment will need to have regard to the context of the arrangement. Payments may be royalties not only because they are for the use or right to use software copyright, but also other IP (or intangible assets) such as patents, trademarks, designs, technical or commercial information, or services which are ancillary to the use or enjoyment of the IP.

22. This Schedule applies to payments you make under an arrangement that involves the purchase or acquisition of software (including rights to software) from a non-resident or its associate (offshore supplier) who holds the IP rights (such as copyright) relating to that software.

23. Table 2 of this Guideline summarises the risk zones for payments made to an offshore supplier.

Table 2: Risk zones

| <b>Risk zone</b> | <b>Description</b>   |
|------------------|--|
| White            | Further risk assessment not required.  |
| Green            | Arrangements where your undissected payment meets any of the criteria at paragraph 27 of this Guideline. |

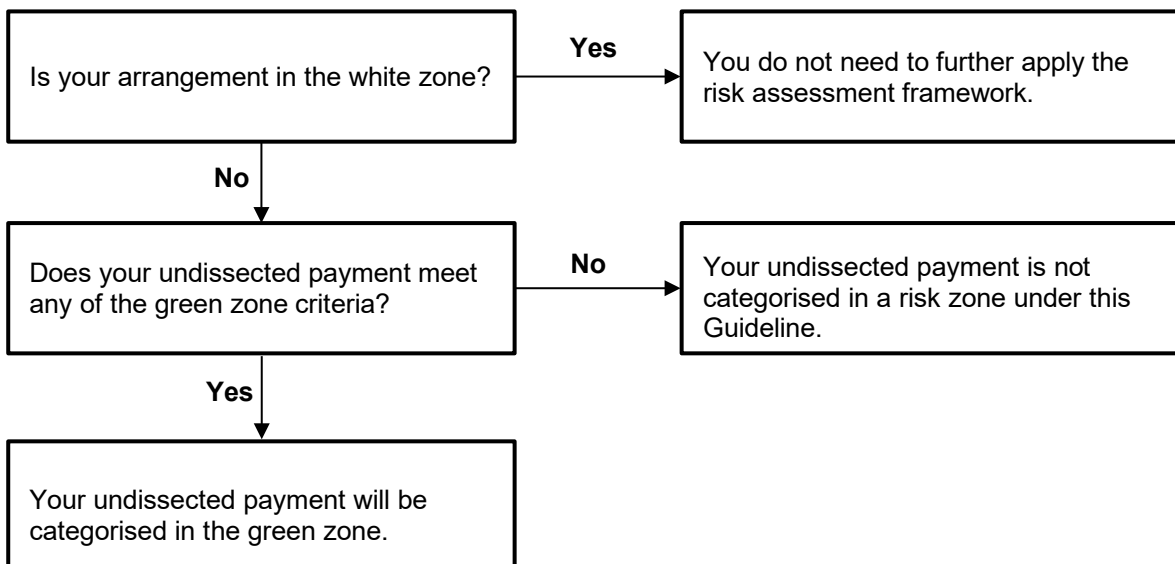
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24. Diagram 1 of this Guideline provides an overview of the risk assessment framework.

Diagram 1: Roadmap to the risk assessment framework.



### **White zone**

25. Your arrangement is in the white zone if any of the following apply to you for an income year:

- There is a settlement agreement or advance pricing arrangement (APA) between you and the ATO, where the terms of the settlement or APA expressly cover the Australian withholding tax outcomes related to the arrangement for the current year, and you have met the conditions of the agreement.
- A court or tribunal has decided (in a proceeding to which you were a party) that a payment under your arrangement does or does not constitute a royalty.
- The income year was subject of a review or audit of the arrangement and we provided you with a 'low risk' rating<sup>3</sup> (or a 'high assurance' rating as part of a justified trust review) in relation to the royalty risk of the arrangement.

26. This is provided there has not been a material change in the available facts and evidence in relation to the arrangement since the time of the settlement agreement, APA, court decision, review or audit. Where information previously provided to us or a court was materially different or incomplete, this condition will not be satisfied.

### **Green zone**

27. Your undissected payment is in the green zone if it is paid only in relation to the acquisition of:

- software acquired solely for private or domestic use

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<sup>3</sup> Including a 'no further action' outcome based on a finding of low risk.

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- software which is
  - installed and used in the course of your own business
  - generally available to the public from other sources and is not substantially customised, and
  - not further sold, licensed or otherwise exploited as a primary object of your business
- finished tangible goods of which software is an inherent or practically inseparable part, the software is to enable the tangible goods to perform their intended function, and the goods are acquired for resale to retail customers, or
- software copies stored on physical media in the course of a business of reselling the software copies and you and your associates do not require or have the rights to use offshore IP (for example, the right to sublicense any IP).

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**Example 1 – internet security software solely acquired for private or domestic use**

28. Sarah wants to enhance her online security and, after researching various internet security software options, decides that she wants a subscription for internet security software from AntiVirus Co.

29. AntiVirus Co is a provider based in a foreign country and specialises in developing internet security software to detect and neutralise computer viruses.

30. Sarah selects a one-year subscription plan on AntiVirus Co's website, enters her payment details, downloads a copy of the software and follows the easy setup instructions to install the internet security software onto her personal computer.

31. For the purposes of this Guideline, the payment by Sarah to AntiVirus Co is categorised in the green zone as the software acquired is solely for her private or domestic use.

**Example 2 – general administrative software ancillary to a business in Australia**

32. EducationCo Australia provides education services to Australian customers.

33. EducationCo Australia has an agreement with EducationForCo to obtain access to a comprehensive suite of cloud-based productivity applications which are licensed by EducationForCo from an unrelated offshore global software provider which develops software that is made generally available to the public.

34. These applications include:

- productivity applications used to create documents and spreadsheets
- project management tools (for production scheduling and resource allocation)
- communication platforms (email, messaging, video conferencing)
- enterprise resource planning systems (to manage inventory, finance, and procurement)

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- *customer relationship management tools (to handle sales and customer interactions).*

35. *EducationCo Australia cannot modify the source code in the software but is permitted by the global software vendor to configure and customise certain features of the cloud applications to fit its unique business needs, within certain constraints. For instance, EducationCo Australia customises the reporting and dashboards within the customer relationship management to display key performance indicators. EducationCo Australia also configures the security roles and access permissions across staff to vary levels of access based on an employee's role.*

36. *EducationCo Australia may work closely with the Software as a Service (SaaS) provider or approved third-party vendors to ensure these configurations align with both their operational needs and the cloud provider's software limitations.*

37. *EducationCo Australia provides access to these cloud-based applications to all staff across its Australian subsidiaries.*

38. *The cloud services agreement places a number of restrictions on EducationCo Australia's use of the software applications. EducationCo Australia is not permitted to disclose its account credentials to third parties or allow the applications to be used by more than 300 devices. EducationCo Australia can pay an additional amount to add more devices to the user base.*

39. *For the purposes of this Guideline, the payment by EducationCo Australia to EducationForCo is categorised in the green zone as the software is used in the course of its own business (productivity applications for EducationCo Australia staff use), is generally available to the public from other sources and is not substantially customised, and is not further sold, licensed or otherwise exploited as a primary object of its business.*

40. *The categorisation of EducationCo Australia's undissected payments as low risk does not preclude further investigation of the unrelated global software provider's arrangements in Australia.*

### **Example 3 – software copies stored on physical media acquired by a retailer**

41. *Electronics Retail Co is a large Australian retail company that sells consumer electronics and white goods at stores located throughout Australia.*

42. *Electronics Retail Co also sells software such as productivity programs on physical media. Electronics Retail Co has wholesale agreements with offshore software companies which enables Electronics Retail Co to purchase the software on physical media at reduced prices.*

43. *Under the wholesale agreements, Electronic Retail Co has no rights to copy, modify or sublicense, nor has any other rights to use the software copyright of the offshore companies.*

44. *For the purposes of this Guideline, the payment by Electronics Retail Co to the offshore software providers under the wholesale agreements are categorised in the green zone as the software copies on physical media are acquired in the course of Electronics Retail Co's business of reselling the software copies and Electronics Retail Co does not require or have the rights to use the IP of the offshore software companies.*

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**Example 4 – washing machines with embedded software**

45. *White Goods Co manufactures washing machines with smart technology and sells the products to Australian customers through its subsidiary distributor AusCo. AusCo makes payments to White Goods Co for the washing machines under a distribution agreement.*

46. *The smart washing machines AusCo purchases from White Goods Co have pre-installed software that allows consumers to remotely control and monitor their washing machine through an application on a smart phone. The software embedded in the washing machine also supports the sensor functions that automatically dispense detergent, monitor energy consumption during wash cycles, and run diagnostic tests and troubleshoot problems.*

47. *AusCo does not have any rights to modify, or rights to sublicense the modification rights, the software installed onto the smart washing machines.*

48. *The payments by AusCo to White Goods Co are categorised in the green zone as they are for finished tangible goods of which software is an inherent and practically inseparable part, and the software is to enable the tangible goods to perform their intended function and the goods are acquired for resale to retail customers.*

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## Your comments

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49. You are invited to comment on this draft Guideline. Please forward your comments to the email address below by the due date.

50. A compendium of comments is prepared when finalising this Guideline, and an edited version (names and identifying information removed) may be published to the Legal database on ato.gov.au.

51. Please advise if you do not want your comments included in the edited version of the compendium.

**Due date:** 17 September 2025

Contact officer details have been removed as the comments period has ended.

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## References

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*Related rulings and determinations:*

TR 2024/D1

*Legislative references:*

- ITAA 1936 6(1)(a)
- ITAA 1936 Pt IVA
- ITAA 1936 177DA
- ITAA 1997 Subdiv 815-B
- ITAA 1997 Subdiv 815-C

*Cases relied on:*

- PepsiCo, Inc v Commissioner of Taxation [2024] FCAFC 86; 303 FCR 1; 2024 ATC 20-918

*Other references:*

World Intellectual Property Organization (2020), [What is Intellectual Property?](#) [website], accessed 1 May 2025

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ATO references

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