Australia

Australian Taxation Office Consults on Characterization of Software Payments as Royalties

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The Australian Taxation Office (ATO) has issued Draft Taxation Ruling TR 2024/D1 that deals with the characterization of payments in respect of software and intellectual property rights as royalties.

By way of background, in 1993, the ATO issued Taxation Ruling TR 93/12 that dealt with computer software payments. Under TR 93/12, payments for a licence that allowed only the "simple use" of software, without permitting any use of the copyright itself, were not classified as royalties.

In 2021, TR 93/12 was withdrawn and the ATO changed its view to a "rights-based" approach in Draft TR 2021/D4, under which a payment for a right to use copyright (or any other intellectual property) should be classified as a royalty regardless of whether or not the right is exercised. This classification is subject to exclusions; for example, payments for a right wholly for distribution of copies of software are not royalties.

Draft Taxation Ruling TR 2024/D1 replaces Draft TR 2021/D4 without changing the ATO's "rights-based" approach. Further, Draft TR 2024/D1 states that payments for a sale of hardware with embedded software could also be royalties where the distributor has a right to use the software. Draft TR 2024/D1 also considers the interaction of the domestic definition of "royalties" with the definition in the Australian treaties should a treaty apply to software payments.

The public consultation on TR 2024/D1 ends on 1 March 2024.