



Tax Insights

ATO releases draft guidance on low-risk payments relating to software arrangements

On 6 August 2025, the Australian Taxation Office (ATO) released draft practical compliance guideline (PCG) [PCG 2025/D4 Low-risk payments relating to software arrangements—ATO compliance approach](#) (PCG 2025/D4).

While the release of PCG 2025/D4 has been eagerly awaited, many readers may be left questioning whether the PCG achieves its intended goal of providing clear and practical public advice and guidance on which taxpayers can rely to manage their tax affairs.

What arrangements does PCG 2025/D4 cover?

PCG 2025/D4 is intended to provide 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.

PCG 2025/D4—which is non-legally binding public advice and guidance—must be read in conjunction with draft Taxation Ruling [TR 2024/D1 Income tax: royalties—character of payments in respect of software and intellectual property rights](#) (TR 2024/D1). TR 2024/D1, which will become the ATO's legally binding view of the application of the law once finalised, defines a software arrangement as:

“An agreement, arrangement or scheme under which a distributor makes payment or payments directly or indirectly to the owner or licensee (as the case may be) of the copyright (or other IP) for the right to be in a position to earn income relating to the use of, or right to use, software.”

PCG 2025/D4 relies on the term “undissected payment” which is said to arise where no portion of a cross-border payment is expressly stated to be a royalty by the instrument under which it is paid.

This term has been previously adopted in paragraph 18 of TR 2024/D1, where the ATO states:

“18. If an undissected amount is paid as consideration for matters all of which are sufficiently connected with the things mentioned in the definition of royalty, *the whole amount of the payment will be taken to be a royalty in the first instance.*”

[emphasis added]

The PCG 2025/4 adopts a definition of “intellectual property” (IP) which is taken from the World Intellectual Property Organization website being:

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.”

PCG 2025/D4 further adopts a definition on “IP rights” being:

“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.”

The definition of intellectual property or IP is not linked to the definition of IP rights. Neither definition is reflective of what IP may be capable of protection under law. The IP rights definition draws from article 12, subparagraph (3)(a) of the standard tax treaty definition of “royalty.” If IP rights are being defined with reference to the treaty and domestic definitions of royalty, noting the definition is currently not exhaustive, it would be helpful for both TR 2024/D1 and PCG 2025/D4 to address how it will treat other asset categories listed in those definitions which are relevant to software arrangements.

Risk assessment framework

Like many other PCGs, PCG 2025/D4 contains risk zones which are intended to assist taxpayers to self-assess the likelihood of the ATO applying compliance resources to like arrangements. Currently, and the title of the PCG 2025/D4 ought to have been an obvious tell, PCG 2025/D4 only contains a white zone and green zone.

White zone software arrangements

These are arrangements which will not require further risk assessment, and are limited to the following:

- There is a settlement agreement or advance pricing arrangement expressly covering the Australian withholding tax outcomes related to the arrangement;
- A court or tribunal has decided that a payment under the arrangement does or does not constitute a royalty; or
- The income year was the subject of a review or audit of the arrangement and the ATO provided a “low-risk” rating or a “high assurance” rating as part of a justified trust review.

Green zone software arrangements

These are required to meet the following criteria and will only apply where the payment is only in relation to the acquisition of:

- Software acquired solely for private or domestic use;
- Software which is installed and used in the course of the taxpayer's own business, is not substantially customised, and not further sold, licensed, or otherwise exploited as a primary object of the business;
- Finished tangible goods of which software is an inherent or practically inseparable part; or
- Software copies stored on physical media in the course of a business of reselling the software copies, where the taxpayer and their associates do not require or have the rights to use offshore IP.

The green zone criteria are accompanied by four examples which focus on software acquired for private and domestic use (example 1), software ancillary to business operations (example 2), software stored on physical medium (example 3), and embedded software (example 4).

Deloitte Australia's observations

Many readers may consider the current risk zones to be more aligned to no-risk software arrangements rather than low-risk. The absence, for now, of risk zones beyond white and green leaves one wondering as to how all other software arrangements are to be treated by the ATO.

Despite multiple rounds of consultation, it remains to be seen whether the ATO will address public concerns raised in respect of TR 2024/D1. Paragraph 3 may suggest that the ATO is wedded to its draft position, however it is noted that the finalisation of TR 2024/D1 is pending the decision of the High Court of the ATO's appeal from the Full Federal Court decision in *PepsiCo. Inc. v. Commissioner of Taxation* [2024] FCAFC 86. The High Court's decision will be handed down on 13 August 2025.

Taxpayers with business operations that involve software arrangements will need to monitor developments for the finalisation or amendment of both PCG 2025/D4 and TR 2024/D1.

While PCG 2025/D4 may not have offered the breadth of guidance required, it emphasises the importance of taxpayers understanding the ATO's perceived risks in respect of software arrangements, namely the characterisation, avoidance of withholding tax obligations, and interactions with transfer pricing and anti-avoidance provisions.

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