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Dear Mr Wilson

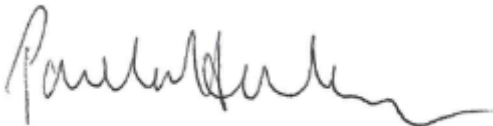
Draft Taxation Ruling TR 2024/D1—Income tax: royalties—character of payments in respect of software and intellectual property rights

The Taxation Committee, together with the Intellectual Property Committee, of the Business Law Section of the Law Council of Australia (the **Committees**), welcome the opportunity to comment on Draft Taxation Ruling TR 2024/D1, which considers when amounts paid under software arrangements are royalties under section 6(1) of the *Income Tax Assessment Act 1936 (ITAA 1936)* and Australia's tax treaties (**Draft Ruling**).

The Committees would be pleased to discuss any aspect of this submission. If you would like to do so, please contact:

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- Chair of the Intellectual Property Committee, Richard Hoad at rhead@jonesday.com, or convenor of the Copyright Subcommittee, Warwick Rothnie at war@vicbar.com.au.

Yours faithfully



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Law Council
OF AUSTRALIA

Business Law Section

Draft Taxation Ruling TR 2024/D1— Income tax: royalties— character of payments in respect of software and intellectual property rights

Australian Taxation Office

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Executive Summary

1. In summary, the Committees make the following comments in relation to the Draft Ruling:
 - (a) **Copyright laws:** In a number of respects, the tax analysis is based on incorrect assumptions and/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. These issues are discussed below, and a more detailed summary of relevant issues has been prepared by the Intellectual Property Committee (see **Schedule 1** to this letter).
 - (b) **Software as a service (SaaS):** The Draft Ruling conflates the concepts of online delivery of computer program functionality (e.g. a service) with the online delivery of the computer program itself. The former may not entail the exercise of copyright. The various references to SaaS in the Draft Ruling should be amended to reflect this distinction.
 - (c) **OECD Commentary—software distributors:** We also have significant concerns with the ATO’s interpretation of paragraph 14.4 of the OECD Commentary on Article 12, which considers arrangements between software copyright holders and distribution intermediaries that have the right to distribute copies of a program without the right to reproduce the program. We believe the ATO has adopted an overly narrow reading of the OECD guidance that is inconsistent with the Commentary’s text and intent.
 - (d) **Simple use:** The ATO previously expressed the view in TR 2021/D4 that payments in consideration for the “simple use” of software did not give rise to royalties. The removal of this concept from the Draft Ruling has created doubt as to what the ATO’s view is in respect of “simple use” of software where it is acquired directly from an offshore supplier. The ATO should more clearly set out its views in respect of “simple use” in the ruling, including appropriate references to paragraph 14 of the OECD commentary.
 - (e) **Examples:** The examples provided in the Draft Ruling need to be revisited in light of the operation of Australian copyright law. In addition, examples should be included that cover other types of ordinary commercial transactions, including accessing SaaS products where there is no communication or reproduction of the underlying code in which copyright subsists.

Submission

Copyright laws

2. In a number of respects, the tax analysis in the Draft Ruling is based on incorrect assumptions and/or misunderstandings about the operation of Australian copyright laws. A more detailed summary of relevant issues has been prepared by the Intellectual Property Committee and is set out in **Schedule 1** to this letter.

Communication to the public

3. The scope of the “right of communication to the public” under the *Copyright Act* 1968 (Cth) appears to be misunderstood. The right is exercised when a relevant work or other subject-matter in which copyright subsists is communicated to the public.
4. “Communication” means (1) electronic transmission of the subject matter, and/or (2) making the subject matter available online.
5. A communication is taken to have been made by the person responsible for determining the content of the communication.¹ The analysis in the Draft Ruling places a great deal of emphasis on the terms of the purchase or licence agreement between a distributor and an end-user as evidence of the distributor being responsible for “determining the content of the communication” because “*the terms of the EULA specify which programs an end-user will obtain use of*”.² See also paragraph 152 which states:

So too any intermediary who enters into a licence with the end-user may be responsible for determining the content of the communication, where that licence specifies the terms upon which the software will be made available to the end-user.

6. In our view, this represents a misunderstanding of the application of the law in this context because it is neither the purchaser, nor the distributor, who determines the content of each relevant software program purchased, but the supplier of the program.
7. The Full Court explained this concept as follows (emphasis added):³

The communication right—person responsible for the communication

69. *Section 22(6) was introduced by the Copyright Amendment (Digital Agenda) Act 2000 (Cth) (“the 2000 Amendment”) and is in the following terms:*

“For the purposes of this Act, a communication other than a broadcast is taken to have been made by the person responsible for determining the content of the communication.”

70. *The November 1999 Advisory Report on the Copyright Amendment (Digital Agenda) Bill 1999 at par 6.13 states that this section was specifically intended to address “the issue arising from the music on hold case”, namely, Telstra Corporation Ltd v Australasian Performing Right Association Ltd (1997) 191 CLR 140. That is, the section was intended to protect ISPs, carriers and carriage service providers from liability for direct infringement of the communication right where they were not*

¹ Subsection 22(6), Copyright Act

² See, for example, paragraph 29.

³ *Universal Music Australia Pty Ltd v Cooper* (2005) 150 FCR 1 at [69] – [74]. Tamberlin J’s ruling on this issue was not affected by the Full Court.

responsible for determining the content of the infringing material: see “Digital Agenda Copyright Amendments: Exposure Draft and Commentary” (February 1999), par 116; “Copyright Reform and the Digital Agenda”, Discussion Paper (July 1997), par 4.72; “Revised Explanatory Memorandum” to the Copyright Amendment (Digital Agenda) Bill 2000, par 41.

71. There is no statutory definition of the expression “person responsible for determining the content”. Counsel for the applicants again resorts to the Macquarie Dictionary, which defines “responsible for” to mean “chargeable with being the author, cause or occasion of”. The word “determine” is defined to mean “to decide upon.” As discussed above, the approach of the applicants suffers from the difficulty that it is too literal and analytical and does not pay sufficient attention, in my view, to the collocation of the expressions used, as distinct from the individual words.
72. The applicants say that the focus of attention of s 22(6) of the Act is not on the person carrying out the technical processes involved in the communication but rather on the person bearing the responsibility for the content of the communication. They note, however, that the criteria for the Court to take into account in determining responsibility for a communication are not set out in the Act.
73. The applicants point out that statements in the extrinsic materials which they rely upon, namely, the “Revised Explanatory Memorandum” to the Copyright Amendment (Digital Agenda) Bill 2000 (Cth) and the “Digital Agenda Copyright Amendments: Exposure Draft and Commentary” (February 1999), generally speak of “the person” or “a person” who is responsible for determining the content of a communication. They note that there is no specific discussion in the extrinsic material of a situation in which two or more persons jointly determine the content of a communication. However, I accept the applicants’ submission that there is no logical reason why more than one person could not be responsible for a communication and that it is open to read the reference to “the person” in s 22(6) in the plural where the context indicates.
74. On the natural and ordinary meaning of the words used in s 22(6), in the context of the present dispute, I do not think it can be said that a person who is the proprietor, manager or operator of a website which provides hyperlinks to other websites on which the sound recordings are hosted **determines** the content of the communication. It is artificial in the extreme to suggest that the person or body who facilitates access from the website to a remote site and provides a trigger which enables sound recordings to be downloaded from that remote site is responsible for the content of the communication from the remote website. The fact is that, on the evidence, Cooper does not “determine”, “formulate” or “create” the content of the remote website from which the communication takes place.
75. The applicants point to Cooper’s ability to control the links on his website, to determine precisely what files would be made available by means of the links created on his website and the manner in which the files were made available to internet users as indicative of his responsibility for determining the content of the communication. However, a power to remove a hyperlink to a remote website from the Cooper website is not a power or responsibility for determining the content of that remote website and the content of the communication to the internet user. The capacity to prevent hyperlinks from being added to the website and therefore to prevent internet users from accessing sound recordings via the Cooper website, is not the same as the ability to determine the content of a communication from a remote website. In cross-examination, Mr Speck agreed that Cooper had no control over whether a music file remained available on a remote website. Mr Speck said that should a remote website become unavailable, a visitor to the Cooper website would be unable to access the music files listed on the Cooper website as being

available from the hosting website and would receive an error message whenever he or she attempted to visit that site and recover files from it.

76. It is the entitlement and role of the designer, operator and owner of a remote website to determine what is placed on that website and therefore what is the “content” of that website. If the content includes infringing copyright material, then the responsibility for that lies with the person or persons who place that material on the remote website and thereby make it available for transmission to the public. This is consistent with the “Digital Agenda Copyright Amendments: Exposure Draft and Commentary” (February 1999).
8. Similar analysis may be found in Emmett J’s judgement in *Roadshow Films Pty Limited v iiNet Limited* [2011] FCAFC 23 at 166 (emphasis added):

Section 22(6) provides that the maker of a communication is the person responsible for determining the content of the communication. Section 22(6A) has the effect that a person is not responsible for determining the content of a communication merely because the person takes a step to gain access to what is made available online or to receive an electronic transmission. It is not correct to say that the sole causative factor in the transmission taking place and the content of the transmission is the request from the downloading computer. The process of electronic transmission is not simply one of a request and transmission, determined by the requesting party. The sender of the Film file is the party who determines the content of the communication, by having the BitTorrent Client software installed in a computer so as to respond to a request for a Film file, thus permitting the communication to occur.

9. Subsequently, an intermediary was found to be the, or a, maker of the communication as a result of very close consideration of the detailed facts including the technical, contractual and other practical matters. The circumstances included that the intermediary itself set up the scheme, hosted the server from which the files were transmitted and effectively undertook all the dealings with the end-users.⁴
10. The copyright authorities support the position that the “communication” and “transmission” of a work are not the same as “accessing” a work or even facilitating the “access” to a work. For the copyright right to be exercised, the relevant work or other subject-matter itself must be communicated. “Accessing” relevant work or other subject matter that has already been uploaded to an online server does not involve an exercise of the copyright unless there is a reproduction, or adaptation, of a substantial part of the copyright material.
11. The Draft Ruling also misconstrues the *Roadshow* case⁵ as support for the proposition that both a copyright owner and a distributor that does not decide the content of a software program are responsible for determining the content of a communication on the basis, among other things, that more than one person may be responsible for determining the content of a communication.⁶ However, the *Roadshow* case concerned numerous parallel suppliers of parts of a whole work. It is not, therefore support for the position that an intermediary who does not decide the content uploaded to a website is also the maker of the communication of the content on the website when the intermediary provides access to that content to an end-user.

⁴ [Pokémon Company International, Inc. v Redbubble Ltd](#) [2017] FCA 1541; 129 IPR 1 at [48]. (Pagone J)

⁵ *Roadshow Films Pty Ltd v iiNet Limited* [2012] HCA 16; 248 CLR 42; 86 ALJR 494; 286 ALR 466.

⁶ Paragraph 170, Draft Ruling. The proposition in the second paragraph of the first bullet point of paragraph 170 referencing s 43B of the Copyright Act 1968 is controversial.

Authorisation

12. The Draft Ruling misstates the nature of a copyright owner’s “authorisation right”. It is a right to authorise a person to do an act *comprised in the copyright*.
13. If the action said to be authorised does not involve an exercise of a right comprised in the copyright, there is no exercise of the authorisation right as authorisation in the copyright sense is not required.
14. Therefore, the authorising of simple “access” to a work, which does not generally amount to a “communication” of the work by the authorising party (see above), nor the exercise of copyright by an end-user (such as a communication, reproduction or adaptation of a substantial part of the copyright material), is not an exercise of the right to authorise. Nor would the authorising party in such an instance have been granted a “right to authorise” because they do not have a right comprised in the copyright when the right is limited to a right to grant end-users access to an owner’s copyright material.
15. Further, the premise of the “authorisation right” is that the owner of copyright can exercise the right to “authorise” another person to do things that would otherwise amount to an infringement of the owner’s copyright. It is, therefore, incorrect to characterise an intermediary, such as a distributor, as *authorising* the *owner* of the copyright to do an act comprised in the copyright.⁷ The owner of the copyright, by definition, cannot do an act which infringes their own copyright or that requires authorisation.

Intermediaries

16. Whether an intermediary entity is providing software to end-users for the owner of the software copyright as part of a service or on its own behalf (and hence exercising a right comprised in copyright) will depend upon the respective rights and obligations of the parties.
17. The use of an intermediary entity to facilitate the “communication” of a work to the public by the copyright owner does not automatically mean the intermediary is exercising the copyright or authorising someone else to exercise a right in the copyright. Whether the intermediary can be said to have authorised the exercise of copyright will depend very much on the precise nature of its relationship with the copyright holder and end-user, what the end-user “uses” or is enabled to do, and all the circumstances.
18. Consistent with the OECD’s position in paragraph 14.4 of the OECD Commentary on Article 12, on the basis of the authorities considered above, where an intermediary has mere distribution rights, without rights to reproduce, modify or adapt the software, the intermediary’s role should be characterised as a service performed on behalf of the owner of the copyright in the work, rather than a “communication” of the work by the distributor on its own behalf.
19. The position is likely to be different where the intermediary modifies or otherwise alters a substantial part of the original work before the work is communicated to the public because then the intermediary, rather than the copyright owner, is determining the content of the communication.

⁷ See, for example, paragraph 170 of the Draft Ruling.

20. Further, there should be no difference between the tax treatment of hard and soft copies of software: i.e. the tax treatment should be the same for the sale of software on a CD and the end-user accessing a website to download software that was uploaded by the copyright owner. Drawing a distinction between the distributions of hard and soft copies of software is:
- not consistent with Australian copyright law in respect of when a work has been “communicated” (see above);
 - inconsistent with OECD guidance (see further below); and
 - places emphasis on form over substance.
21. In summary, the Draft Ruling does not sufficiently address the different capacities in which distributors may deal with the public.

Software as a service

22. SaaS arrangements take many and varied forms; there is not a standard or “pro forma” form defined by the term “SaaS”. As a result, SaaS arrangements do not necessarily involve either the reproduction or communication to the public of any computer program. Users under SaaS arrangements may well be able to utilise the functionality delivered by the service without reproducing any part of the code, and without receiving any communication of the code. In this sense, users may “use” the program, but they do not exercise a right comprised in copyright in the course of such use.
23. A person who, for example, accesses an online calculator (e.g. mortgage payment calculators, BMI calculators), converter (e.g. currency converters, time converters) or search engine has no visibility in respect of the underlying code for those programs. In such circumstances, there is no “communication” of the subject-matter in which the copyright subsists because the code is not made available to the end-users. The users will simply enter inputs and receive outputs of data or information.
24. In addition, even if the end-users are able to access the underlying code, “accessing” the relevant work or other subject matter does not involve an exercise of the copyright unless there is a reproduction, or adaptation, of a substantial part of the copyright material: i.e. the underlying code.
25. The Draft Ruling conflates the concepts of online delivery of computer program functionality (e.g. a service, such as an online calculator) with the online delivery of the computer program itself (the underlying code). The former will not of itself entail the communication of a copyright work (i.e. the underlying code) to the public.
26. Having regard to the above, the Draft Ruling should be amended to reflect the correct position under copyright law for SaaS products to make it clear that making software available **for use** online is not the same as communicating something in which copyright subsists. See for example, paragraphs 144, 149, 152 and 174. Note, in particular, paragraph 150 which states:
- However, this does not prevent the conclusion that access to the functions of the software by the end-user is a consequence of the software being made available online.*
27. While the above sentence is strictly correct, the fact that the “software” is available for access online does not mean that the underlying code in which the copyright subsists

has been made available or “communicated” by the software provider. Where there has been no communication of the underlying code, there has been no communication of the work to the public.

28. We consider that the Draft Ruling should include specific examples involving SaaS products.

OECD Commentary

29. We have significant concerns with the ATO’s interpretation of paragraph 14.4 of the OECD Commentary on Article 12 in Draft Ruling TR 2024/D1. We believe the ATO has adopted an overly narrow reading of the OECD guidance that is inconsistent with the Commentary’s text and intent.
30. Paragraph 14.4 provides a clear example illustrating that payments by a software distributor who has only obtained limited distribution rights, without the right to reproduce the software, should be treated as business profits under Article 7, not royalties under Article 12. The key principles are:
- (a) the distributor is granted the right to distribute software copies, but not the right to reproduce the software.
 - (b) the distributor is only paying for the acquisition of the software copies, not for the right to exploit the underlying copyright.
31. The OECD Commentary does not limit these principles to the narrow facts of the example. Rather, it articulates the general principle that Article 12 royalties require consideration for the use of, or right to use, the copyright itself—mere distribution rights, without reproduction rights, are insufficient.
32. Notably, paragraph 14.4 expressly states this characterisation applies “regardless of whether the copies being distributed are delivered on tangible media or are distributed electronically (without the distributor having the right to reproduce the software), or whether the software is subject to minor customisation for the purposes of its installation”. This indicates the mode of delivery and minor installation-related modifications are not determinative.
33. However, the ATO’s interpretation in paragraph 185 of TR 2024/D1 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.
34. The ATO’s position also creates significant uncertainty by suggesting the entire payment would be a royalty unless the taxpayer proves the distribution rights had independent value, without providing clear guidance on how to apportion such payments. This will invite disputes and compliance burdens that undermine the Commentary’s aim of providing clear, administrable rules.
35. We submit that paragraph 14.4, read in full context, supports a broader principle that payments for mere distribution rights, without the right to reproduce the software, are not royalties, regardless of the mode of transfer or minor installation-related modifications. The ATO should focus its analysis on the substantive rights at issue, not ancillary factors.

36. A more flexible, substance-over-form approach, focused on whether the distributor has acquired the right to exploit the copyright, would be more consistent with the object and purpose of Article 12 and the OECD Commentary and the decision in *Pepsi Inc v Commissioner of Taxation* [2023] FCA 1490. The ATO's interpretation imposes limitations not supported by the express text of the OECD guidance.
37. Therefore, we respectfully request that the ATO reconsider its position on paragraph 14.4 to avoid an unduly restrictive approach and provide greater certainty to taxpayers. The final ruling should clearly reflect that payments for mere distribution rights, without the right to reproduce the software, are not royalties, in line with the principles and intent of the OECD Commentary.

Simple use

38. The ATO previously expressed the view in TR 2021/D4 that payments in consideration for the "simple use" of software did not give rise to royalties. "Simple use" describes circumstances where rights are acquired in relation to copyright that are limited to those necessary to enable the user to operate the software for the purpose for which it was designed—for example a limited right to reproduce the program only for the purposes of copying the program on to the user's computer but not extending to the right to modify or adapt the software. This approach was consistent with paragraph 14 of the OECD commentary on Article 12.
39. The concept of "simple use" has been removed altogether from the Draft Ruling, and the ATO has commented that it cannot accept the principle that "*payments made by a distributor for the right to distribute software to purchasers who make simple use of the software cannot be a royalty*".⁸ This has created doubt as to what the ATO's view is in respect of "simple use" where an Australian resident end-user purchases software directly from a foreign supplier which owns the copyright in the software (i.e. there is no Australian distributor). The ATO should clarify whether it intends that all end-users must pay royalties in such circumstances.
40. If so, the ATO should also clearly explain why the ATO is taking a position that is inconsistent with paragraph 14 of the OECD commentary on Article 12 which concludes that: "*payments in these types of transactions would be dealt with as commercial income in accordance with Article 7*".
41. If that is not the ATO's new position, then the ATO should explain why the treatment is different where there is an Australian distributor of such software, because, other than the provision of marketing services by the Australian distributor, there is no economic difference between these two scenarios.

Examples

Examples generally

42. The examples in Scenarios 1 and 2 cover very specific fact patterns and there are no examples of arrangements in which no royalty will be taken to have been paid. It is submitted that the examples provided in the Draft Ruling are too restricted in scope to provide sufficient guidance to taxpayers and further examples which are consistent with common commercial arrangements, including SaaS arrangements, should be included in the Draft Ruling.

⁸ Paragraphs 183 and 184, Draft ruling.

Specific examples in Draft Ruling

43. For the reasons set out above and below, the conclusions in respect of the various examples in the Draft Ruling should be revisited.

(a) Scenario 1

- The facts of this example entail OBA (the Australian distributor) obtaining a licence from a foreign related entity (IEL) to copy the Programs⁹ and OBA licensing that right to end-users to copy Programs for their personal use. As such, OBA obtains intellectual property rights from IEL in the form of the licence which it confers on end-users. The analysis needs to be amended to more clearly reflect the licensing arrangements, rather than the discussion of “rights to communicate” and “authorisation rights”.
- It is not a correct application of copyright law concepts to say that necessarily “OBA authorises the communication of the Programs to the end-user by IEL”.¹⁰ It is incorrect to characterise an intermediary, such as a distributor, as authorising the owner of the copyright to do an act comprised in the copyright.

(b) Scenario 2

- In this example, for the reasons set out above, under copyright law, AusCo does not “communicate” or “authorise” the communication of any software to end-users.
- There is a question as to why no amount is charged by ForeignCo for the licence/use of the software by end-users. To the extent that the fees collected by AusCo from customers relate to rights granted by ForeignCo to end-users under the IP licence, it might be argued that AusCo is effectively collecting ForeignCo’s licence fees. However, this would appear to be a good example of when the “simple use” exception should apply to such payments.

(c) Scenario 3

- “Computer games” are more properly considered cinematograph films for the purposes of the Copyright Act than “computer programs”.¹¹ The copyright in a cinematograph film does not include a right to enter into a commercial rental arrangement.¹² The example should be amended taking these issues into account.

⁹ It is assumed for the purposes of this example that end-users obtain access to the underlying code in which copyright subsists.

¹⁰ Paragraph 29, Draft Ruling.

¹¹ *Galaxy Electronics Pty Ltd & Gottlieb Enterprises Pty Ltd v Sega Enterprises Ltd* (1997) 75 FCR 8; 37 IPR 462 (Lockhart, Wilcox and Lindgren JJ).

¹² Compare Copyright Act, s 31(1)(c) and (d) [original works] and s 85(1)(d) [sound recordings] and s 86 (cinematograph films).

- The rights granted for the distribution of online access to the video-editing software are not correctly described as “*necessitating the use of IP rights*”¹³ because:
 - End-users may not obtain rights in respect of the underlying video-editing software in which the relevant copyright exists, rather, the access rights provided to end-users may be rights to solely use the functionality of the software. In that case, there would be no “communication” of work in which copyright subsists to the public; and
 - For the reasons set out above, even if the end-users do obtain copies of the underlying software, under Australian copyright law, the distributor should not be considered to “communicate” or “authorise” the communication of any software to end-users. As such, the distributor should be considered to be providing a simple service to the owner of the copyright in the software.
 - The following statement is not correct from a valuation perspective. Distribution rights for physical games and online software have the same essential character and the values of the distribution rights should be assessed by reference to the actual inherent values of such rights, not the fact that one right relates to an online product and the other right relates to a physical product:

A reasonable method of apportionment would take into account the fact that valuable IP rights were granted in respect of the online access to the video-editing software and that no such rights were granted for distribution of computer game copies. As such, it would be expected that any apportionment method adopted would result in the majority of the consideration being allocated to the IP rights used in respect of the online distribution.

¹³ Paragraph 117.

Schedule 1 - Intellectual Property Law Committee (IPC)— Detailed Comments

44. The IPC considers there are inaccuracies and ambiguities in the interpretation and application of intellectual property principles which underpin the Draft Ruling.
45. In the limited time available, we identify a number of the significant problems but by no means all. The inaccuracies and ambiguities are sufficiently important that they create serious issues for interpretation of the Draft Ruling.

Scope issues

46. First, the intended scope of the Draft Ruling should be described with more precision.
47. Paragraph 1 of the Draft Ruling states the Draft Ruling is addressed to when amounts paid under “a software arrangement” will be subject to royalty withholding tax. This is contradicted, however, by the title of the Draft Ruling and paragraph 3 which states the scope is directed to payments for a right to “use” copyright or some other, unidentified “like property right” or even more generally “other intellectual property rights”.¹⁴
48. Secondly, the Draft Ruling refers to “software”. The term “software” does not have a fixed legal meaning and it is doubtful that the glossary reflects its “ordinary meaning”, if it has such a meaning in Australian usage.
49. We note the glossary also includes a definition of “computer program” and the Draft Ruling also uses the term “Program”. We are not sure whether this different terminology is intended to reflect some different meaning or concept. Further, as discussed below, the Draft Ruling does not appear to use the term in this narrow sense.
50. For example, paragraph 125 of the Draft Ruling does state:

The Copyright Act recognises categories of subject matter that may be subject to copyright.^[109] The Commissioner’s view is that the term ‘copyright’ is a reference to any exclusive right of the copyright owner in a work^[110] to which Australian copyright law applies. Any act done in relation to a substantial part of a work is deemed to be done in relation to the whole of the work.^[111]

51. Footnote 110, however, refers to the definition of “work” provided by section 189 of the Copyright Act. This is wholly inapposite as section 189 is the definition section for Part IX—Moral Rights. The Draft Ruling, however, is concerned with “copyright”—the economic rights conferred by section 31 of the Copyright Act (in the case of original works) and ss 85 to 88 (in the case of “other subject matter”); not the exercise of moral rights such as the right of attribution and the right against derogatory treatment.
52. The definition of scope apparently intended to be provided by paragraph 125 of the Draft Ruling is much broader than the definition of “software” set out in the glossary.¹⁵ The definition of “software” in the glossary is said to be the ordinary meaning of the term.

¹⁴ As discussed further below, the terms “software” and “right to use” lack legal content and should be avoided.

¹⁵ While the glossary includes separate definitions of “computer program” and “software” although the significance of this distinction in the Draft Ruling is not clear to the reader.

53. For the most part, the Draft Ruling appears to be using the term “software” to refer to “computer program” (as that term is defined in Copyright Act).¹⁶ In a few places, however, the Draft Ruling refers, or appears to be referring, to other things such as films (“cinematograph films” for the purposes of the Copyright Act) or “computer games”. 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 has considered computer games to be cinematograph films for the purposes of the Copyright Act rather than “computer programs”.¹⁷
54. One consequence of this confusion is that the exclusive rights subsisting in the copyright are different depending on the nature of the subject matter. For example, the copyright in a cinematograph film does not include a right to enter into a commercial rental arrangement.¹⁸
55. As the Draft Ruling is intended (according to paragraph 125) to capture income derived from the exercise of a right subsisting in copyright and the rights are different according to what type of copyright is involved, the Draft Ruling needs to be amended to more precisely identify the subject matter involved and the rights being exercised.

Right to “use”

56. Noting that paragraph 125 of the Draft Ruling appears to indicate the Draft Ruling is directed to the exercise of one or more of the exclusive rights comprised in a copyright, it is important to be recognised that, unlike the legislation relating to trade marks and patents, the Copyright Act does not confer exclusive rights to “use” copyright, or even to “use” works or other subject-matter in which copyright subsists. Rather, as noted above, the legislation creates specific subject matter which comprised of specific exclusive rights.
57. The “use” of works (such as computer programs) or other subject-matter in which copyright subsists is regulated by the Copyright Act *only* to the extent that such use involves the exercise of one or more of the exclusive rights of the copyright owner (such as the right of reproduction, or communication to the public). Although a commonly used term, in a context calling for clear determination of or guidance to rights and obligations, it is therefore quite inaccurate and liable to result in error to loosely refer to rights “to use” software, particularly where the use of software may or may not involve the exercise of any copyright right, depending on the specific circumstances involved.¹⁹

¹⁶ For example, see the definition of “software” in the glossary and paragraph 126 refers to the reader to paragraphs 130 to 174 for a discussion about the exclusive rights of an owner of copyright in a computer program.

¹⁷ *Galaxy Electronics Pty Ltd & Gottlieb Enterprises Pty Ltd v Sega Enterprises Ltd* (1997) 75 FCR 8; 37 IPR 462 (Lockhart, Wilcox and Lindgren JJ).

¹⁸ Compare Copyright Act, s 31(1)(c) and (d) [original works] and s 85(1)(d) [sound recordings] and s 86 (cinematograph films).

¹⁹ *PM Sulcs & Associates Pty Ltd v Detroit Diesel-Allison Australia Pty Ltd* (1997) 39 IPR 328 (Lehane J), *Cantor Gaming Ltd v Gameaccount Global Ltd* [2007] EWHC 1914 (Ch) and *Racing and Wagering WA v Software AG (Australia) Pty Ltd* [2008] FCA 1332

58. The definitions of royalties, on their face, conflate the subject legal rights (e.g. copyright) and their relevant object (software or whatever else is the work or other matter in which such legal rights subsist). This is compounded by the definitions:
- (a) in part referring to legal rights (copyright ... or other like ... right);
 - (b) in part referring to the subject matter of the rights (i.e. the non-rights items listed in the definitions) and
 - (c) in part referring to terms which might be construed as either (i.e. patents, designs and trade marks).
59. This gives rise to real issues about whether payments are “royalties”:
- (a) if there is an exercise of one or more of the expressly-stated intellectual property rights or, otherwise, the use of the stated items; or
 - (b) if they are for the right to deal in something in which the legal rights subsist in whole or in part (or otherwise for the other listed (non-rights) items).
60. For example, a reseller contract involving “smart” goods (e.g. a vehicle or a refrigerator) which does not allow the reseller to exercise the appointor’s intellectual property rights. If paragraph 59(a) above is the correct construction then the reseller’s payments to the appointor would not be royalties. It would be otherwise if paragraph 59(b) above is the proper construction.
61. The ruling does not make the ATO’s position on this clear to the reader. So far as “software” is concerned, there are suggestions that what is intended is paragraph 59(a) above (payments for the exercise of copyright in the “software”), but equally there are also references to paragraph 59(b) above (payments for rights to deal in “software” regardless of the intellectual property licensing terms). Not every “software arrangement” will involve the exercise of a copyright right. In the case of a payment made in relation to a software arrangement which does not involve, or result in, the exercise of a right comprised in the copyright—or some other intellectual property right, this payment would not be characterised as a royalty on ordinary principles.
62. We understand that the international tax treaties, like the definition of “royalty” in ITAA 1936 section 6(1), do refer to “use” of software or the right to “use” software. We are not aware whether the Commissioner considers that the references to “use” in the international tax treaties extends the concept of royalty beyond ordinary principles and, if so, the basis for the Commissioner’s view.
63. The IPC recommends that the Draft Ruling review these references and revise them to make the ATO’s position clear and why, having regard to the proper characterisation principles.

International copyright

64. It is not clear what message paragraphs 127 to 129 of the Draft Ruling are intended to communicate in respect of the interaction between the Copyright Act, section 184 and the Copyright (International Protection) Regulations (**C(IP)R**).
65. The effect of the C(IP)R is that, when copyright subject matter is created in a foreign country (such as a member of the WTO), a corresponding copyright automatically comes into existence in Australia.
66. So, for example, if a citizen or resident in New Zealand (or any other member of the WTO) creates an original artistic work, or original literary work such as a computer program, a corresponding copyright arises in Australia.²⁰
67. Other countries' laws do have similar operation so that, for example, if an Australian author makes an original literary work such as a computer program, copyright should also come into existence in the other members of the applicable international conventions such as the WTO without the need to register or apply for the grant of copyright there. Copyright Act, section 184 and the C(IP)R do not address that situation.
68. However, if an American taxpayer creates in America an original literary work such as a computer program and as a result copyright in that computer program also comes into existence in Australia and, say, the UK, income or royalties received by the American taxpayer from licensing the copyright in the UK does not involve the exercise of *any* copyright (or any other right) in Australia. Whether or not this is what the Commissioner intends should be clarified.

Communication to the public

69. The Draft Ruling discusses the communication right in particular at [142]—[152].
70. The second aspect of the communication right, the making available right, involves acts such as uploading to an online server. As its definition indicates, it does not involve either transmission or “accessing”. (For present purposes, we assume that the copyright law in the place where the overseas server is located includes the making available right.)
71. In this context, therefore, the distinction between “communicated” and “accessed” is significant. For the copyright right to be exercised, the relevant work or other subject-matter itself must be communicated. “Accessing” the relevant work or other subject matter does not involve an exercise of the copyright unless there is a reproduction, or adaptation, of a substantial part of the copyright material.
72. Whether or not there is a communication, reproduction or adaptation of the whole or a substantial part of copyright material will depend therefore on the copyright subject matter involved and the nature of the service being provided.
73. The Draft Ruling appears to be based on a view that “accessing” a SaaS service necessarily involves the transmission of some portion of the underlying code to the end-user. This is not necessarily so.

²⁰ For example, *Enzed Holdings Ltd v Wynthea Pty Ltd* (1984) 4 FCR 450; 3 IPR 619 (Sheppard, Morling and Wilcox JJ).

74. It is significant that “SaaS” (software as a service) arrangements take many and varied forms. They do not necessarily involve either the reproduction or communication to the public of any computer program. Users under many SaaS arrangements are able to utilise the functionality delivered by the service without reproducing any part of the code, and without receiving any communication of the code. In this sense, users may “use” the program, but they do not exercise a right comprised in copyright in the course of such use.
75. The Draft Ruling in places appears to gloss over this important distinction, conflating the concepts of online delivery of computer program functionality with the online delivery of the computer program itself; similarly the making available online of a particular service, as distinct from the making available online of the computer program. Not every SaaS arrangement involves a communication to the public of a copyright work; it will be a question of fact in each case whether or not any copyright right is engaged.
76. In this regard, it is notable that none of the scenarios posed in the Draft Ruling appear to involve SaaS products, or products involving access to “cloud-based” software alone. In each of the scenarios, there is an identifiable potential exercise of copyright, for example, an act of reproduction by way of download from servers or on to the user’s device, which renders the analysis more straightforward. The application of the Draft Ruling where such acts do not occur is significantly less clear and requires much closer consideration of how particular SaaS services work.
77. As the Draft Ruling recognises in paragraph 152, whether the involvement of an intermediary will constitute them a “maker” for this purpose will depend very much on the particular circumstances of the case and calls for consideration of the characterisation issues discussed below.

Adaptation right

78. The discussion of the right to make an adaptation (paragraph 156) is very confusing.
79. First, the exclusive right to make an adaptation applies only to original literary, dramatic, musical or artistic works; it does not apply to cinematograph films.²¹
80. Secondly, “adaptation” is a narrowly defined term: see Copyright Act, section 10(1) “adaptation”.
81. Thirdly, *Zecccola v Universal City Studios* does not stand for the proposition it is cited as authority for in footnote 151. The case related solely to whether or not there was a *prima facie* case sufficient to support an interlocutory injunction and specifically did not address the issues raised by the adaptation right. On the contrary, the adaptation right has been conferred because there is not the required objective similarity between the adaptation and the original work.²²

²¹ Compare Copyright Act, s 31(1) and s 86.

²² See e.g. the problems discussed in *Motorola Solutions, Inc. v Hytera Communications Corporation Ltd (Liability)* [2022] FCA 1585; 172 IPR 221 at [1220] to [1223] and [1198] to [1219]. Judgment in the appeal has been reserved.

Authorisation right

82. The Draft Ruling's explanation of the authorisation right ([163]—[174]) appears to us to be problematic.
83. First, the Draft Ruling appears to be using “authorisation” in its dictionary sense rather than as it has developed a legal concept of copyright law. The High Court has made it clear that the question of authorisation does not simply turn on whether a person can be described as sanctioning, approving or countenancing the relevant conduct. Rather, it requires a very close focus on all the facts and must be decided by reference to the factors mandated by Copyright Act, sections 36(1A) and 101(1A).²³
84. Secondly, the right to authorise (whether direct or indirect) is implicated only when the act being authorised is itself an act comprised in the copyright. For example, Copyright Act, section 13(2) is not just a right to authorise “in gross”. It is a right to authorise a person to do a right comprised in the copyright.
85. If the action said to be authorised does not involve an exercise of a right comprised in the copyright, there is no exercise of the authorisation right as authorisation in the copyright sense is not required.
86. For the “right to authorise” to be implicated, what is “authorised” must be something which if done without authorisation would be an infringement of copyright.
87. As a result, the analysis in the Draft Ruling in relation to provisions in the Copyright Act such as sections 43B is contestable. So far as we are aware, it has not finally been settled in Australia that section 43B involves the exercise of the copyright which is excused as a defence or, alternatively, operates as a limitation on the scope of the exclusive right so that acts falling within the scope of the provision do not involve an exercise of copyright and so do not require permission. On this second view, if the conditions of section 43B are met, there is no exercise of the copyright requiring a licence from the copyright owner.
88. Secondly and correspondingly, the concept that an intermediary such as a distributor or licensee can authorise the owner to exercise a right comprised in the owner's own copyright is controversial. The owner of the copyright by definition cannot do an act which infringes their copyright or that requires authorisation. If the owner has granted someone else an exclusive licence of copyright and then exercises the copyright themselves, or licenses a third party to do so, that may breach the contract between the owner and the exclusive licensee but it is not an infringement of copyright.²⁴
89. In this respect, the discussion in paragraphs 172 to 174 is very confusing and requires considerable clarification. The last sentence of paragraph 173 does not appear to be controversial in that it treats as a royalty a payment where the taxpayer has authorised another person to do an act which is within an exclusive right of the relevant copyright owner. The second and third sentences seem to suggest that some element of apportionment may be involved to the extent the payment may relate to things other than the exercise of a right in the copyright. This is not clear.
90. Whether or not there is a payment for the exercise of an intellectual property right should depend on a proper characterisation of the transaction.

²³ *Real Estate Tool Box Pty Ltd v Campaigntrack Pty Ltd* [2023] HCA 38; 98 ALJR 27 esp. [64] – [65].

²⁴ *CBS United Kingdom Ltd v Charmdale Record Distributors Ltd* [1980] FSR 289 at 295.

Characterisation

91. The guidance given by the Draft Ruling would be significantly enhanced by more detail regarding characterisation in the body of the Ruling, including as to the importance, but not conclusiveness, of the terms of the relevant parties' agreement. At present the draft only deals with the characterisation issue in the context of the Commissioner's position under hypothetical Scenario 1:

Characterisation of payment

34. The terms of the [stated scenario's] Licence Agreement are relevant to, but not determinative of, the characterisation of the payment. The payments under the Agreement are characterised from a practical and business point of view. That is, neither the use of the term 'distributor' . . . nor the grant of a right to 'distribute' . . . are determinative of the character of the payment. Similarly, the fact [that a clause states that] the fee is 'not a royalty' does not determine the character of the fee.

92. How the Commissioner proposes to approach characterisation of transactions and arrangements for payments is fundamental. In the IPC's recommendation, the Commissioner's approach should be spelled out much more clearly and as a matter of general application, not just for one scenario.
93. Further, this guidance could helpfully be developed by reference to what was said in *PepsiCo v FCT* [2023] FCA 1490 at paragraph 240:

*The question whether payments are consideration for the items set out . . . [in the royalties definitions] . . . involves an exercise of characterisation. . . . Fundamental to this task are the terms of the relevant agreement (or agreements) . . . In my view, it is necessary to consider the terms of the agreement in their business and commercial context. This is consistent with general principles of contractual construction that have regard to the commercial purpose or objects to be secured by the contract: *Electricity Generation Corporation v Woodside Energy Ltd* [2014] HCA 7; 251 CLR 640 at [35] per French CJ, Hayne, Crennan and Kiefel JJ. This approach furthers the evident purpose of Art 12, which is concerned with identifying the taxing rights of the Contracting States in relation to payments that are, in their business and commercial context, consideration for the use of, or the right to use, the relevant items. Likewise, this approach furthers the evident purpose of the royalty withholding tax provisions of the ITAA 1936, which are concerned with assessing tax on amounts that are, in their business and commercial context, consideration for the use of, or the right to use, the relevant items. [Emphasis added]*

Annexure A: About the Business Law Section of the Law Council of Australia

The Law Council of Australia represents the legal profession at the national level; speaks on behalf of its Constituent Bodies on federal, national, and international issues; and promotes the administration of justice, access to justice, and general improvement of the law.

The Business Law Section of the Law Council furthers the objects of the Law Council on matters pertaining to business law.

The Section provides a forum through which lawyers and others interested in law affecting business can discuss current issues, debate and contribute to the process of law reform in Australia, and enhance their professional skills.

The Law Council's Constituent Bodies are:

- Australian Capital Territory Bar Association
- Law Society of the Australian Capital Territory
- New South Wales Bar Association
- Law Society of New South Wales
- Northern Territory Bar Association
- Law Society Northern Territory
- Bar Association of Queensland
- Queensland Law Society
- South Australian Bar Association
- Law Society of South Australia
- Tasmanian Bar
- Law Society of Tasmania
- The Victorian Bar Incorporated
- Law Institute of Victoria
- Western Australian Bar Association
- Law Society of Western Australia
- Law Firms Australia

The Business Law Section has approximately 900 members. It currently has 15 specialist committees and working groups:

- Competition & Consumer Law Committee
- Construction & Infrastructure Law Committee
- Corporations Law Committee
- Customs & International Transactions Committee
- Digital Commerce Committee
- Financial Services Committee
- Foreign Corrupt Practices Working Group
- Foreign Investment Committee
- Insolvency & Reconstruction Law Committee
- Intellectual Property Committee
- Media & Communications Committee
- Privacy Law Committee
- SME Business Law Committee

- Taxation Law Committee
- Technology in Mergers & Acquisitions Working Group

The Section has an Executive Committee of 11 members drawn from different states and territories and fields of practice. The Executive Committees meet quarterly to set objectives, policy and priorities for the Section.

The members of the Section Executive are:

- Dr Pamela Hanrahan, Chair
- Mr Adrian Varrasso, Deputy Chair
- Dr Elizabeth Boros, Treasurer
- Mr Philip Argy
- Mr Greg Rodgers
- Mr John Keeves
- Ms Rachel Webber
- Ms Caroline Coops
- Ms Shannon Finch
- Mr Clint Harding
- Mr Peter Leech

The Section's administration team serves the Section nationally and is part of the Law Council's Secretariat in Canberra.

The Law Council's website is www.lawcouncil.asn.au.

The Section's website is www.lawcouncil.asn.au/business-law.