Investment income and royalties paid to foreign residents

You may be required to withhold tax from investment income and royalties paid to foreign residents.

Overview

Introduction to the requirements of withholding tax from payments to foreign residents.

Interest, dividends, royalties and MIT payments

Understand which types of payments you may need to withhold tax from.

Who withholds

Understand who must withhold tax from interest or royalties paid.

When to withhold

Learn when you should withhold tax from interest, dividends and royalties you pay to a foreign resident.

Withholding rate

Find out about withholding rates for joint accounts and Australian resident living overseas temporarily.

Obligations

Both you and the payee have obligations you must meet with regards to withholding from investment income and royalties.

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Overview

Introduction to the requirements of withholding tax from payments to foreign residents.

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Australian payer who pay interest, dividends, royalties or managed investment trust (MIT) payments to foreign residents, must generally withhold the final tax amount from the payment. For dividend payments, you will only withhold tax from the unfranked component.

If the amount you withhold was:

- greater than the tax owed , the payee can apply for a refund (see **Refund of over-withheld withholding: how to apply**)
- less than the tax owed, the payee must make a top-up payment to us.

Note: Australian payers can be an Australian resident or foreign resident with a permanent establishment in Australia.

For more information, see:

- **Managed investment trusts – withholding rules**
- **Permanent establishments.**

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Interest, dividends, royalties and MIT payments

Understand which types of payments you may need to withhold tax from.

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On this page

Interest

Interest for withholding tax purposes includes:

- interest payments
- amounts you pay in the nature of interest, such as a discount on a security
- amounts you pay as a substitute for interest, such as a lump sum paid instead of paying periodical interest
- dividends you pay for non-equity shares but not an amount that is a return on an equity interest in a company
- the profits on the transfer of a qualifying security – that is, a security where the sum of the payments to be made (excluding periodic interest) exceeds the issue price
- charges you pay under hire purchase and similar financial arrangements

- the discount element of payments you make to offshore acceptors of bills of exchange and promissory notes
- non-monetary payments.

Temporary residents

Temporary residents who are Australian residents for tax purposes do not have to withhold tax from payments they make to foreign lenders.

Example: Exemption for a temporary resident

John is an Australian resident for tax purposes who works in Australia under a business (long stay) temporary visa. John owns a house overseas for which he continues to make monthly mortgage payments. John does not have to withhold tax from the interest payment he makes to the overseas bank.

If John was an Australian resident holding a permanent resident visa, he may have to withhold tax from each interest payment he makes. It is likely that John's loan contracts will include an indemnity clause that requires him to pay the withholding tax in addition to the interest payment.

See **Work out your residency status for tax purposes** and **Exempt foreign employment income** for more information.

Dividends

Dividends for withholding tax purposes include:

- any distribution made by a company to any of its shareholders in the form of money or other property
- any amount credited by a company to any of its shareholders
- the return on all equity interests, including non-share dividends (not including dividends paid for non-equity shares that are subject to interest withholding tax).

You must issue a statement to your shareholder or payee that indicates the extent the dividend is franked or is conduit foreign income. You do not have to withhold tax if the dividends you pay have been fully franked or they are conduit foreign income.

See **Receiving dividends and other distributions** for more information.

Royalties

Royalties are generally payments made by one person for the use of rights owned by another person. They may be periodic, irregular or one-off payments.

Royalties also include payments or credits of any kind in return for:

- the use of, or the right to use
  - any copyright, patent, design or model, plan, secret formula or process, trademark, or other similar property or right
  - industrial, commercial or scientific equipment
  - motion picture films, television films or video tapes, or tapes for radio broadcasting
  - satellite, cable, optic fibre or similar technology in television and radio broadcasting, whether or not such material is edited or the broadcast is delayed
- the supply of scientific, technical, industrial or commercial knowledge or information
- services that are related to, or part and parcel of enabling the above property, rights, equipment or knowledge to be applied or enjoyed
- receiving, or the right to receive, public transmissions by satellite, cable, optic fibre or similar technology
- an undertaking that any of the above property or rights will not be granted or supplied to anyone else
- film and video tape royalties.

MIT payments

A managed investment trust (MIT) is a type of unit trust in which members of the public collectively invest in passive income activities, such as shares, property or fixed interest assets. A trust qualifies as an

MIT if it meets certain requirements for the income year it is in operation.

The rate of tax to be withheld from payments to non-resident members will vary according to whether the member is a resident of a country that has a tax treaty or exchange of information agreement with Australia, and whether the amount is:

- a payment of dividends, interest and royalties
- a 'fund payment'.

See **Managed investment trusts – overview** for more information.

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Who withholds

Understand who must withhold tax from interest or royalties paid.

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You must withhold tax from the **interest** or **royalties** you pay if you are:

- an Australian resident payer and pay
  - a foreign resident payee with an overseas address
    - whether the loan is for business or private purposes
    - where the royalty payment relates to your business in Australia
  - another Australian resident payee where
    - your payee carries on their business outside of Australia, and
    - the payment relates to your business carried on in Australia
- a foreign resident payer in Australia and pay
  - a foreign resident payee with an overseas address where the payment relates to your business in Australia

  - an Australian resident payee where
    - the payee carries on their business outside of Australia, and
    - your business is carried on in Australia.

If you operate a company that is an Australian resident, you must withhold amounts from unfranked or partly franked **dividends** that are not conduit foreign income if either of the following applies:

- the payment is made to an entity which has an address outside Australia
- your company is authorised to pay the dividend to any entities outside Australia.

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When to withhold

Learn when you should withhold tax from interest, dividends and royalties you pay to a foreign resident.

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On this page

When you should withhold

You should withhold tax from interest, dividends and royalties you pay to a foreign resident when any of the following occurs:

- you make the payment
- you credit the payment to the foreign resident's account

- you deal with the payment on behalf of, or at the direction of, the foreign resident.

If you are an Australian agent of a foreign resident, you should withhold tax when you:

- receive the payment on behalf of the foreign resident
- have the amount credited to your account
- have the payments dealt with at the direction of yourself or the foreign resident payee.

Exemptions – interest

You do not have to withhold amounts from interest if the payee is not liable to pay withholding tax on those amounts, for example if a payee is entitled to the foreign income exemption for temporary residents.

Other exemptions may include interest relating to certain:

- exempt non-resident entities involved in
  - charitable, educational or scientific pursuits
  - community service
  - aviation and tourism promotion
  - sports, culture and recreation
- non-resident hospitals
- non-resident sports, cultural and recreational entities

Some payments exempt from income tax in the payee's country of residence include payments relating to:

- certain exempt non-resident charitable institutions
- certain publicly offered company debentures or debt interests
- certain publicly offered unit trust debentures or debt interests
- certain offshore borrowings by offshore banking units
- certain tax avoidance schemes where income is diverted
- certain non-resident superannuation funds for foreign residents

- certified infrastructure borrowings
- trustees, assessed to trustees under particular trust provisions
- a nostro account derived by a non-resident foreign bank
- a non-resident carrying on a business in Australia through a permanent establishment the non-resident has in Australia (excluding certain limited partnership arrangements)
- amounts subject to family trust distribution tax
- trustee income under certain closely held trust provisions.

You should refer to the specific provisions in order to determine eligibility for an exemption in these circumstances.

Example: Exemption for a foreign resident

PQR is a foreign resident carrying on a business through a permanent establishment in Australia that issues debentures. Provided the debentures meet the public offer test, PQR will not have to withhold tax from the interest they pay to their foreign resident debenture holders

Exemptions – royalties and dividends

You do not have to withhold amounts from royalty or dividend payments you make to a foreign resident of a treaty country if the:

- foreign resident payee carries on a business in Australia through a permanent establishment
- payment you make is effectively connected with the payee's business.

This means that the payee will need to include the royalty or dividend payments in the assessable income of the payee's business in Australia.

However, if you are a foreign resident payer carrying on a business through a permanent establishment in Australia and you make royalty or dividend payments to another foreign resident that does not carry on a business in Australia, withholding tax will apply.

See **Subsection 128B(3)** of the *Income Tax Assessment* Act *1936* for more information.

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Withholding rate

Find out about withholding rates for joint accounts and Australian resident living overseas temporarily.

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On this page

The withholding rate is:

- 10% for interest payments
- 30% for unfranked dividend and royalty payments.

These rates apply to all payees **unless**:

- the payment is made to a resident of a country which has a tax treaty with Australia
- a lower rate is specified in the relevant treaty.

If this is the case, the lower treaty rate will apply.

Tax treaties are special agreements that Australia has entered into with over 40 countries and help prevent the same income being taxed more than once.

Joint accounts

If an account is held jointly by a resident and non-resident, the amount of withholding will depend on whether the resident quotes a tax file number (TFN) or Australian Business number (ABN).

If the resident does not quote a TFN or ABN or claim an exemption, the TFN/ABN withholding provisions apply to the total amount of interest or dividends payable to the joint account.

If the resident satisfies their TFN/ABN obligations, non-resident withholding applies to the total amount of interest or dividends paid.

Australian resident living overseas temporarily

If you are an investment body such as a financial institution and you have Australian resident payees who temporarily live overseas, the amounts you pay to those payees are not subject to foreign resident withholding tax if they:

- advise you that they continue to be Australian residents
- provide you with their TFN or ABN.

If they are Australian residents and have not provided their TFN or ABN, you must withhold at the top rate of tax.

See **MIT withholding rules** and **What are tax treaties?** for more information.

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Obligations

Both you and the payee have obligations you must meet with regards to withholding from investment income and royalties.

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On this page

Your obligations

You must:

- withhold tax from the payments you pay to foreign residents
- pay the amounts you withhold to us
- issue **payment summaries** to your payees
- lodge a **PAYG withholding from interest, dividend and royalty payments paid to non-residents – annual report**.

You do not have to lodge this annual report if you have correctly reported interest or dividend payments to foreign residents in an **annual investment income report** (AIIR).

For more information see **Types of payment summary** and **Annual investment income report – Supplier lodgment declaration form**.

Payee obligations

Foreign residents do not have to pay us any more tax if their only Australian income is from interest, dividends and royalties which have had the correct amount of withholding tax withheld.

Foreign resident payees must lodge an Australian tax return if they have assessable income other than interest, dividends or royalties in Australia.

Certificates of payment

A foreign resident payee may require a certificate of payment to provide the tax authorities in their home country.

We will issue a certificate of payment for a foreign resident payee who has had amounts withheld under Australian non-resident interest, dividend or royalty withholding where they require proof of payment to comply with their home country's taxation requirements.

Applications for certificates of payment should be:

- made by the payer who withheld tax from the relevant payments
- completed only if the payee has advised their payer they need to obtain a certificate of payment.

To request a certificate of payment, payers must:

- complete the **Application for certificate of payment** (NAT 6408)
- make the request at the end of the financial year of the country that needs the certificate
- lodge a **PAYG withholding from interest, dividend and royalty payments paid to non-residents - annual report before** applying for a Certificate of Payment.

To meet Australian tax law requirements, a payer will need to provide a payment summary to their payee as this must still be issued in addition to a certificate of payment.

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Our commitment to you

We are committed to providing you with accurate, consistent and clear information to help you understand your rights and entitlements and meet your obligations.

If you follow our information and it turns out to be incorrect, or it is misleading and you make a mistake as a result, we will take that into account when determining what action, if any, we should take.

Some of the information on this website applies to a specific financial year. This is clearly marked. Make sure you have the information for the right year before making decisions based on that information.

If you feel that our information does not fully cover your circumstances, or you are unsure how it applies to you, contact us or seek professional advice.