

## QUESTIONS WE'VE BEEN ASKED

# Deductibility of overseas travel expenses

Issued: 30 August 2022

QB 22/06

This item considers whether income tax deductions can be claimed for overseas travel costs (other than meal costs). It also covers how to apportion costs when only part of the total amount incurred is deductible.

### Key provisions

Income Tax Act 2007 – ss DA 1, DA 2

**REPLACES: Policy Statement “Overseas travel expense claims” published in *Tax Information Bulletin* Vol 7, No 2 (August 1995): 13.**

## Question

Can income tax deductions be claimed for overseas travel costs (other than meal costs)?

## Answer

Income tax deductions can be claimed for overseas travel costs (other than meal costs) but only to the extent that they have a connection with deriving assessable income or carrying on a business.

Income tax deductions cannot be claimed for any part of the costs that are of a private or domestic nature, of a capital nature, or incurred in deriving exempt income or income from employment.

If the costs need to be apportioned between deductible and non-deductible amounts, then this must be done on a basis that is reasonable in the circumstances.

## Key terms

**General permission** a rule in s DA 1 that allows a deduction for costs incurred.

**General limitations** rules in s DA 2 that deny a deduction for costs incurred.

## Explanation

### Scope of this QWBA

1. This Question We've Been Asked (QWBA) discusses the deductibility of overseas travel costs (other than meal costs).
2. It also covers how to apportion costs when:
  - only part of the total amount incurred is deductible under the general permission (s DA 1); or
  - a deduction for part of the amount is denied under a general limitation (s DA 2).
3. This QWBA updates and replaces the policy statement "Overseas travel expense claims".<sup>1</sup> That policy statement stated that when travel relates to a group tour or

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<sup>1</sup> *Tax Information Bulletin* Vol 7, No 2 (August 1995): 13.

conference, tour organisers may apply to Inland Revenue for prior approval of expense claims. This is no longer the case. Unless a taxpayer applies for a private or short-process ruling under part 5A of the Tax Administration Act 1994,<sup>2</sup> current Inland Revenue policy is that no prior approval is available because of the different circumstances of each taxpayer.

4. This QWBA does not consider the following two issues:
  - Whether a companion's travel costs may be deducted by a taxpayer who takes a business trip. This issue is considered in [QB 13/05: Income tax – Deductibility of a companion's travel expenses](#).<sup>3</sup>
  - The deductibility of meal costs. This issue is considered in [IS 21/06: Income tax and GST – Treatment of meal expenses](#).<sup>4</sup>
5. This QWBA addresses the deductibility of **overseas** travel costs only. Although the statutory tests for deductibility apply in the same way to domestic travel costs, more specific provisions may apply to domestic travel costs.
6. For the avoidance of doubt, this QWBA applies to costs incurred by a person on overseas travel that the person takes themselves (that is, costs incurred by a self-employed person who is travelling for the purposes of their income earning activity) and to costs incurred by an employer on overseas travel of employees.
7. Examples of how the law applies are provided at the end of this QWBA.

## Deductibility

8. A taxpayer's overseas travel costs will be deductible if they satisfy the requirements of the general permission. The general permission is satisfied where costs<sup>5</sup> are incurred by the taxpayer and a sufficient nexus or connection exists between the advantage gained or sought to be gained by the costs and:
  - deriving assessable income; or
  - carrying on of a business for the purpose of deriving assessable income.

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<sup>2</sup> A short-process ruling may be a good option in this context. For information on short-process rulings see the IRD website [Short-process rulings](#).

<sup>3</sup> *Tax Information Bulletin* Vol 26, No 1 (February 2014): 40.

<sup>4</sup> *Tax Information Bulletin* Vol 33, No 7 (August 2021): 30.

<sup>5</sup> These rules also apply to losses (eg, depreciation losses), but this QWBA generally refers to costs for ease of reading.

9. To determine whether a sufficient nexus exists, the nature of the costs and their relevance to the taxpayer's income earning process or business must be considered.<sup>6</sup>
10. Even if the costs satisfy the requirements of the general permission, a deduction will not be allowed if one of the general limitations applies. The relevant general limitations are the:
  - private limitation;
  - capital limitation;
  - exempt income limitation; and
  - employment limitation.
11. To decide whether a general limitation applies to a cost, it is necessary to consider the cost from the perspective of the person who incurred it. This involves determining what the person intended to achieve from a practical, business point of view. In doing this, trivial or minor advantages are effectively ignored.<sup>7</sup>
12. The general permission and general limitations contemplate apportionment; that is, part of the costs may be deductible, and part may not.
13. Special rules apply to prepaid travel and accommodation costs over \$14,000.
14. The general limitations, apportionment, and the special rules applying to prepaid costs are discussed further below. This discussion is followed by examples.

## Private limitation

15. The private limitation denies a deduction for costs to the extent to which they are of a private or domestic nature.
16. Costs are of a private nature if they are costs of living as an individual member of society, such as costs for food, clothing, or protective shelter. Costs are of a domestic nature if they relate to the individual household or family unit.
17. Certain kinds of costs have some relationship with deriving income because they are necessary prerequisites, or incidental or relevant to deriving income (for example, travel to a place of work and childcare costs). Despite this, because of the private limitation, such costs are not deductible.

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<sup>6</sup> See, for example, *CIR v Banks* (1978) 3 NZTC 61,236 (CA).

<sup>7</sup> *Cox v CIR* (1992) 14 NZTC 9,164 (HC) at 9,176.

18. It is noted that the private limitation does not apply to companies since they are not natural persons who have need of food, clothing, or protective shelter. Where a company incurs costs on a shareholder or an employee that is of a private or domestic nature for the shareholder or employee, then more specific provisions may apply to the company. Such costs may be:
- deductible wages and salary subject to PAYE;
  - deductible fringe benefits subject to fringe benefit tax ; or
  - non-deductible dividends that may be subject to the imputation credit rules.
19. Also, where a company incurs costs on a shareholder or an employee that is of a private or domestic nature, the amounts involved may be assessable income of the shareholder or employee if they are wages, salary, a dividend or income under ordinary concepts.

## Capital limitation

20. The capital limitation denies a deduction for costs to the extent to which they are of a capital nature.<sup>8</sup>
21. When considering whether the capital limitation applies, the courts have identified various factors that may be relevant.<sup>9</sup> These factors include:
- the need or occasion that called for the costs;
  - whether the costs were of a once-and-for-all nature, producing assets or advantages that were an enduring benefit;
  - whether the costs were expended on the business structure of the taxpayer or whether they were part of the process by which income was earned;
  - whether the costs were made from fixed or circulating capital; and
  - how the costs would be treated under ordinary principles of commercial accounting.
22. If the capital limitation applies to deny a deduction, then the costs may have produced depreciable property and a depreciation deduction may be available instead.

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<sup>8</sup> In *Case K32* (1988) 10 NZTC 286 and *Case L73* (1989) 11 NZTC 1,426 deductions for the cost of overseas travel were denied because of the capital limitation.

<sup>9</sup> See, for example, *Trustpower Ltd v CIR* [2016] NZSC 91, (2016) 27 NZTC 22-061.

## Exempt income limitation

23. The exempt income limitation denies a deduction for costs to the extent to which they are incurred in deriving exempt income.
24. Exempt income includes income derived by a person who is a transitional resident if the income is foreign-sourced and is neither employment income nor income from the supply of services.

## Employment limitation

25. The employment limitation denies a deduction for costs to the extent to which they are incurred in deriving income from employment.
26. This means that if a taxpayer is an employee and incurs overseas travel costs to derive employment income, then no deduction is available to the taxpayer.
27. If an employer incurs the costs of their employee's private overseas travel (for example, as a bonus or reward or as part of the employee's remuneration) then a deduction may be available to the employer. However, as noted when considering the private limitation, more specific provisions may apply to costs incurred by the employer.

## Prepayments

28. Costs are usually deductible in the income year they are incurred. However, where costs are prepaid, deductions may be spread over multiple income years. This applies to advance bookings for travel and accommodation over \$14,000, or to bookings that are for more than six months after a taxpayer's balance date.<sup>10</sup>
29. The deduction is spread by treating part of the prepayment (the "unexpired portion") as income.<sup>11</sup> Then in the following income year a deduction will be allowed for the unexpired portion of the costs.<sup>12</sup> This is repeated, if necessary, until the prepayment has been fully allocated to the income years in which the advantage of the costs has been enjoyed.

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<sup>10</sup> [Determination E12: Persons excused from complying with section EA 3 of the Income Tax Act 2007](#) (Inland Revenue, Wellington, March 2009).

<sup>11</sup> Under s EA 3 (Prepayments).

<sup>12</sup> Under s DB 50 (Adjustment for prepayments).

## Apportionment

30. The use of the phrase “to the extent to which” in the general permission and the general limitations means that apportionment is required in relevant situations.
31. Where two advantages are sought and a general limitation applies to one advantage, then it will be necessary to apportion the costs between the two. The method of apportionment must be reasonable in the circumstances.
32. One way of apportioning overseas travel costs is an apportionment based on the number of days spent on business as a fraction of the total number of days spent on travel. This method was accepted as a reasonable method of apportionment on the facts considered in *Case G5*.<sup>13</sup>
33. The Commissioner will accept other methods of apportionment if they are reasonable in the circumstances.
34. The cost of an international airfare needs to be apportioned where the travel has income-earning and private purposes, and neither purpose is incidental to the other.<sup>14</sup> In a case where the private purpose is incidental to the income earning purpose, a deduction can be claimed for the full cost of the airfare.<sup>15</sup> In a case where the income earning purpose is incidental to the private purpose, no deduction should be claimed for the cost of the airfare. In any case, other costs such as accommodation and local travel may still require apportionment.

## Record keeping and care

35. Because the onus of proof rests on the taxpayer, they will need to retain sufficient evidentiary documents to justify any deduction claimed, including evidence justifying the apportionment of costs. Unless authorised otherwise, records must be kept in New Zealand and in either English or te reo Māori.<sup>16</sup>
36. It is important to be careful when working out what costs are deductible. If a taxpayer claims costs that are not deductible, then, depending on the circumstances, the

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<sup>13</sup> *Case G5* (1985) 7 NZTC 1,011.

<sup>14</sup> *Case G5; Case K48* (1988) 10 NZTC 397.

<sup>15</sup> *Case F152* (1984) 6 NZTC 60,324.

<sup>16</sup> The Commissioner has the discretion to authorise the offshore storage of records or to authorise records being kept in a language other than English or te reo Māori. See s 22(2BA) of the Tax Administration Act 1994. See also [SPS 21/02 Retention of business records in electronic formats, application to store records offshore and keeping records in languages other than English or te reo Māori](#) (6 May 2021).

taxpayer could be liable for shortfall penalties. For more information, see the guidance on Inland Revenue's website on [Shortfall penalties](#).

## Case law examples

37. TRA cases on the deductibility of travel costs include *Case F152* (1984) 6 NZTC 60,324; *Case G5* (1985) 7 NZTC 1,011; *Case K32* (1988) 10 NZTC 286; *Case K48* (1988) 10 NZTC 397; and *Case L73* (1989) 11 NZTC 1,426.
38. Some of these cases concern now-repealed provisions (such as provisions allowing deductions for employment-related costs and export incentives). However, they are still useful for their consideration of different factual situations.

### Case F152 – travel by an employed electrician to do contract work

39. In *Case F152*, the taxpayer was a qualified electrician who carried out electrical contracting work in partnership with his wife. The taxpayer travelled to Australia with his wife for 14 days. The taxpayer spent 4 days visiting the factory that made the electrical units on which he was doing contract work. His wife did not accompany him on these visits.
40. The taxpayer claimed a deduction for two-thirds of the cost of the return airfares for himself and his wife.
41. The TRA accepted that the reason for the taxpayer's travel to Australia was to visit the factory in Melbourne. Had it not been for that reason, the travel would not have been undertaken. The TRA also accepted that the visit to the factory was rewarding for the taxpayer and, in turn, for the partnership business.
42. The TRA held that the cost of the taxpayer's ticket was wholly incurred for business purposes. The TRA saw no justification or ground for an apportionment of the cost of the taxpayer's airfare. However, the TRA held that the private limitation applied to the cost of the wife's airfare.

### Case G5 – travel for both business and private reasons

43. In *Case G5*, the taxpayer travelled to Europe for 42 days. He spent 11 days visiting factories and a motor show and the remainder of his time (31 days) visiting his parents (who were having their 50<sup>th</sup> wedding anniversary).
44. The TRA found that the travel had a dual purpose. The TRA found that:



- the taxpayer would have travelled for private purposes even if not for the purpose of visiting the factories and motor show; and
  - the taxpayer would have needed to go to Europe at some time to visit the firms if he had not done so while on his trip to visit his parents.
45. The Commissioner had argued that no part of the expenditure was deductible because it was all of a private or domestic nature. Therefore, the question of how to make an apportionment was not in issue. Nevertheless, the TRA considered that the cost of the airfares was apportionable and properly apportionable on the basis claimed in the taxpayer's return. The taxpayer had claimed a deduction for \$588, being his accountant's estimate of 11/42 of the total return air fare cost of \$2,354.
46. Having regard to the facts, the TRA considered this amount to be reasonable. The TRA noted that it was based on the time the taxpayer was involved with visiting factories and the motor show during the total period he was overseas. The TRA described this as a commonsense, fair and intelligible basis of apportionment for that case. Therefore, the TRA held that the taxpayer had, on the balance of probability, satisfied the onus of proof of providing an acceptable basis of apportionment.

### **Case K32 – travel to establish a new plant**

47. In *Case K32*, the taxpayers were a manufacturing company and the company's shareholder–managing director. The company manufactured auto electronic devices that its managing director designed for the local market. Among other things, this case concerned the deductibility of overseas travel costs incurred by the company when the managing director travelled to two overseas markets. The purpose was to establish a manufacturing plant for some of the company's products.
48. The TRA held that the principal object of the overseas trips had been to establish new plants permanently where none had existed previously. Hence, the travel costs were of a capital nature for capital development. Therefore, the capital limitation applied to deny a deduction for the costs incurred.

### **Case K48 – travel for business and recreation by married taxpayers and their family**

49. In *Case K48*, the taxpayers were a married couple who had been fully engaged in a family enterprise. Between 1973 and 1977, the taxpayers and some family members had travelled overseas on four occasions – in part for business and in part for recreational purposes. The Commissioner allowed deductions for only 5% of the overseas travel costs as being related to carrying on their business.

50. The TRA held that it was more important to focus on the nature of the costs in the context of the business and to be satisfied that a nexus of “obvious necessity” existed between the costs and the income-earning process. It held that the taxpayers’ claim for overseas travel costs appeared to have been overstated. It also held that the Commissioner’s allowance of only 5% of the costs seemed too abstract. What should have been done was to assess the worth of each trip against the taxpayers’ account of how the time was spent. Accordingly, the TRA held that deductions should be allowed for 40% of the taxpayers’ costs for the 1973 trip, 5% for the 1974 trip, 15% for the 1976 trip, and 5% for the 1977 trip.

### **Case L73 – travel paid for by taxpayer company for employee who was also self-employed**

51. In *Case L73*, the taxpayer was a company carrying on business as a milk vendor. Its main employee and shareholder was also a self-employed engineering contractor who maintained certain machines. The taxpayer paid for an overseas trip for the employee to learn about maintenance of the machines. Depending on the results of the trip, it was contemplated that the taxpayer might commence business maintaining or running the machines.
52. The TRA held that the costs were preparatory to the establishment of a new business venture by the taxpayer that had not previously been involved with the maintenance of machines. Therefore, the costs were of a capital nature and not deductible.

## **Examples**

### **Example 1 - Travel overseas for two purposes**

Gertrude owns a transport business. In May this year she went to Europe to visit her parents on their 50th wedding anniversary and to negotiate contracts for her business. She was overseas for 42 days and spent 11 days on business.

Gertrude would have gone to visit her parents regardless of whether she went over for business. However, she needed to go overseas at some stage during the year for business. Before she left, Gertrude contacted her business contacts overseas and arranged to meet them.

Gertrude travelled overseas for two different purposes. In the circumstances, a reasonable apportionment is to allow a deduction for 11/42 of the cost of the airfare

and allow deductions for the cost of accommodation and meals on the 11 days while she was on business.

### Example 2 - Incidental purpose

Fred is the owner-operator of a hardware store. He was running short of stock, so he went to Australia to buy stock. While there, Fred took the opportunity to spend a day with his old friend Bert. Fred spent a total of three days in Australia, one day on holiday and two days on business.

In Fred's situation, the holiday aspect of the trip is a trivial or minor purpose to the main business purpose. Fred visited Bert only because he was there for business and took the opportunity to see him.

A reasonable apportionment would be to allow a deduction for the total cost of the airfare, and the cost of two days of accommodation for business.

### Example 3 - Employee travel

Eat Auckland Ltd provides hospitality promotion services to Auckland Council. The company decides to send Kasey, one of the company's employees, to Melbourne to run a stall at a food festival to promote restaurants in Auckland.

Kasey is keen to catch up with some mates while she is in Melbourne and her manager agrees to push out the return flight by three days and approve some annual leave.

The company pays for Kasey's return flights and travel costs other than for the extra three days that Kasey is on leave, which Kasey covers herself.

The purpose of the trip was business-related. Although Kasey's manager was happy for Kasey to extend the trip and take some time off, this was not a purpose of the trip.

The company can claim a deduction for the full cost of the return flights and the accommodation costs that it incurred.

#### ***Variation***

Same facts as above, except Eat Auckland Ltd agrees to pay for the cost of Kasey's three additional nights' accommodation as a reward for Kasey's recent good performance. Kasey stays at the same hotel for the whole trip and pays for the accommodation using a company credit card.

In this variation, Eat Auckland Ltd needs to treat the cost of the additional three nights' accommodation as income subject to PAYE in Kasey's pay for the relevant period.

#### **Example 4 - Main purpose of travel is private**

Chris, who lives in New Zealand, owns a rental property on the Gold Coast of Australia. She uses a property manager to look after the tenancy and maintenance of the rental property.

Chris travels to the Gold Coast for her annual holiday. While on holiday, Chris arranges to meet with the property manager at the property for an inspection. Chris hires a car for the day to travel from her hotel to the property.

The main purpose of Chris's trip to the Gold Coast was for a holiday. Chris accepts that she wouldn't have travelled to the Gold Coast just to attend the property inspection.

Chris can claim a deduction for the cost of the hire car for the day. There is a sufficient nexus between this expenditure and her rental activity. However, Chris cannot claim deductions for any part of her airfare to the Gold Coast or for her other holiday travel costs.

#### **Example 5 - Cancellations**

Deborah is self-employed. She had booked and paid for transport, accommodation and conference costs for a business-related conference in France. The conference is scheduled to take place before the end of the income year. Due to unforeseen events, Deborah cancels the bookings for the flights, accommodation and conference. She receives a refund for some of the costs incurred. But she still has \$1,200 of costs that could not be refunded. Can Deborah claim a deduction for these costs?

Despite not being able to enjoy the benefits of the costs, the costs were still incurred by Deborah in the course of carrying on a business for the purpose of deriving her assessable income. In this case, Deborah's entire trip was for the business-related conference. This will satisfy the general permission and no general limitations will apply. Therefore, the \$1,200 of costs are deductible.

## References

### Legislative References

Sections DA 1, DA 2, DB 50, EA 3 of the Income Tax Act 2007

### Case References

*Case F152* (1984) 6 NZTC 60,324.

*Case G5* (1985) 7 NZTC 1,011.

*Case K32* (1988) 10 NZTC 286.

*Case K48* (1988) 10 NZTC 397.

*Case L73* (1989) 11 NZTC 1,426.

*CIR v Banks* (1978) 3 NZTC 61,236 (CA).

*Cox v CIR* (1992) 14 NZTC 9,164 (HC) at 9,176.

*Trustpower Ltd v CIR* [2016] NZSC 91, (2016) 27 NZTC 22-061.

### Other References

[Determination E12: Persons excused from complying with section EA 3 of the Income Tax Act 2007](#) (Inland Revenue, Wellington, March 2009) *Tax Information Bulletin* Vol 21, No 2 (April 2009): 13.

[IS 21/06: Income tax and GST – Treatment of meal expenses](#) *Tax Information Bulletin* Vol 33, No 7 (August 2021): 30.

Policy Statement “Overseas travel expense claims” *Tax Information Bulletin* Vol 7, No 2 (August 1995): 13.

[QB 13/05: Income tax – Deductibility of a companion’s travel expenses](#) *Tax Information Bulletin* Vol 26, No 1 (February 2014): 40.

## About this document

Questions We've Been Asked (QWBAs) are issued by the Tax Counsel Office. QWBAs answer specific tax questions we have been asked that may be of general interest to taxpayers.

While they set out the Commissioner's considered views, QWBAs are not binding on the Commissioner. However, taxpayers can generally rely on them in determining their tax affairs. See further [Status of Commissioner's advice](#) (*December 2012*). It is important to note that a general similarity between a taxpayer's circumstances and an example in a QWBA will not necessarily lead to the same tax result. Each case must be considered on its own facts.