Overseas construction and tax: Where to start?

Mary Nyhan, tax specialist

In the boom times, tax played a key role when dealing with Irish construction activity. Careful structuring led to significant savings and failure to apply Irish tax rules led to costly mistakes. The question arises as to how relevant are tax and financial structures when dealing with international construction projects.

Surely, the tax position is not relevant given that the project is carried on outside of Ireland and all the focus should be on maximising the economic return. In this article, we outline that a simple but well thought out international tax & financial strategy can manage the financial risks of operating abroad and ultimately increase the net after-tax financial returns.

In Ireland, there is a level of certainty when dealing with tax & construction due to well established principles. Does the same certainty apply to international projects? Unfortunately not due to the diversity and complexity of international tax. Also, countries with current construction opportunities are often those carrying the greatest tax risk and uncertainty due to less established regimes which are also ever-changing.

Structure for operations in the local country – local company?

Often in order to establish a presence in a local country, a joint venture with local partners and to qualify for tenders, the inclination is to proceed immediately with the formation of a company in that particular country.

This process can be time consuming when done as one of the first steps of operating in the country and can take the focus from the objective of agreeing the terms of the construction project and building good initial relationships with the client. Also, the benefit of initial losses can be lost for Irish tax purposes.

Hence, it is best to check whether this company requirement is optical or whether actually required. It is often more important to apply care where the political & economic stability of the local country suggests that it may be preferable to retain bank accounts and a legal presence outside of that country.

Whatever financial structure is adopted, it is key that this structure can be amended regularly to reflect the rapidly changing global environment. Funds spent on establishing a permanent & rigid structure at the outset are funds best spent elsewhere. The cost and process for flexing the original structure needs to be considered at the outset.

On the tax side, there are some general principles when deciding on whether to have a local company. For example, if operating in a high corporate tax jurisdiction, there are benefits of a company in the local country in order to establish a corporate veil for the local activities. Another example would be the benefit of an Irish company where there are tax treaties involved and the overseas tax is creditable against the Irish tax.

Separate group from Irish activities

Often the risk profiles associated with Irish and international operations are so vastly different that one needs to go one step further and review the possibility of not just having separate companies but also a separate corporate group for Irish and international operations. The objective in this case is to limit liabilities from the international activities and ring-fence the Irish operations or vice versa.

Even if two groups are involved, it should still be possible to structure the position so that funding/guarantees can be transferred between all companies. In my view, regardless of the tax analysis, the overriding objective of the financial structure chosen is to protect the existing value within the operations.

Where a number of local companies are involved, a holding company would be required in order to link the various companies. Too often, the inclination is to form a holding company in tax havens, which is fraught with difficulty if the strategy for the remission of funds to Ireland along with the complex Irish tax rules dealing with overseas companies held by Irish businesses are overlooked. In addition, the after-tax position needs to reflect any tax cost of remission of the funds to Ireland and unfortunately, this is often forgotten.

Where to start?

The starting point in determining the tax and financial approach is an international strategy which allows finance personnel to balance the tax, financial and HR objectives.

At a minimum, such a strategy will give food for thought on the impact of financial decisions on the after-tax financial return and business risk along with providing a real assessment of the financial success of the overseas operations after all costs (including taxes) are reflected.

The strategy must reflect the actual cash position rather than a discussion of mere principles. Once that strategy is in place, it can be flexed for each new international location and a simple visit to the location is usually the best way to achieve this.

In February 2013, Mary Nyhan established Nyhan Tax Advisers, a boutique firm which specialises almost exclusively in providing tax & financial advice to Irish owned entrepreneurial businesses as they expand.

Mary was Head of Tax for the Mercury Group during the formation of its international activities. Previous roles also include tax partner at RSM Farrell Grant Sparks, Tax Director at KPMG and she commenced her career in the tax department of Arthur Andersen.

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