

Who would want to be a director?

PJ HENEHAN on the Revenue Commissioners' Guidance Note on the treatment of non executive director's remuneration.

The latest attack on the already stressed cohort of non-executive directors was launched recently by the Irish Revenue Commissioners ("Revenue") with the issuing of a guidance note on the treatment of directors' remuneration. The attack on self-employed status follows hard on the heels of greater legal and regulatory burdens designed to "improve standards" and ensure those on boards of companies which are subject to regulatory oversight are limited in the number of directorships they can accept.



The 'essence' of the non-executive director is that of an independent voice on the board - often in a minority of one in the case of unregulated companies. The role of the INED as demanded in the case of regulated entities carries with it strict oversight to ensure that independence is seen to be maintained. Before looking at the recently published Revenue 'guidance' note, the fundamental question to be asked is - how can such a person be regarded as employed under a contract of service? It is a contradiction in terms!

It should be emphasised that Revenue guidance notes are just that! They are not definitive interpretations of the law although they are sometimes worded as if they were. This one is in that category in the writer's view. In fairness to Revenue there is a lot of inconsistency in how non-executive directors structure their affairs. Over the years some myths have become established, including:

1. That a concession applicable to partners in professional firms and whose directors fees were mandated to their firms weren't subject to PAYE/PRSI could apply generally to all so called 'professional directors'.

2. That an individual could supply his own services as a director and that was somehow a separate activity taxable as if he were a sole trader.

3. That in supplying 'his' services in a sole trade capacity it was necessary or even advantageous for the director to register for VAT.

4. That once the director registered for tax as a sole trader and filed his VAT and Income Tax returns on that basis he was 'safe'.

5. That a person who is not resident in Ireland is not liable to Irish tax on director fees or other income.

These myths led to significant inconsistencies in the way directors were treated under the tax code even as between board members of the same company. For example, executive directors (non-proprietary - more on this later) being fully within the PAYE/PRSI system and non-executives ranged from being treated the same to being self-employed invoicing for their services plus VAT or ignoring VAT. Use of service companies by non-executive directors has also become popular where the activity level justifies this. Furthermore in the context of Trust Company Service Providers (TCSPs) the services of non executive directors are routinely provided as part of their ordinary business. While Revenue are justified in seeking to clarify the situation and ensure equality of treatment across the board, they do have an obligation in doing so not to create more uncertainty by pursuing an agenda as opposed to giving 'guidance'.

The agenda appears to be to make 'one shoe fit all' to maximise tax revenues. If everyone adopts fully all the views as expressed in the guidance note, only those entitled to benefit from the concession outlined at point 1 above will be outside the PAYE/PRSI system fully. Proprietary directors (newly defined) will continue to 'benefit' from the self-employed rate of PRSI. Revenue according to the guidance note, are, of the view that even where a director mandates his fees to a service company that they are fully liable to PAYE/PRSI. They are also of the view that where a company supplies the services of an individual as a director (as in the case of TCSPs) that the fees paid for such services are in the nature of directors' fees from an 'office' and are therefore subject to the full rigours of PAYE/PRSI.

There are potentially serious financial consequences arising from all this (the real motive?). Firstly, employers PRSI at the rate of 10.75% gets charged on all fees - at least that is the Revenue view. In this regard there is separately a shift in the

Revenue's attitude as to when a master/servant relationship exists between the employing company and a non executive director. Indeed there is some disagreement between them and other relevant Government Departments on this issue. For a long number of years it has been accepted that a proprietary director is one who held at least 15% of the voting shares. Recently Revenue have been contending that only "controlling" (50 per cent or greater) directors can be subject

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to the self employed PRSI rate. The combined result of all this is potentially a significant added cost for companies employing non-executive directors - the jury is still out as to whether companies will bear this cost or effectively pass it on to directors'/TCSP's.

Apart from the PRSI issue there is in addition the potential for individuals to be taxed on income they do not receive or to be taxed effectively twice on the same amount. On the other hand the question regarding the status of non-residents is at face value simple - if a non resident is a director of an Irish company and they receive remuneration in respect of this 'office' then they are liable to Irish payroll taxes in the same way as an Irish resident and subject to all the same questions and issues raised above. However in addition each such case should be examined by reference to the relevant Tax Treaty or other reciprocal arrangements that may be in place between Ireland and his or her country of residence.

The big question given the Revenue's fairly rigid views on this issue is whether anything can be done? In their guidance note Revenue have made certain assumptions and attempted to create certain impressions which need to be examined closely. The following arrangements are specifically mentioned in the Revenue briefing paper:

- Mandating remuneration in favour of another person
- Contractual restrictions requiring part payment of remuneration to another person
- Payment by means of shares in lieu of remuneration

- Payment by means of benefits in kind to a director *

- Payment by means of expenses (other than reimbursement of actual costs incurred in accordance with Revenue guidelines)

* Payments to a Director include payments to spouses', relatives or other connected persons.

The above could give the impression that it is all embracing as no indication is provided that certain situations which arise in practice are not subject to PAYE/PRSI and USC for example:

- Where fees are waived, for example as The Government have "requested" with regard certain State Bodies

- Where as a matter of course no directors' fees are paid, for example Charities, new companies or companies who are not in a position to pay fees

- Where directors agree between themselves that no fees will be paid

Executive directors often do not get paid directors' fees separate from their ordinary remuneration package (everything is deemed to be included in the package).

In summary there is no law which says a director has to be paid for his services or that remuneration paid to him or someone else for "other" services should be subject to PAYE etc. There is also nothing in law which says that payment for "other" services has in some way to be attributed to directors' fees.

Consider the example of a CEO of a multinational group who as part of his

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duties is required to sit on many boards including subsidiaries based in Ireland. There is no requirement to attribute part of his remuneration to "fees arising from a public office in the state" and subject them to PAYE/PRSI and USC. However if, say, the Irish company paid him directly and that amount was deducted from his overall package then he would be bringing himself within the Irish tax system. A further example relates to TCSPs who as stated

above generally will provide the services of one or more director as part of their suite of services and charge a fixed fee for this service. They will, if Revenue guidelines are not amended, find themselves having to make changes to their contracts or face significant financial cost if they are not able to pass the increased costs on to their customers. Furthermore some service providers do not specifically charge directors' fees but do charge for time spent working for the client by staff including time spent by the "nominated director". The Revenue guidelines appear to suggest that these fees may also be liable to PAYE/PRSI and USC.

I could go on to cite other examples (there are many variations within this same theme), however, the principle point has been established - Revenue has a very narrow view and care needs to be taken regarding the substance and documentation of the relationship between the provider and recipient so that the correct tax treatment is achieved.

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