

Short notes on:

NON-EXECUTIVE DIRECTOR – IS YOUR HOUSE IN ORDER?

Introduction

For many companies, having a board of directors means having both executive and non-executive directors that serve on it. An executive director is also an employee of the company and therefore, can be described as more operationally involved or involved on a more permanent basis with the day-to-day running of the company.

A non-executive director, on the other hand, is involved only in attending directors' meetings. As such, he or she has little or no operational involvement.

These non-executive directors often serve on several boards as experts in their respective fields.

So, the question is – how have they structured their own affairs?

The distinction between an executive and non-executive director from a legal perspective

The question that should be asked is, what is the true nature of the appointment. Are you independent, or are you seen as an employee of the company?

This is an important distinction to be made, particularly from a tax perspective. On the surface of the issue it seems fairly simple. Do you have an employment contract or not? Or stated differently - does your contract outline how independent you are?

A non-executive director is by virtue of the office itself independent of the company. Therefore, if an appointment is made as a non-executive director, he/she would not be subject to any control or supervision of anybody in the conduct of his or her trade.

However, if the lines are practically or contractually blurred – this may cause substantial issues.

SARS

According to Engela Crocker (Directorship Magazine 2017), if the company you are serving as a director is a private company, SARS could easily argue that you are holding an office. Subsequently, SARS can subject you to the limitations imposed by Section 23(m) of the Income Tax Act, No. 58 of 1962 as amended (the "Income Tax Act"). Consequently, this will result in all the expenses claimed against the director's remuneration to be disallowed.

The definition of "trade" is extremely broad and reads as follows:

'Trade' includes every profession, trade, business, employment, calling, occupation or venture...

It is therefore possible that the acceptance of a non-executive directorship could potentially meet the definition of a trade, as set out above.

On the other hand, expenses incurred in the production of the income from that trade, can be claimed in terms of Section 11(a) of the Income Tax Act.

In my view, this should serve as a valid argument for any disallowed deductions. With that being said - a point of contention may be any expenses incurred from home offices.

Home offices

It is not uncommon for a non-executive director to incur home office expenses and these expenses incurred may also be claimed under the general deduction formula of Section 11(a) as aforementioned.

However, according to Crocker, directors should be extremely careful to ensure that the expenditure is indeed truly incurred at the home office.

It is important that the provisions of section 23(b) be noted:

- (a) *Such part shall not be deemed to have been occupied for the purpose of trade unless such part is specifically equipped for purposes of the taxpayer's trade and regularly and exclusively used for such purposes; and*

(b) No deduction shall in any event be granted where the taxpayer's trade constitutes any employment or office unless-

- (i) His income from such employment or office is derived mainly from commission or other variable payment which are based on the taxpayer's work performance, and his duties are mainly performed otherwise than in an office which is provided to him by his employer ;
or*
- (ii) His duties are mainly performed in such part.*

Accordingly, the home office should only be that. For example, a bed or toy storage containers in it could serve as evidence to the contrary and that it would then not be seen to be used exclusively for your trade.

Conclusion

It is important to obtain the necessary legal and tax advice before accepting the appointment as non-executive director. In addition, to have your service level agreement reviewed to ensure that your role and independence is unerringly clear, or even to obtain advice where SARS has already disallowed any deductions. Contact us for assistance today.