


Characteristics, Legal Nature and Taxation of Management Contracts According to the Macedonian Law


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Abstract: Managerial contracts are essentially synthesis of the power of management and the power of the leadership of the company. The conclusion of management contracts is not a simple and routine task which the contracting parties will easily access or, on the other hand, they will assign that task to other (third) persons. With the adoption of corporate decisions by the company, at the moment of appointment to the management body, and thus becoming a member of the body, rights and obligations determined by law arise. In the process of transferring the status powers to the management body or the manager, the owners of the companies or their representatives inevitably have to share a part of the power with the elected managers. The managerial contract is an act of free entrepreneurial will of the two parties that conclude the contract. Thus, this contract regulates the salary, allowances, participation in profit, reimbursement for expenses, reimbursement for life insurance, insurable income, and other employment rights and obligations. On the other hand, managers as individuals facing professional risk are to create a professionally based coalition of interests of all those involved in realizing the company's corporate goals and business policy and thereby enable economic growth and development.

1. Introduction

The problem related to management contracts¹ has become particularly significant and relevant in the last few years. Its actuality comes to the fore especially after the adoption of the new Company Law Act in 2004, which sets the normative foundations for the existence of management contracts in the Republic of Macedonia. Two decades later, the impression is that the research and professional practice related to the issue in question in our country is at a relatively low level.

It is more than clear that the dilemmas in practice were and still are tremendous, starting from the legal nature of management contracts, the content aspect, the determination of the status position of managers, their employment-legal status, taxation of income, insurable incomes, terminological ambiguities and inconsistencies in the laws, the “interference” of laws in the determination of the status position of the managers, the insufficient demarcation of the different echelons of management in the company, etc.

The determination of the type and volume of total income and other rights and obligations arising from the employment relationship of the manager is appropriate to the type and volume of tasks entrusted to and the responsibility of the manager, as well as the manager’s personal contribution to the success of the company’s operations. Accordingly, the application of compulsory and voluntary social contributions and the taxation of personal income differs in some respects from the “normal” employment contract.

For the purposes of this paper, an analysis has been conducted of the legal framework and domestic laws that set the rules and provisions for management contracts. Additionally, a comparative approach will be used to explore the contractual provisions in the manager contract vs the regular employment contract. The historical method will facilitate the chronological analysis of the laws and provisions no longer in force or repealed, with laws in force and enforceable provisions.

¹ In this paper, both terms “manager contract” and “managerial contract” are used without referring to the specifics of these terms used worldwide.

4. Legal Nature of the Management Contract

The status, that is, the position of an executive member of the board of directors, or the member of the management board, is acquired only on a status basis, by a corporate act passed by an authorized body of the company. The financial and material position of the executive member of the board of directors or the member of the management board, is significant for relations that are established on a contractual basis. However, management contracts are not only a legal instrument or a formality with which wages, benefits, rights and obligations are regulated between the contracting parties in relation to the operation of the company and other particulars of mutual relations, but it is a key document in which success depends significantly on the specific job. For those reasons, the Company Law expressly prohibits executive members of the board of directors or members of the management board from entering into an employment contract. With the agreement that regulates the relations between the company and the executive member of the board of directors, or a member of the management board, i.e. the manager, salary, monthly allowance, the right to life insurance and other types of insurance, the right to compensation for travel and other expenses, the right to participate in the annual profit (payment in money, shares, dividends etc.) and other rights can be arranged and determined. With the conclusion of the management agreement, certain obligations established by law arise in the exercise of the authority of the executive member of the board of directors, member of the management board, i.e. of the manager in the interest of the company (managerial obligations), attention to orderly and conscientious trade, keeping of business secrecy during and after the termination of the mandate, prohibition of competition and obligation to disclose conflicts of interests and transactions with interested parties.

While investors and company owners can make decisions based on personal judgments in investing in a business venture, often guided by bare intuition, since they are putting their own funds into the project, and thus taking on their own risk, it is expected of managers that they will assess the sustainability of a given business plan professionally and responsibly, and, based on that assessment, accept or not accept personal involvement in its implementation. That is, in contrast to other

knowledge, skills and abilities that can be relatively easily obtained from the labor market with adequate remuneration, managers have a specific value because they cannot be easily replaced. They do not offer their time at rates according to the company's collective agreements, but what they offer is their entire career, work energy and their ability to concentrate on the prospects of the business venture, while taking personal, professional and legal risks.

Managerial contracts by their legal nature are contracts of autonomous law. It is a special *sui generis* legal institution predicted in the Company Law. In terms of their form and content, management contracts reflect the imperative mandate, i.e. of the business-legal relations of the company and its management, rather than of clearly qualified and measurable proposals for cooperation, on which the established corporate goals, mutual rights, powers and responsibilities are based, including and the remuneration of managers. When preparing and concluding the contract for the regulation of relations between a member of the management body and the company, it is necessary to refer exactly to the legal norm that governs these contracts, in order to know what level of management it refers to. This is of particular importance if it is known that to exercise their powers established by the Company Law, executive members, i.e. the members of the management board, can appoint managers who manage the day-to-day governance of the company in accordance with the decisions, guidelines and instructions of the executive members of the board of directors.

An executive member of the board of directors, or a member of the management board, that is, a manager for the time for which they were elected, can perform the function with or without an employment relationship. When they perform the function based on an employment relationship, they exercise the rights resulting from such a relationship according to the conditions established in the agreement regulating the relations between an executive member of the board of directors, or a member of the management board, i.e. manager and the company, in accordance with the Company Law on Commercial Companies. The provisions of the Law that refer to the executive member of the board of directors and the member of the management board also apply to the manager of other forms⁶ of

⁶ I.e. Limited Liability Company.

6. Parties to the Management Contract

When determining the status of managers in the company, the introduction to the management contract should clearly state the act based on which the decisions for the selection and appointment of the managers are made, i.e. the members of the management body, and the authorization of the person representing the company, the status position of the manager in the company, the contractual powers and limitations in the legal turnover and representation of the company, as well as the general and special acts that determine the rights, obligations and responsibilities of the managers that are not covered by the management contract.

The rights and obligations of the executive members of the board of directors/the members of the management board, i.e. the manager, in addition to the rights and obligations determined by law, can also be determined by an agreement (contract) to regulate the relations between the company and an executive member of the board of directors, or member of the management board, that is, the manager. The Macedonian Company Law determines the parties that conclude the management contract. On behalf of the company, the contract with an executive member of the board of directors is concluded by the non-executive members of the board of directors and signed by the president of the board of directors. In the two-tier system of managing the company, the contract with the members of the management board or the manager is concluded by the supervisory board and signed on behalf of the company by the president of the supervisory board. The board of directors, in accordance with its powers, applies for registration of the executive members authorized to represent the company in the commercial register. The representative of the company is a natural person who, according to the law, is authorized to represent the company. The application is signed by all members of the board of directors unless the members have given written authorization to an executive member of the board of directors to sign it. When registering with the commercial register, the executive members submit signatures certified in accordance with the provisions of the Law. The Law provides continuity in the process of creating management contracts, with their negotiation at the initial stage, followed by the conclusion and signing, and finally application for their registration with the commercial

register. The Company Law stipulates that a company management body can decide to appoint persons with special powers and responsibilities called managers. Managers exercise their rights and obligations in the company according to the conditions established in the agreement regulating the relations between the management body and the managing person.

The contract for managing the relations with managers, which by its nature has all the elements of a management contract, regulates the salary, allowances, participation in profit, reimbursement of expenses, reimbursement for life insurance and other types of insurance, as well as other employment rights. In the content of the contract, the type and amount of total income and other rights of the manager should be determined in great detail, to correspond to the type and volume of entrusted tasks and the responsibility of the manager, as well as the manager's personal contribution to the success of the operation of the company. The success and realization of business policy goals as a motivational set in a company must largely be in accordance with the mutual connection and professional relationship of the two contracting parties and be encouraged in the process of negotiation and conclusion of the management contract. The contracting parties of the management contract create a professionally based coalition of interests of all those involved in the realization of the business policy goals of the company and thereby enable economic growth and development. On behalf of the management body of the company, the contract with the managing person is signed by the president of the management body. The regulation of relations between companies and business persons is largely harmonized with the regulation of this issue applicable in the European Union, and it includes the principles of corporate governance accepted in wider international frameworks.

The problems related to the legal framework regulating relations between the management and the company are covered by different legislations mainly in laws concerning company law. For example, in Serbian legislation, management contracts are governed by the Company Law, the Law on Labour, the Law on Contributions and Mandatory Social Insurance, the Law on Pension and Disability Insurance and other related laws. Similarly, to Serbian legislation, Croatian legislation regulates this issue in the Law on Commercial Companies and other

- state of the ownership structure in the company expressed through the indicators of the capital structure;
- the financial power of the company expressed through the available own sources of financing, income, costs and profitability;
- the organizational complexity of the company's business venture, which can be either a small, medium or large organizational unit;
- the complexity of the production program expressed in the number and types of products, their quality and technical equipment, and
- the position of the company in the market and its competitive position.

The second component for determining the manager's salary represents a set of parameters by which the justification of the company's business policy goals can be expressed. As a set of desired changes, they can be expressed descriptively or with concrete projects in temporal and financial dimensions. Their viability depends on the behavior of the company and its competitive position, the complexity of the market, the quality of the available resources and the content of the production program. The complexity of the manager's role in the company is a significant component in determining the basic salary of managers provided for in the management contract. The attractiveness of the basic salary will also depend on the professional references of the candidate, as well as on the framework and intensity of the responsibilities of the assigned mandate. These factors will equally affect other components for evaluating and determining the salary of managers. However, certain essential rules systematized in several categories are of great importance for determining the salary in the negotiation between the contracting parties before the conclusion of a management contract. These rules say that:

- if the amount of the manager's salary stipulated in the management contract and other permanent compensations is higher, it entails a proportionate reduction of the share of remuneration on account of participation in the profit and shares of the company;
- the manager's salary is not a gift and it should be earned to the extent that the company's business policy goals are met, i.e. by delegating the powers and trust to manage the company's operations, managers invest a lot in the development of their own career and as such have numerous alternatives in the labor market (demand and supply of managers);

- the salary must be sufficiently motivating for the managers to be part of the company's mid-term and long-term development business goals;
- the salary should be a measure of the professional reputation and prestige of managers, which tends to make their salaries proportionate to the position and reputation of the owners of the company in the market;
- the salary should be projected in such a way that it compensates in advance the possible inflation and the rise of living costs during the mandate;
- if the owner of the company offers a relatively low salary to the manager and high expectations for rewards and other benefits, it implies that they are interested in a manager-entrepreneur willing to take business risks, or they believe that the company's business policy goals are easily achievable;
- if the owner of the company offers the manager a relatively high salary and a modest package of benefits, it means that they are interested in a manager-professional not willing to engage in high-risk games who considers that the company's business policy goals are not easily achievable, and
- if the manager accepts a relatively high salary, it leaves them more room in the negotiations for the conclusion of a management contract to better position themselves with regard to the rewards and other benefits arising from the assigned mandate, and above all in the fair participation in the business profits, through different forms of rewards.

The rights of the executive members of the board of directors, and the members of the management board, i.e. the manager, are regulated by a management agreement, according to the type and scope of the entrusted tasks, the work-legal status and their personal contribution to the success of the company's operations. In addition to the right to salary, i.e. monthly compensation, for the work of the executive members of the board of directors, and the members of the management board, i.e. the manager, the assembly can also decide to approve profit sharing.

The approved participation in the annual profit of the company is calculated based on the part of the annual profit that remains after the reduction of the realized profit by the amount of the total losses carried over from previous years and the amounts set aside for reserves.

As mentioned above, the status of the managers is mostly based on dispositive legal rules, which gives the executive member of the board of directors, and the member of the management board, or a manager the right to agree to this position with or without employment status. As mentioned above and prescribed in Article 365 paragraph 2 of the Company Act, “The executive members of the board of directors, the members of the management board, or the manager, shall be entitled to a salary, or a monthly remuneration, right to life insurance and other types of insurance, compensation of travel and other expenses and other rights” and in Article 366 paragraph 2 of the aforementioned Act:

Unless an executive member of the board of directors, a member of the management board, or a manager performs their functions without establishing an employee status, they shall, within the time period they were elected for, exercise the rights arising from such employment status according to the terms stipulated by the agreement regulating the relations between executive members of the board of directors, members of the management board, or manager, and the company.

In both cases, the parties are free to agree upon the duties and rights under the provisions of the Company Law.

If the manager does not have an employment-legal status in the company under a management contract, the tax basis will be the total remuneration, the personal income tax is 10% and usually charged to the company. Income tax is payable by a person on their income earned from various sources during the fiscal year based on their residential status. Macedonian tax residents are taxed on their worldwide income. Non-residents are taxed on their income derived in the territory of Macedonia. “All types of revenues earned in the country and abroad are included in the income”¹² and personal income tax needs to be paid. Personal income tax is paid annually on the sum of the net revenue from all sources, except for the revenues that are tax-exempt under the Law on Personal Income Tax. Those are revenues mentioned in Article 3 of the same Law: personal income from employment, income from self-employment, income from royalties and other related rights, income from sale of own agricultural products,

¹² Article 3, Law on Personal Income Tax.