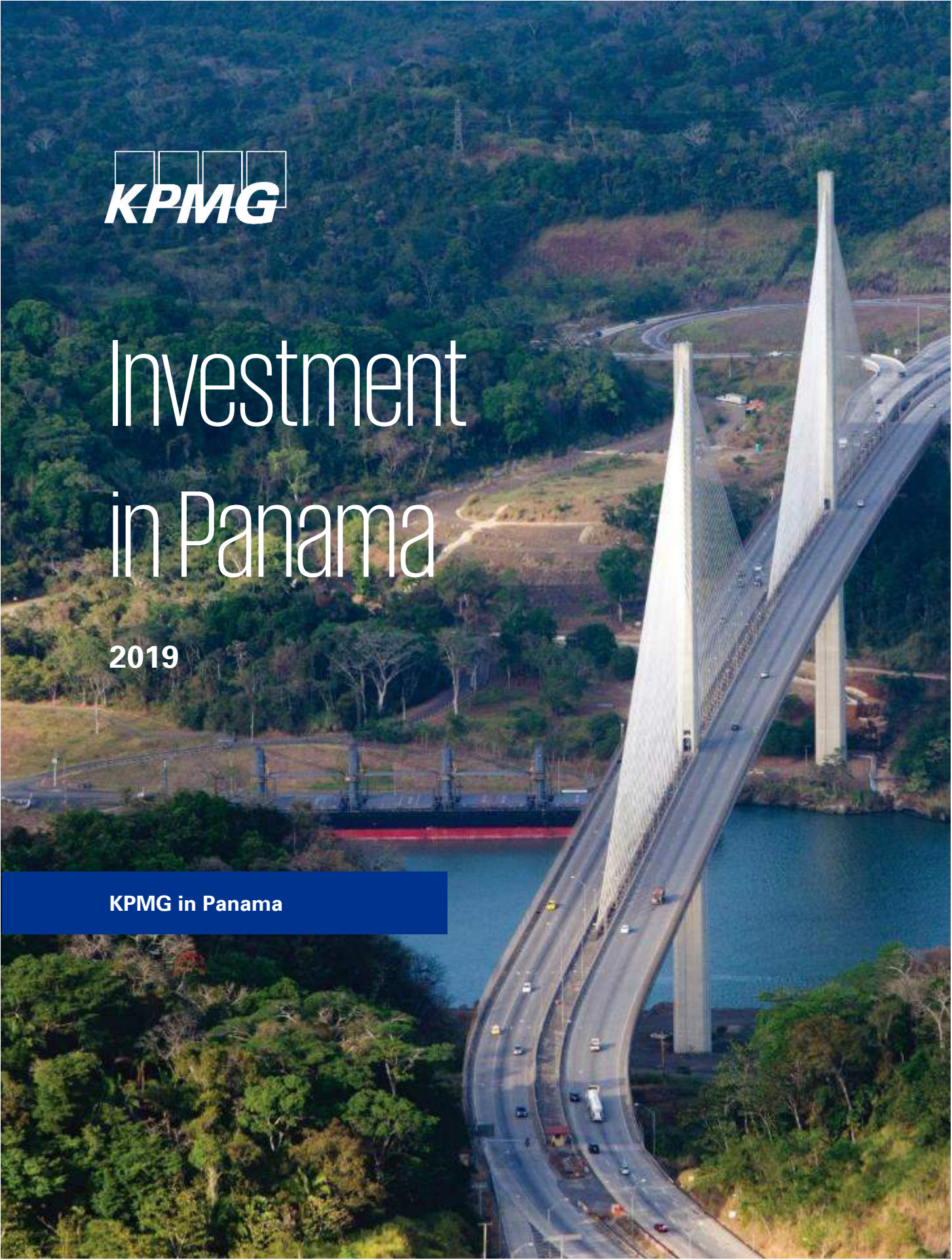




Investment in Panama

2019

KPMG in Panama



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Panama at a Glance

Chapter 1



Chapter 1

1

Panama at a Glance

For over a century, the Republic of Panama has played the role of being a heterogenic, multiethnic country, with a trans-isthmus canal as well as buoyant commercial and financial infrastructures, and has become an emerging tourist destination. Panama is bordered by two oceans and boasts lush tropical rainforests, rivers and national and marine parks with a unique diversity of flora, fauna and sea life, which help to position the country strategically. This is why in native languages, Panama meant “an abundance of fish, birds and butterflies”. Close to this natural scenery is the dynamic and vibrant City of Panama - a modern and cosmopolitan capital, whose coastline is bordered by an ever-growing central business district and a skyline beaming with high-rise offices and residential towers.

Geography and Climate

The Republic of Panama, located between the Republic of Costa Rica and the Republic of Colombia, is indeed at the heart and pulse of the Americas. Panama connects Central and South America, opening its doors and borders for the purpose of doing business, enhancing world trade and uniting people from various countries.

Being a true crossroads, it is only 80 kilometers wide at its narrowest point. Its Caribbean Sea coastline extends 1,287.7 kilometers and its Pacific coastline is 1,700.6 kilometers long. The isthmus has a land mass of 75,517 square kilometers. Panama has a tropical climate throughout the year, with two seasons: the windy season, from January through April, and the rainy season, from May through December. The temperature at sea level averages 27°C to 33°C during the day (80°F to 85°F); however, the temperature is typically cooler and more pleasant at night.

The country lies in a hurricane-free zone and has had relatively few earthquakes or other natural disasters. The mountainous areas and protected reserves on the country’s eastern and western extremities benefit from cooler temperatures. Panama’s official time zone is five hours behind GMT.

History

Panama emerged from the ocean more than 3.5 million years ago, joining North and South America. Before the arrival of the Spanish conquerors, the native people known as “the Cuevas” inhabited this land. Rodrigo de Bastidas is known as the discoverer of the Isthmus of Panama in 1501; some years later, Vasco Nuñez de Balboa led an expedition across the isthmus that discovered the Pacific Ocean in 1513. After other settlements were founded on the Atlantic shore, Panama was the first Spanish village on the Pacific side, established in 1519. The site of this original settlement is currently called ‘Panama La Vieja’ or ‘Panama Viejo’.

In 1538, the village became the seat of the Royal High Court of Panama, and the colonial region was valued not only as the departure point for ships leaving to conquer South America, but also as a trade route from the Peruvian Inca Empire to Spain. It was in 1671 that English pirate

Henry Morgan attacked the City of Panama, burning it to the ground. The City was rebuilt in 1673 in a new site known as 'Old Part of the City' or 'Casco Antiguo' within the district of San Felipe, approximately eight kilometers southwest from the original settlement.

In 1997, both villages, i.e. the 16th and 17th century "Old Parts of the City," were declared a world heritage site by the United Nations Educational, Scientific and Cultural Organization (UNESCO).

Panama remained a Spanish colony until 1821, when it declared its independence from Spain and became part of The Great Colombia. In November 1903, however, after several failed attempts at emancipation during the nineteenth century, Panama broke its alliance with what remained of The Great Colombia, the Republic of Colombia, to become a fully independent republic. More recently, the consolidation of democratic institutions since 1989 has resulted in a sustained reduction of political risk. Government participation in economic activities is limited to regulating the markets and providing social and infrastructure services in areas where private capital is not available. Having been an independent country for more than a century, and given its strong history of openness and dealing with foreign investors, Panama continues to maintain a strong policy of encouraging national and foreign investment.

Government

The Republic of Panama is politically a representative democracy divided into ten provinces and four indigenous reservations. Panama enjoys a presidential system of government divided into three separate branches: the Executive, the Legislative and the Judicial. An independent Public Minister is part of the government structure, headed by an Attorney General. The President and the Vice President (only one Vice President since 2009), who are elected by direct vote for a five-year term, without the possibility of immediate re-election, are currently part of a Cabinet of 15 ministers appointed by the President, which makes up the Executive Branch. They are elected by direct popular vote. The Legislature (National Assembly) is a one-chamber body composed of 71 members who are elected by direct popular vote and who are responsible for passing laws.

The Judicial Branch is composed of nine senior judges appointed to the Supreme Court of Justice, and both the Superior District Courts and other lower courts are established by law. Supreme Court judges are appointed by the President (Executive Branch) and are subject to confirmation by the National Assembly. The Supreme Court of Justice is responsible for the judicial review of laws, and its third chamber reviews the issuance of legal decisions, including for administrative matters.

An independent electoral tribunal governs political elections.

Population, Languages and Religion

Growing at an annual rate of 1.5 percent, Panama has an estimated population of over 4.1 million inhabitants; 40 percent of its total population lives in Panama City, located on the Pacific coast of the isthmus.

The official language of Panama is Spanish. However, English is widely spoken as a second language and a language of business, particularly in the main cities of Panama and Colon. Minority groups speak Arabic, Chinese, French, Greek, Hebrew, Hindi and Italian, amongst others. The literacy rate is approximately 95 percent, and the unemployment rate is 6 percent, according to the Office of the Comptroller General's statistics.

Freedom of religion is enshrined in the Panamanian Constitution, although most Panamanians are Roman Catholics, as declared by the country's Constitution itself. State and religious affairs are kept separate.

General State Budget

Panama's annual budget has various revenue sources: tax revenues are added to non-tax revenues (current income), in addition to capital revenues or state assets. No income could be derogated or modified without proper substitutive revenue authorized by law.

Currency

Panama's official currency is the "Balboa" (B/.) or the Panamanian Balboa (PAB), which has the same value as the US dollar. However, the "Balboa" does exist in the form of coins minted in the same size as US coins. The US dollar is legal tender throughout the country, as stipulated by the Tax Code, and circulated freely alongside Panamanian coins prior to 1903 although legally since 1904, when Panama signed the Monetary Treaty with the United States.

Although Panama has its own currency, it does not have a central bank, like most countries do. The Banking Act amended in 1998, and modified in 2008, organized the Superintendency of Banks, which also functions as a central bank by determining a reserve system and interest rates. Panama enjoys monetary stability as a result of its fully dollarized economy. The state-owned bank, *Banco Nacional de Panama*, is in charge of the supply of US dollars from the Federal Reserve Bank of New York. As the US dollar is legal tender in Panama, it has free circulation and there are no foreign exchange regulations or restrictions on other banks importing US dollars into Panama.

Because of Panama's monetary system, inflation tends to be low. For expatriate executives, the cost of living in Panama has increased in the last five years. Nevertheless, it remains one of the cheapest cities in the region.

Economy

Moodys gave Panama a BAA1 rating in 2019, reflecting a positive outlook. Panama's economy is heavily service-oriented, with more than 70 percent of the Gross Domestic Product and 50 percent of the nation's employment being attributable to this sector.

Panama has been a member state of the World Trade Organization (WTO) since 1997 according to Law 23 of 1997. Due to this affiliation, a number of economic measures have been implemented by successive governments, including the privatization of state-owned companies, compliance of domestic laws with international standards, as well as a drastic reduction in import tariffs and the tariff process in the agricultural sector. The country has signed comprehensive bilateral trade agreements with its major trading partners (e.g. the United States – Panama Free Trade Agreement, in force since 2011), and it has also entered into free trade agreements (FTA) with other important trading partners, such as Canada, Costa Rica, Chile, El Salvador and Singapore, among others.

Taxation System

National and municipal taxes are governed on the basis of the territoriality principle. The national network includes direct and indirect taxes collected by the tax authorities. Meanwhile, authority for municipal taxation resides with the city council of each district, based on its laws.

A broad network of treaties governing the avoidance of double taxation (TDT) under the aegis of the OECD is available. Panama has had a total of seventeen (17) treaties pertaining to avoidance of double taxation (TDT) since January 2018.

Panama has engaged in several peer reviews to align its local systems and legislation with BEPS standards. Some clear commitments on the part of Panama to comply with OECD standards with respect to tax matters and transparency are the signature of the Convention on Mutual Administrative Assistance in Tax Matters (MAC), CRS Multilateral Competent Authority Agreement (CRS MCAA), a Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, and several tax information exchange agreements (TIEA) with other jurisdictions and tax authorities, among others.

Housing

A reasonable selection of executive-standard apartments is normally available for rent. Currently, the market is adequately supplied with rental properties or properties for sale, ranging from studios and lofts to apartments and houses with a garden. These are available, both furnished or unfurnished. Condominiums are being built as second residences for foreigners. Remarkably, housing is growing fast in the trans-isthmus area as well as in rural areas. In 2017, there was a marked decrease in the tax rate for real estate. This reduction represents major savings for real estate owners in Panama. Before the bill was passed in 2017, taxpayers had to pay an amount equivalent to 0.6% of their residential real estate value, from US\$30,000 to US\$100,000. The excess was taxed at 1%. Now the first US\$120,000 are exempted, and an amount equivalent to only 0.5% is payable for values up to US\$250,000. Any amounts in excess of US\$250,000 will be taxed at a rate of 0.7%. For non-residential real estate, owners will pay 0.6% between US\$30,001 and US\$250,000. The tax rate will be 0.8% for values to US\$500,000 while properties valued at US\$500,001 or higher will be taxed at a rate of 1%.

Transportation Infrastructure

Within the City of Panama, a modern metro-bus system is already operational, transforming the public transportation service. Also, the first subway line has been inaugurated, being used by more than 300,000 commuters daily. The second line was inaugurated in April 2019. The third line, connecting Panama City with West Panama province, is the subject of a call for tenders issued by the government. Construction is expected to begin in 2019. Domestic and international cargo transportation services are provided by more than 50 companies based in Panama. Some international cargo carriers offer transportation services on a regular basis to the Western Hemisphere. Most major American car rental agencies operate in Panama. Moreover, Panama is well served by international airlines, with daily flights to major cities in Canada, the United States, Mexico, Central and South America, the Caribbean and Europe from the hub of the Americas at the Tocumen International Airport. Additionally, flights are available to Asia, Africa, Oceania and the Far East. Throughout the country, four international airport projects are being contemplated for the not-too-distant future. A second terminal initiated operations in the Tocumen International Airport which is expected to boost airport traffic. This would allow larger aircraft to land in Panama, thereby creating more opportunities for transatlantic routes flying to and from the airport. During the last five years, transatlantic routes to cities such as Paris, Frankfurt, Istanbul, and Beijing were created. In March 2018, Panama's Tocumen Airport was ranked the best airport in Central America and the Caribbean by Skytrax.

Inaugurated in 1855 and significantly improved during the last decade, the Panama Trans-Isthmus Railroad offers cargo and passenger service, running parallel to the Panama Canal. In addition to the railroad and a huge port to be built in the future (apart from Vacamonte) on the Pacific side, the following five international ports are located near the Panama Canal area:

Balboa (on the Pacific coast as well) and Cristobal, the Manzanillo International Terminal, the Colon Container Terminal and the Colon Port Terminal (on the Caribbean coast).

The Panama Canal, and its expansion

After its secession from Colombia in 1903, Panama signed a treaty with the United States for the construction of the waterway. The Panama Canal Commission was a US Government Corporation (agency) that managed, operated, and maintained the Canal until December 31, 1999, when its administration was transferred to Panama. Since 1914, the Panama Canal has provided transit services to more than 800,000 ships. At least 13,000 ocean-going vessels transit via the Canal every year, at an average of 40 per day.

Since it was handed over to Panama in 1999, the Canal has been successfully managed, operated and maintained by the Panama Canal Authority (ACP as per its acronym in Spanish). The ACP is an autonomous entity of the Panamanian government, which is duly recognized by the Constitution and led by an administrator under the supervision of an eleven-member board of directors, and whose workforce consists of approximately 9,000 people. Following the handover, the ACP assumed responsibility for the modernization of the Canal as well as the protection and conservation of its watershed. The average transit time was formally nine hours. Major improvements have been made since the Panamanian administration took over the Canal, cutting transit time to 7.4 hours. Furthermore, the Canal has experienced an increase in traffic in terms of net tonnage, total transits and transits of Panamax vessels (ships measuring 100 feet or more in beam are the largest that can pass through the Canal), in addition to improvements in workplace health and safety standards.

In June 2016, a third set of locks was inaugurated, after ten years of construction. The first ship that passed through the new set of locks was the Chinese ship called Cosco Shipping. These sets of locks were built for larger vessels, such as the Post-Panamax ships, to pass through, making it possible for more tonnage to transit through the Canal. These sets of locks have doubled the Canal's capacity and significantly increased its earnings by fifteen (15) per cent. The tonnage that passed through the Canal in 2017 increased by twenty-two (22) percent. According to the Canal Authority, 68.3% of the tonnage passing through the Panama Canal originated in or was destined for the United States. The principal users in 2017 were the United States, China, Chile, Japan, Mexico and Colombia.



Businesses

Chapter 2



2

Chapter 2 Businesses

All domestic and foreign businesses have equal rights under the Panamanian Constitution and must fulfill the same basic requirements to organize and carry on business activities in Panama. However, there are restrictions for foreign companies operating retail trade activities as well as certain professional practices. Individuals may engage in business activities under their own names or through legal entities.

Types of Legal Entities

The following are the different types of legal entities that may be formed, based on Panamanian civil and business laws. A foreign entity may also re-domicile in Panama or open a Panamanian branch.

Partnerships

- General partnerships (“sociedades colectivas”): Partners’ responsibilities are unlimited, unless the partnership agreement provides that a partner will be liable only for a limited sum (which cannot be lower than the contribution to the partnership).
- Simple limited partnerships (“sociedades en comandita simples”): Limited partnerships with general and limited partners. General partners share management responsibilities and are jointly and severally liable for partnership debts. Limited partners are liable only up to the amount of capital that they have invested.
- Joint-stock partnerships (“sociedades en comandita por acciones”): Limited partnerships, similar to simple limited partnerships, but with the partners’ capital represented by shares.
- Limited liability companies or LLC (“sociedades de responsabilidad limitada”): Under this form of organization, the liability of shareholders is limited to the individual capital invested. The name of the partnership must include the words “Sociedad de Responsabilidad Limitada”, the initials “S. de R. L.”, or the abbreviations “Sdad. Ltda.” or the partners’ liability will be unlimited.

Joint Ventures

- Joint ventures (“asociaciones accidentales o cuentas en participación”): This type of partnership is used for temporary associations for business purposes without incorporation. Joint ventures are widely accepted in Panama although they have no separate legal registry.
- Therefore, in order for this type of association of persons to carry on a single business enterprise for profit, the Directorate General of Revenue may assign a tax number to joint ventures for payment of taxes.

Private Interest Foundations

As per Law 25 of 1995, Panamanian legislation created a new type of entity known as a private interest foundation, inspired by Liechtenstein's Family Foundation Law.

- Private interest foundations shall not be profit oriented.
- They may nevertheless engage in commercial activities in a non-habitual manner or exercise rights deriving from titles representing the capital of business corporations held

as part of the assets of the foundation, provided that the economic results or proceeds from such activities are used exclusively towards the foundation's objectives.

- The law also allows that one or more natural or legal persons register under their own name, or through another, to incorporate a private interest foundation.
- A private interest foundation may be formed with an amount of no less than US\$10,000 in authorized capital.
- The founders must select a name to identify the foundation.
- The objectives, term, place of domicile, and board of the foundation must also be indicated, along with the names of beneficiaries.
- The foundation's charter must be notarized and registered.
- The private interest foundation is very similar to a trust in its operation, but unlike the trust, there is no need to transfer the assets to a third party.
- Where foundation assets are located outside of the territory of Panama, no taxes are levied when these assets (whether movable or immovable property, shares, bonds, etc.) are transferred.

Corporations

- Two or more persons, either Panamanian or foreign nationals, may establish a local corporation known as a "sociedad anónima" (stock company) in Panama.
- Corporate law does not require any minimum paid-in capital.
- Bearer shares are not allowed for incorporations after December 31, 2015.
- A single person or a corporation may own all shares.
- Under corporate law, every corporation must prepare the articles of incorporation (pacto social) and register by way of a public deed before a Panamanian notary.
- The public deed must then be registered in the Mercantile Section of the Public Registry.
- The usual procedure is for two attorneys within the same law firm to incorporate the company and then assign their rights to their clients.
- The identification of the shareholders need not be disclosed in the articles of incorporation, save for exceptions.
- A lawyer as resident agent is needed.

Legal Requirements for Incorporation

Law 32 of 1927 and its amendments regulate corporations. The following requirements must be satisfied in order to incorporate a company in the Panamanian Public Registry:

- Panamanian law requires registration of a name for the corporation.
- A statement of the main objectives of the corporation is required, although the law entitles the corporation to perform any legal business other than the specified principal objective.
- Disclosure of information regarding the amount of authorized capital is required, including the number of shares.
- In the event of shares without par value, information regarding the amount of authorized capital, including the number and nominal value of shares, is required.
- No minimum or maximum capital is required to commence operations.

Share Structure

- Under Panamanian law, shares may be issued with or without par value.
- These shares may be of different classes and have different values and rights.
- Also, shares may be issued in a nominative form, bearer form or both.

Identity of Directors

- Panamanian law requires a minimum of three directors, with no restriction on a maximum number of directors.
- The full names and addresses of directors must be provided.
- Citizens from any country may be appointed as directors.
- Also, legal entities (legal persons) may act as directors for a corporation.

Identity of Corporate Officers

- The full names and addresses of corporate officers must be provided.
- Panamanian law requires a president, secretary and treasurer.
- The same person may hold more than one position. For practical purposes, it is not recommended that the same person be appointed as President and Secretary.

Term and Place of Domicile of the Corporation

- The corporation may exist for an indefinite period.
- The place of domicile may vary although it is usually in the Republic of Panama.

Resident Agent and Annual Tax Fees

Panamanian law requires every corporation to hire a local attorney acting as resident agent of the corporation. Fees for this service start at US\$250 per year. Additionally, there is an annual franchise duty of US\$300.

Procedures

The procedures to establish a Panamanian corporation are as follows:

- The required information is provided to the resident agent.
- A corporate charter must be drawn up by the resident agent (articles of incorporation). A notary public must notarize this charter.
- The notarized document will be registered in the Public Registry of the Republic of Panama.
- The resident agent will prepare share certificates and the legal books of the corporation.
- Foreign corporations may be registered in Panama. In such cases, documents certifying the authenticity and good standing of the corporation are requested. These documents have to be certified by the Panamanian Consul at the place of origin.

Registration Fees

Registration fees vary according to the registered authorized capital, as follows:

Authorized Capital	Registration Fee
For the first US\$10,000	US\$50
For each additional US\$1,000 or fraction	US\$0.75

Accounting Requirements

- All companies operating in Panama are required by law to maintain accounting records according to generally accepted accounting principles in the Republic of Panama, i.e. International Financial Reporting Standards (IFRS), or NIIF as per the abbreviation in Spanish.
- The following records are required for corporations operating in Panama: a general journal, a general ledger, a minute book, and a stock register (shareholders registry). Only two books are mandatory for merchants: a general journal and a general ledger.
- All accounting records must be maintained in Spanish.
- Accounting records, supporting documents and correspondence must be kept in Panama, as long as the operations are carried on locally. They must be up to date and ready to be inspected by authorities at any time.
- According to the Business Code, endorsement by a certified public accountant is required when capital exceeds US\$100,000 or the sales volume is over US\$50,000.
- For companies engaged exclusively in offshore operations, the legal and accounting records must be maintained with the resident agent or this person has to be informed of the location of those documents.
- For all companies operating in the Republic of Panama, tax regulations require taxpayers to maintain the financial statements available to the Directorate General of Revenue and attested by a certified public accountant in accordance with generally accepted auditing standards in Panama.
- Although not required, financial statements can be registered in the Public Registry of Panama.
- There is a statutory audit requirement in Panama for banks, insurance companies and reinsurance companies, as well as for companies registered under the National Securities Commission as well as companies operating in a free trade zone. The financial statements of these entities must be certified annually by independent auditors.
- When the accounting records are maintained via technological or electronic means, specific certification from a certified public accountant is required.
- Accounting records must be prepared according to the accrual basis of accounting in accordance with International Financial Accounting Standards (IFAS), with few exceptions.
- Banking institutions are authorized to maintain their accounting records in accordance with either IFRS or US GAAP.

Legal Entity Annual Franchise Duty

- Every registered corporation, limited liability company or any other legal person, domestic or foreign, must pay to the Treasury an annual tax of US\$300 (*"tasa única anual"* or TUA).
- Private interest foundations must also pay this annual tax, but the applicable fee is US\$350.00 for the first year and US\$400.00 for all subsequent years.

- Notwithstanding non-profit or non-governmental organizations (NGOs), cooperatives and civil partnerships are exempted from TUA. Civil partnerships were required to pay for a specific period (between 2009 last semester and 2010 first semester). Refer to Executive Decree 539 of 2011.
- The law states that penalties shall be applied when the fee is not paid for two consecutive or alternate periods.
- Under Law 52 of 2016, legal entities which do not pay the annual franchise duty for three consecutive years/periods will be sanctioned, with the suspension of their corporate rights.
- Payments should be made by the legal representative or registered/resident agent.

Notice of Operation

To engage in commercial or industrial activities, all corporations, partnerships, or individuals must obtain a permit, called the “notice of operation” (in Spanish, *aviso de operación*). The application for and granting of the notice of operation is done through an electronic system, www.panamaemprende.com, with the Ministry of Commerce and Industries. Law No. 5 of 2007 regulates this matter.

Process for Obtaining a Notice of Operation

- All enterprises doing business in Panama are asked to adhere to the following procedure in order to obtain a notice of operation, in addition to specific procedures for each of the field activities:
- Previous authorization must be obtained for certain activities before receiving the notice of operation.
- Registration of activities must be completed in the *Panama Emprende* system.
- All taxes, fees or contributions must be paid.
- The system will issue the number of the notice of operation, which includes a code number and the tax identification number (or RUC, as per its acronym in Spanish).
- The RUC must be used for payment of all taxes (central and municipal taxes).

Procedural Requirements

In order to begin the procedure, the users’ registry must be submitted, after which the following steps must be completed:

- Filing of a request form, including necessary information to identify the applicant, such as the name of the establishment, the name and address of the person requesting the notice, as well as the capital and activities in which the company will be involved.
- A sworn declaration must be attached to the notice.
- A fee of US\$15 for natural /individual persons or of US\$55 for legal entities must be paid.
- An additional cost for obtaining a business notice depends on the activity.
- There are two types of activities to conduct business: commercial or industrial.

Industrial Activities

Industrial activities are described as extractive and manufacturing activities. Such activities include the wholesale and retail sale of products to the government; construction companies hiring workers; manual, homemade and handicraft industries employing more than five workers.

Wholesale Business

According to Law 5 of 2007, “wholesale business” is defined as follows:

- The performance of services in general, except those qualified as retail operations under current legislation.

- Sales to the government and to businesses.
- The performance of all types of commercial activities, with the exception of those qualified as retail operations.
- Examples of wholesale business activities include commercial and mortgage banks, financial companies, international financial brokers, insurance and reinsurance companies, international transportation agencies, mutual funds, public utilities, and high technology service companies.

Retail Business

According to Law 5 of 2007, retail business includes:

- Sales of goods to consumers.
- Representation or agency of a producer or mercantile business.
- Any other activity qualified as such under the law.
- According to the Constitution, only Panamanian citizens are permitted to carry on a retail business activity and foreigners may be individually authorized to do so or be incorporated as a manufacturing business.

Activities exempt from the notice of operation

- Exemptions from the business notice registry are granted to natural/individual persons or legal entities engaged either in agricultural activities or in the handicraft business or producing homemade goods with no more than five employees.
- Non-profit associations such as those engaged in charitable activities do not require a business notice of operation either.
- A free trade zone company is also exempted.

Other Approvals and Licenses

- Among other activities, banks and trust companies must obtain operating licenses from the Superintendency of Banks.
- Insurance companies, insurance brokers, reinsurance companies, reinsurance brokers, captive insurance companies and insurance administrators must also obtain authorization from the Superintendency of Insurance and Reinsurance.
- Securities brokers must obtain licenses from the National Securities Commission.

Commercial and Industrial Protection

Product Registration

- In general, all food products and beverages sold in cans, bottles or any other form of packaging should be registered with the Ministry of Public Health and must comply with hygiene and quality control standards.
- Importing food products into the Panamanian territory is prohibited, if the products are not authorized in the country of origin.
- The Executive Branch is responsible for creating sanitary regulations at the request of the Ministry of Public Health, regarding the manufacturing, warehousing, importation, and sale of medicines and related products.
- These products cannot be manufactured in or imported into the country without prior analysis and registration.
- In the case of foreign products, a certificate of free sale issued by the sanitary authority of the country of origin, authenticated by the Panamanian Consul, should be included with the application for sanitary registration.
- The National Authority of Food deals with new imports.

- Based on Law Decree 11 of 2006, it is responsible for introducing and managing food security standards in the country.

Patents

- Law 35 of 1996 and Law 61 of 2012 enacted a substantial reform for the protection of industrial property in the Republic of Panama.
- Panamanian law protects and recognizes the right of the author of any invention, through a patent of invention license issued by the Ministry of Commerce and Industries, which will assure the inventor of the exclusive rights to use the invention for a period of twenty years.
- No patent will be issued if it creates conflict with previous acquired rights.
- Patents will be cancelled when they are issued to the detriment of third parties' rights, or when they are not used.
- Inventors who have obtained patents in other countries can obtain a corresponding patent of invention in Panama, provided that the inventions are not in the public domain.

Trademarks

- Trademark protection for products and services underwent substantial reform in Law 35 of 1996 and Law 61 of 2012 mentioned above. This legislation updates industrial property protection and complies with international standards and treaties in this area.
- Trademarks may be represented by a word, a phrase and a symbol, or a combination thereof, or any other means capable of individually identifying a product or service in business.
- They should be sufficiently different one from the other, so that a given trademark can be clearly distinguished and no confusion arises in the course of its use.
- Any owner of a trademark, either a foreign national or a Panamanian citizen, may request registration with the Ministry of Commerce and Industries, in order to acquire the exclusive right to use it in the Republic of Panama.
- The application should be published once in the Industrial Property Bulletin, and if after two months (60 days) from the date of publication, no claim to the contrary is filed, registration of the trademark shall be made.
- Registration is granted for a ten-year (10) term, renewable for equal periods of time, provided that the renewal is requested a year in advance or six months following the date of expiration. If renewal is not requested within the period of time specified above, the registration will be cancelled and the rights acquired will be lost.

Copyrights

- In addition to the international agreements approved by Panama, Law 15 of 1994 was issued to protect the intellectual property rights of literary, educational, scientific or artistic works regardless of kind, manner of expression, merits or destination.
- Proof of title to the work is required by law, but the work need not be registered to obtain the protection granted by the law. The author is recognized unless the contrary is proven. The author is basically granted moral and patrimonial rights.
- The copyright is granted to the author while the person is alive and to heirs for a fifty-year (50) period after the person's death.

Electronic Commerce and Related Issues

The Law 51 of 2008 defines and regulates electronic documents and electronic signatures and the provision of storage of technological documentation as well as certification of electronic signatures. It includes other provisions for the development of electronic commerce.

This law confers jurisdiction of the Directorate General of Electronic Commerce (located at the Ministry of Commerce and Industries) to regulate this area as well as to register the service providers regarding certification of storage (or file) technology (or digital) of documents, while the Public Registry is the authority in charge of regulating and certifying the electronic signature in Panama, according to Law 82 of 2012, which amends various provisions of Law 51 regarding this matter.

One of the particularities regarding Law 51 is that it allows all traders keep their accounts using books, electronic documents or other legal means that always ensure that such records cannot be modified or subsequently eliminated, including in the Panamanian law in 2008. Electronic documentation is valid, without the need for printed accounting records, as adopted in 1997 under commercial law (article 71 of the Business Code).

Also, Law 51, referring to the commercial transactions carried out via Internet, makes use of electronic invoices for which terms and conditions are determined by the government, through the tax authorities (Directorate General of Revenue or DGI), which, to date, has regulated electronic invoicing through the tax provisions on the basis of Law 8 of 2010 and Law 72 of 2011.

Since 1996, prior authorization by the DGI has been required to use any computerized billing system (based on Executive Decree 26 dated February 1, 1996).

On the other hand, the Ministry of Commerce and Industries (MICI) has begun using the Web to obtain the information required for the registration certificate at no cost to the users to allow MICI officials accredited in the Public Registry (PR) to verify any information in the PR required by the MICI.

On October 17, 2018, through Resolution JDN006-2018, the Colon Free Trade Zone created the Operating License, for companies who sell goods through electronic commerce.

Bookkeeping

Panamanian business regulations require that accounting records be kept on file for at least five years. Documentation supporting the accounting records and transactions, such as invoices issued or received, withholdings made, etc., must be retained for a period of time similar to the statute of limitations for any action that could arise therefrom. However, information regarding social security contributions should be kept for at least 20 years according to the Social Security Act. Thus, it would be advisable to list the supporting documentation in order to establish the need to maintain the different documents on file, on a category-by-category basis. Electronic filing is mandatory, with a few exceptions, and is authorized by the administrative tax authorities.

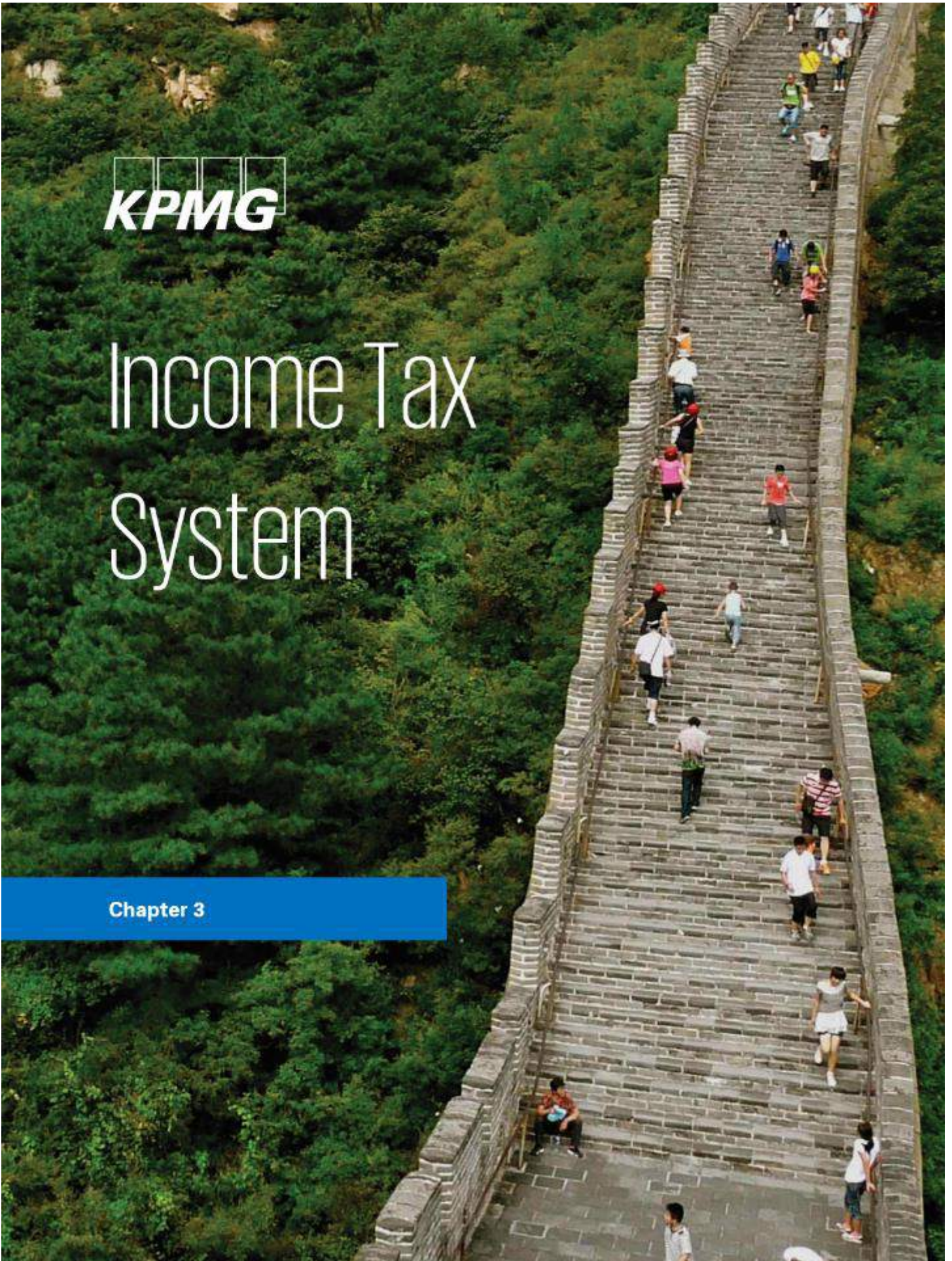
A chart summarizing the statutes of limitations is presented below, setting out the rights, duties and obligations of business people, merchants, employers and taxpayers to maintain records.

Bookeeping and Statutes of Limitations	
Topic	Time (years)
Constitutional limitation period for redeeming bonds	20
Social security matters	20
Taxation (general rule)	15
Withholding income tax	15
National Treasury debts and credits	15
Real estate tax collection	10
Income tax collection and refunds	07
Income tax assessments	03
Income tax credit (to be refunded in cash)	03
ITBMS (or VAT)	05
Commercial matters (general rule)	05
Accounting records (retention period after closing)	05
Auxiliary records (retention period after closing)	05
Technological storage of documents	Same



Income Tax System

Chapter 3



Chapter 3

3

Income Tax System

Overview of Panamanian Tax System

It is a fundamental constitutional principle in the Republic of Panama that no tax, duty or contribution shall be levied unless such tax has been legally established through the enactment of a law ratified by the National Assembly, following the Roman aphorism that reads 'no tax without law' ("*Nulle taxe sine lege*").

The Supreme Court of Justice oversees constitutional control through the judicial review of laws and rulings and has a crucial role in providing certainty to the legal system. The Third Chamber of the Supreme Court or Chamber III, for its part, oversees legal control over administrative acts, e.g. tax matters.

As a national tax, income tax is covered by the Tax Sections of the Tax Code and some other laws. Hereinafter this document will refer to 'Tax Code' when addressing the Tax Sections of the Tax Code.

Basic Principles in Levying Income Taxes

Territoriality principle

The Republic of Panama bases its income tax system on the territoriality principle, as opposed to the worldwide taxation method used in most countries. This means that all income derived from local (or domestic) operations is subject to income tax while income arising from foreign sources is exempt, as is any other income specifically exempted under the Tax Code or special tax legislation.

According to the territoriality principle, income produced in Panama, or considered to be Panamanian sourced, is taxable regardless where the contracts are signed, where the amounts are paid, or the place of domicile or nationality of the parties involved. Thus, given how the Panamanian tax system is structured as a governing set of laws, residents and non-residents are taxed on Panamanian-source income.

Sources of Income

Our territoriality principle divides the income accrued by individuals or legal entities by their source: i.e. local, foreign and exempt income. General provisions regarding sources of income are set out in the Tax Code and more specific provisions can be found in Executive Decree No. 170 of 1993.

Local/domestic (Panamanian-sourced) Income

The following income is considered to be Panamanian-sourced income:

- a) Generated from civil, commercial, industrial or similar activities, and from working in any professional field, or other occupations and all services performed, carried out or fulfilled within the territory;

- b) Generated from international transportation activities on the portion that corresponds to freight, passenger tickets, cargo and other services whose origin or destination is Panama, regardless where the company is incorporated or domiciled;
- c) Remuneration of personnel working within the Panamanian territory, regardless whether they work in free zones or for entities receiving foreign source income;
- d) Remuneration of personnel working at diplomatic or consular Panamanian missions;
- e) Revenue from real estate property located in Panama;
- f) Revenue produced by goods or rights used economically in Panama as well as capital and securities invested economically in Panama;
- g) Net income obtained by communications and telecommunications companies on the portion that corresponds to the telephone calls and/or any other transmission or receipt of sound or images;
- h) Insurance companies (insurance and re-insurance operations covering domestic risks);
- i) All income received by individuals or legal entities not domiciled in Panama that arises from any service or action that benefits persons in Panama is considered to be Panamanian-source income, including fees, copyrights, royalties, goodwill, trademarks, patents, know-how, as well as industrial or commercial secrets. The amount should be considered as an expense by the person receiving such services in Panama. The amount of taxes to be withheld for remittance is based on one-half of the sum remitted at regular rates for legal entities and natural persons respectively (refer to sections 699 and 700 of the Tax Code).
- j) Within a free zone, transfers of any securities, goods and real estate property , including rentals;
- k) When the final destination is within the Panamanian customs territory, all income received from storage, bond, internal moving of merchandise and cargo, invoicing, repackaging, etc., including commissions for services to entities or individuals established in any free zone;
- l) Any income not contemplated above that constitutes civil or natural yield, as long as it is earned within Panama, either by the use of goods or the provision of services.

Foreign-source Income

Income earned either from an activity or a transaction performed abroad is considered foreign-source income under Section 694, Paragraph 2 of the Tax Code, which reads as follows: “*Any income arising from the following activities is not considered to be earned within the territory of the Republic of Panama*”. The following is not Panamanian-source income:

- (a) Income from invoicing sales, merchandises or products for amounts greater than billed costs from an office in Panama, provided that the merchandise or product does not enter Panama;
- (b) Income from carrying out transactions which are completed or produce effects outside of Panama from an office located within Panama;
- (c) Dividends and other profit distributions from legal entities that do not require a notice of operation or do not generate taxable income, when such dividends or profits are paid out of income not produced in Panama, including income from activities mentioned in paragraphs (a) and (b).

Briefly, clarifying the rules for income tax purposes and according to Executive Decree 170 of 1993, income derived from the following activities is not considered income earned within Panama or derived from Panamanian sources. Therefore, such income is not subject to income tax.

- a) Invoicing from an office in Panama for the sale of merchandise or products for a sum exceeding the amount invoiced to the office established in Panama, provided that such merchandise or products are only transferred abroad or are in transit through national ports or airports;
- b) To direct, from an office established in Panama, transactions that should be completed or carried out abroad. Bearers of a temporary special visitor's visa (TVSV) to work in Panama are included for foreign-source income;
- c) The provision of services, outside the Panamanian territory, when they are not economically related to taxable activities that the taxpayer performs within the national territory;
- d) To distribute profits or dividends from legal entities that do not require a notice of operation, permit, registry, license or any other authorization for operating in the Colon Free Zone or in any other free zone or do not generate taxable income in Panama, when such profits or dividends are derived from income not produced within Panama;
- e) Interest, financial commissions, and other similar receipts, obtained by an individual or a legal entity, regardless of their place of domicile (where they reside) or of incorporation, derived from loans, cash deposits, or from any other financial transaction carried out with borrowers outside the country. The provision and use of the cash, however, must take place outside of Panama, even if the capital and interest are reimbursed within in the country;
- f) Interest, financial commissions, and other similar receipts, derived from loans, credits, or from any other financial transaction carried out with legal entities, regardless of their place of domicile (where they reside) or of incorporation. This includes life annuities, old-age or disability retirement pensions or other similar revenues granted abroad as long as the beneficiaries only receive non-taxable income within Panama, including non-taxable income derived from interest, financial commissions, etc., that may be received;
- g) Income from freight, passenger tickets and passenger or cargo-in-transit services as well as income derived from maritime passenger tickets and other services obtained by cruise companies as long as their home port is Panama (even though international transportation is taxed on the portion corresponding to freight, tickets, cargo and other services whose origin or destination is the Republic of Panama);
- h) Trusts ("fideicomisos"), established under Law 1 of 1984 in regards to properties abroad, cash deposited by an individual or a legal entity, whose income is not of Panamanian source. Stocks or securities of any kind, issued by companies whose income is not of Panamanian source, regardless whether the cash, stocks or securities are deposited in the Republic of Panama;
- i) Rental payments under leases that are paid to the lessor in the case of international financial leasing contracts, which are referred to in Law 7 of 1990;
- j) Premiums derived from insurance and reinsurance contracts that cover personal or property risks abroad as well as reinsurance premiums being ceded to companies located abroad;
- k) The disposal of stocks and shares of legal entities formed, under the laws of the Republic of Panama, when the activities of such entities are carried out exclusively outside of the Panamanian territory;
- l) Payments to non-residents engaged in international business activities, such as those related to hotels and car rental companies, ship and aircraft repairs, freight on account of international shipping agencies and international tourism operators, insofar as goods or services payments are financed, contracted or executed abroad;
- m) International business activities, as long as foreign operations are needed to generate income declared in Panama, provided that goods and services payments are financed, contracted or executed abroad;

- n) Cruises operated by foreign parties generating profits of the sale of passenger tickets, tour excursions in Panama driven by third parties in Panama, marketing on board by companies established in Panama, services to passengers in waterways and ports, or payments received when disembarking at Panamanian ports.

Tax-exempt Income

The following is a list of Panamanian-source income exempt from income tax.

- Income derived from freight, tickets and services to passengers or cargo in transit in the territory of Panama, as well as income from tickets and other services provided by cruise ship operators whose home port is Panama;
- Income from the embarkation, disembarkation, or both, at a Panamanian port, by passengers on vessels crossing national waters, or through the Panama Canal;
- Income from the disposal of ships or aircraft registered in the National Merchant Marine or in the Panamanian Registry Office, engaged in international trade;
- Income from the operation of vessels or aircraft registered in foreign countries, if the country in which such vessels or aircraft are registered applies the principle of reciprocity, with regard to the taxation of income obtained in said country by vessels registered in the Panamanian Merchant Marine or aircraft registered in Panama;
- Income from the operation of ships or aircraft of any nationality, by foreign persons whether or not resident in the national territory, provided that the country of nationality of the individual, or the country under whose laws the legal entity was formed, grants an equivalent exemption to individuals of Panamanian nationality, or to legal entities formed in accordance with the laws of the Republic of Panama, or to persons who have elected domicile in the Republic of Panama, by virtue of the principle of reciprocity;
- Income from rentals under leases, derived from international financial leasing contracts, and from merchant ships or aircraft engaged in international maritime trade;
- Interest and commissions paid, or credited by banks established in Panama to international banking or financial institutions established abroad, for inter-bank loans and credit facilities;
- Interest paid on local or foreign savings accounts and term deposits maintained in banking institutions established in Panama;
- Interest paid to persons or corporations on loans to finance the construction of social housing units, as determined by the Ministry of Housing;
- Income from interest that national or foreign banks receive or accrue, derived from loans granted to farmers in Panama, within the planting cycle. The proceeds from these loans are to be used in the planting of rice, corn, beans and sorghum, with an interest rate no greater than eight (8) percent per year;
- Income from interest, commissions, and other expenses that the government and autonomous public entities contracted by way of loans;
- Interest and commissions earned by banks and financial or credit institutions, in respect of loans or other credit facilities, granted to the agricultural, livestock, or agricultural industry sector, provided that the legislative requirements have been met;
- Prizes paid by national lotteries, or in raffles, bets and games of chance operated by the government or by non-profit entities duly authorized by the Gaming Board of Control, as well as prizes obtained in contests or events held for publicity purposes;
- Sums received as compensation for labor accidents and insurance in general, alimony allowances, and benefits paid by the Social Security Agency;
- Income from sums received by individuals upon termination of employment, such as notices, seniority premiums, indemnities, bonuses and other benefits set out in collective agreements and individual labor contracts, up to five thousand US dollars (US\$5,000);

- Pension funds under Law 10 of 1993, when periodic sums are received by beneficiaries;
- Income from sums received or accrued by a person abroad in respect of royalties paid by persons established in the Colon Free Zone;
- Properties received as inheritance, legacy, or donation;
- Income of individuals, up to an amount of US\$11,000.00;
- Any other income exempted by a special law.

The following persons are exempt from income tax:

- Individuals or corporations exempt from taxes as a result of public treaties or contracts with the government;
- The state, municipalities (including their associations), autonomous and semi-autonomous institutions and state institutions;
- Churches of any denomination, seminaries and religious or charitable societies, when such income is obtained as a direct result of worship or charitable activity;
- Duly recognized nursing homes, orphanages, non-profit foundations and organizations, provided that such income is intended exclusively for civic, business and society activities, social assistance, public welfare, education, or the promotion of sports. Such entities should be registered with the tax authorities;
- Salaries and fees paid to foreign personnel of diplomatic entities accredited in Panama;
- Salaries and fees paid to foreign consular personnel accredited in Panama, provided that the same treatment is given to Panamanian consulates abroad;
- Individuals or legal entities that qualify for such exemptions due to public treaties or under contract authorized or approved by law;
- Foreign investors on interest they may receive, provided that the capital on which the interest is paid is invested exclusively in the construction of low-income housing, as determined by the Ministry of Housing. Foreign governments or governmental institutions must guarantee the lending of capital;
- State and private institutions dedicated to agricultural research, provided that these are non-profit in nature, for the sums donated to the development of their programs, and those institutions carrying out research for the improvement of systems and technological transfers;
- Artists, or classical music groups, contracted by a non-profit organization registered with the National Institute of Culture (INAC). This organization must be involved in the promotion, execution and broadcasting of cultural, musical and artistic values and use the profits from such activities to meet its objectives. Prior authorization must be obtained from the Directorate General of Revenue, but only for a specified amount;
- Agricultural producers that have annual gross income of less than two hundred fifty thousand US dollars (US\$250,000). Certain restrictions apply for legal entities;
- Cooperative associations covered by Law 17 of 1997, provided that they comply with the requirements established by Executive Decree 137 of 2001;
- Industrial companies covered by Law 3 of 1986, provided that their total production is exported;
- Industrial companies covered by Law 3 of 1986 under certain other conditions;
- Tourism companies under the special tourist zone governed by Law 8 of 1994;
- Micro, small and medium businesses, under certain conditions;
- Hydrocarbon companies under Law 8 of 1987;
- Free Trade Zones (formerly referred to as “Export Processing Zones”) governed by Law 25 of 1992 and Law 32 of 2011;
- Any other person specifically exempted under a special law.

Taxpayers and Taxable Income

Section 694 of the Tax Code defines a taxpayer as: *“the individual or legal entity, either Panamanian or foreigner, that receives taxable income subject to income tax.”* Regulations have also added trusts (in Spanish, *fideicomisos*), joint ventures and any other legal entity receiving assessable income as taxpayers.

Taxable income is defined as income produced, from any source, within the Panamanian territory, regardless of the place where the income is received. Deviating from the territoriality principle, Panamanian tax laws also consider as taxable income any income that, even when derived from acts or services rendered abroad, benefits individuals or legal entities residing in Panama and relates to the generation and continuance of their Panamanian-source income.

Taxation Year

Generally, the normal taxation year for all taxpayers begins on January 1 and ends on December 31. However, an application may be filed with the tax authorities to change a taxation year to a special period that covers a total of 12 consecutive months.

Tax Rates

Individuals earning taxable income are subject to a progressive tax rate, according to their annual accrued income.

- The first US\$11,000 earned by an individual is exempted from taxes.
- Income between the US\$11,000 threshold and up to an amount of US\$50,000, will be taxed at a tax rate of 15%.
- For last income bracket, amounts are taxed on a fixed amount of US\$ 5,850 for the first US\$ 50,000 and any excess income is taxed at a rate of 25%.
- Corporations and legal entities will be subject to a fixed tax rate of 25%. Corporate taxation is discussed in the next chapter.

Procedures for Paying Income Tax

Income taxes will be triggered by the filing of the income tax return, and shall be payable before the 31st of March of each year, regardless of any extension period given for the filing of the return.

Non-residents rendering services in the Panamanian territory to individuals and entities will be subject to income tax via withholding, for which the party responsible for filing the forms, as well as remitting and paying taxes, will be the Panamanian entity that received the services.

Withholding income taxes shall be paid within a period of 10 days after the payment of the services or the recording of the expense in the accounting books.

Income taxes can be paid via bank transfer of the funds to the National Treasury's account, in cash or by way of a cheque attached to a payment slip that specifies the amount of tax being paid. Such amounts may be paid through banks or at the tax authorities' offices.

Stability of the Investment System

Freedom of investment, which includes acquisition of private property, is allowed under the Panamanian Constitution. For foreigners, the protection of property is not limited to measures found in the Constitution and other domestic laws. Foreigner investors' intellectual and industrial property is subject to the same regulations as those for national investors. The benefits and conditions of investing in Panama offered under international agreements and signed by the Panamanian authorities apply to national and international investors alike. In addition to bilateral

trade agreements, Panama is also a signatory to the Multilateral Investment Guarantee Agreement (MIGA) for promoting and protecting investments.

Locally, Panama promotes and protects investment through the stability of its investment system established under Law 54 of 1998. This system provides equal treatment for national and foreign investors, grants stability for direct taxes and guarantees the repatriation of capital, dividends, interest, profits and capital gains.

The system's stability applies to investment activities within the Panamanian territory, which include: the tourism industry, agro-export, agro-forest, mining, export processing zones (now named free trade zones), commercial and oil free zones, telecommunications, construction, railroad and port development, electric power generation, distribution and transmission, irrigation projects and the efficient use of hydro resources and other approved activities for improving technology.

The law governing the stability of investments (Law 54 of 1998) reads as follows:

- For investors, obligations include planning of investments representing no less than two million US dollars (US\$2,000,000) and paying a fifty US dollar (US\$50) fee to register with the Minister of Commerce and Industries (MICI);
- Stability of direct taxes for a ten-year period is granted to any national or foreigner or corporation that meets the requirements, unless causes such as public interest matters present conflicts;
- Indirect taxes are excluded from this system (e.g. ITBMS or Panamanian VAT);
- Stability for the local tax system (e.g., municipal taxes) is granted for a five-year period;
- In the event of a legal dispute, reconciliation and arbitration decisions are acceptable, except in the case of taxation disputes, which should be submitted to courts.

In 2007, Cabinet Decree 17 extended this stability to include the following activities:

- Hydrocarbon exploration and exploitation, as well as refining, storage and transportation of petroleum, its derivatives and natural gas;
- Production of alternative fuel sources;
- Activities relating to research within the City of Knowledge, such as laboratories and specialized training centers.

International Taxation (TDT/TIEA)

Tax Treaties

Since June 2011, Panama's income tax treaty network expanded quickly as it was aiming to comply with the OECD's peer review process in order to be removed from their black list of tax havens.

Until January 2018, Panama had in force a total of seventeen (17) double taxation treaties with the following countries:

1. Mexico, in force since 2011
2. Barbados, in force since 2012
3. Qatar, in force since 2012
4. Spain, in force since 2011
5. Luxembourg, in force since 2012
6. The Netherlands, in force since 2012
7. Singapore, in force since 2012

8. France, in force since 2012
9. South Korea, in force since 2013
10. Portugal, in force since 2013
11. Ireland, in force since 2013
12. Czech Republic, in force since 2014
13. United Arab Emirates, in force since 2014
14. United Kingdom, in force since 2014
15. Israel, in force since 2015
16. Vietnam, in force in 2018
17. Italy, in force in 2018

Panama's tax treaty network in force offers the following reduced tax rates:

Treaty Partner (rates)	Dividends	Interest	Royalties	Services
Barbados	0 - 5 - 7.5%	0 - 5 - 7.5%	0 - 7.5%	0 - 7.5%
Czech Republic	0 - 10%	0 - 5 - 10%	0 - 10%	-
France	0 - 5 - 15%	0 - 5%	0 - 5%	-
Ireland	0 - 5%	0 - 5%	0 - 5%	-
Korea	0 - 5 - 15%	0 - 5%	0 - 3 - 10%	-
Luxembourg	0 - 5 - 15%	0 - 5%	0 - 5%	0 - 5%
Mexico	0 - 5 - 7.5%	0 - 5 - 10%	0 - 10%	0 - 12.5%
Netherlands	0 - 15%	0 - 5%	0 - 5%	-
Portugal	0 - 10 - 15%	0 - 10%	0 - 10%	0 - 10%
Qatar	0 - 6%	0 - 6%	0 - 6%	0.00
Singapore	0 - 4 - 5%	0 - 5%	0 - 5%	0.00
Spain	0 - 5 - 10%	0 - 5%	0 - 5%	0 - 7.5%
United Arab Emirates	0 - 5%	0 - 5%	0 - 5%	0.00
UK	0 - 15%	0 - 5%	0 - 5%	-
Israel	0 - 5 - 15 - 20%	0 - 15%	0 - 15%	-
Vietnam	0 - 5 - 7 - 12.5%	0 - 10%	0 - 10%	0 - 7.5%
Italy	0 - 5 - 10%	0 - 5 - 10%	0 - 10%	0 - 10%

In addition to double taxation treaties, Panama has also signed several exchange of information agreements with the United States of America, the Faroe Islands, Finland, Iceland, Canada, Norway, Sweden, Denmark, and Greenland.

Panama also supports the OECD's BEPS developments and signed the Convention on Mutual Administrative Assistance in Tax Matters on February 23, 2017. It is committed to applying the minimum standards set out in the Inclusive Framework on October 31, 2017.

Tax treaties already passed as laws by the National Assembly have demanded tax reforms and might request other changes in the near future. The international tax measures included in the new Panamanian system are summarized below.

As of 2010, Law 33 introduced an adequacy standard in order for Panama adjust to tax treaties. This includes the following:

- An arm's length principle was introduced in order to value transactions between taxpayers and related parties, in addition to methods for applying this principle;
- A definition of related parties was introduced;
- The standard authorizes the Directorate General of Revenue to oversee authorized operations to taxpayers;
- The scope of application of these provisions is clearly set out;

- The specific treatment applicable to services between related parties is also set out;
- Simultaneous proof and general principles for providing and documenting information are set out;
- The concepts of permanent establishment and tax residence are introduced;
- This entire adequacy standard is applicable to tax treaties.

Transfer Pricing

Since 2010, Panama has transfer pricing policies in force for transactions between related parties abroad. Initially, these policies were applicable only to countries with double tax treaties signed with Panama. However, transfer pricing rules were broadened in 2013 to cover all transactions between Panamanian entities and related parties abroad.

Entities are obliged to file Form 930 reporting their transactions with related parties abroad each year, before June 30th, only if these transactions have an impact in the entity's income, cost or expense accounts affecting its taxable income in Panama. A transfer pricing study is not required to be filed, unless the tax authorities explicitly request this, in which case the entity will have a period of 45 days to present such study to the tax authorities.

BEPS and Exchange of Information

By January 2018, the government of Panama had made some efforts to improve tax cooperation and transparency, which include implementing the Common Reporting Standard (CRS) since August 2017, signing the Multilateral Convention on Mutual Administrative Assistance in Tax Matters and joining the Inclusive Framework on BEPS, both in October 2016. It has also included very strict regulations in its domestic law regarding money laundering, the accounting records of offshore entities, and many other matters.

The Panamanian government is actively seeking to comply with the international standards established by the OECD and the Global Forum to fight tax evasion and to improve the exchange of information between tax authorities.

On January 24, 2018, Panama joined the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS (also known as Multilateral Instrument or MLI). However, it has not yet ratified its final list of positions and reservations for applying the MLI to its current list of tax treaties.

On December 2018, Panama introduced a new regulation (Law No.69 of 26 December 2018) following BEPS Action 5 focused on countering harmful tax practices. By means of this provision, the nexus approach for IP regimes was included, therefore the benefits granted –by virtue of a special law or preferential tax regime- to IP income would only be available if it is linked to the taxpayer's qualifying R&D expenditures (substantial requirement).



Corporate Income Tax

Chapter 4



4 Chapter 4

4 Corporate Income Tax

Taxable Income

A corporation's taxable income is the balance that results after deducting applicable costs and expenses from gross income. The costs and expenses required to carry on a business and generate taxable income in Panama are deductible, provided that they are adequately documented and, since 2010, that they do not exceed the maximum deductible costs and expenses formula (discussed in this chapter).

Tax rates

- As of January 1, 2014, the general corporate income tax rate is 25 percent.
- However, companies in which the state is a shareholder, or has a stake of more than forty percent (40%) of shares, will continue to be taxed at the rate of thirty percent (30%), as established prior to the 2010 amendment to the Panamanian Tax Code.

Methods for Calculating Taxable Income

There are two mutually exclusive methods for calculating the income tax due by a taxpayer with gross income above one million five hundred US dollars (US\$1,500,000).

These methods involve applying the general rate or the appropriate one, according to activity and tax period, to the greater of:

- The net taxable income (calculated under the conventional principles); or
- The net taxable income that arises after applying 4.67 percent to the total taxable income (defined as the amount resulting from deducting the exempt income and foreign source income from total income), resulting in an effective tax rate of 1.4 percent;
- Deductions are only admitted for this second method of calculating income tax, based on the legal presumption of revenues (known in Spanish as *cálculo alternativo* and, abbreviated as "CAIR", even though this terminology was eliminated by Law 8 of 2010).

Alternative Method for Calculating Income Tax - Highlights

- Income from commissions will be calculated based on the total amount of commissions.
- Companies that embedded the selective consumption tax and fuel consumption tax in their sales price are allowed to deduct from their total income the amounts arising from these two taxes, in order to determine their taxable income (hence the alternative calculation).
- Taxpayers engaged in the importing, distribution and sale of certain fuel products such as 91 and 95 octane gasoline, LPG and diesel fuel, can deduct the cost of acquiring these products from taxable income for alternative minimum tax purposes.
- If a company or legal entity incurs tax losses, or if the effective income tax rate of such losses exceeds the general rate (or the applicable one), it will have the option to apply for a waiver for the alternative tax calculation from the Directorate General of Revenue (DGI).

The DGI must authorize the taxpayer to use the first option (traditional calculation instead of the alternative method, as determined by a formula provided under law).

Deductible Expenses for Corporations or Other Legal Entities

- Deductible expenses are those incurred in the generation of taxable income or in the maintenance of its source.
- Expenses incurred must be related to Panamanian-source income.
- Consequently, expenses incurred to generate foreign or exempt income are not deductible. If the portion that actually corresponds to each kind of income cannot be determined, the expenses incurred to obtain both taxable and non-taxable income must be allocated in proportion to the ratio of taxable and non-taxable income. All expenses or disbursements must be supported by proper documentation in order to be deductible.
- Expenses between a corporation and its subsidiaries and affiliates, or its directors, officers, executives and shareholders, or their relatives within the fourth degree, and in-laws within the second degree, are restricted when both parties do not use the same accounting system.
- Expenses are only deductible in the taxation period during which they are actually incurred.
- Other relevant deductible expenses are discussed in detail below.

Bad Debts

- Taxpayers may choose one of two methods for deducting bad debts: direct write-off or establishment of a reserve.
- In order to be considered a bad debt, an account must satisfy three requirements: first, it must have been a generator of taxable income; second, it must be duly accounted for and be included as gross income; and third, the debtor's insolvency or the statute of limitation of the debt must be proven.
- If a bad debt that was deducted is recovered, such recovered amount must be deducted from the total deductible costs and expenses in the year of recovery.

Bonuses and Other Extraordinary Remuneration

Profits that employers distribute among their employees, as well as bonus payments, are deductible for income tax purposes in the taxation period in which they were paid, but limiting the deductibility to one month of salary in those cases where the family relationship between the owner and the employee is within the fourth degree of consanguinity or whenever the employee holds more than fifteen percent (15%) of the shares of the company.

Depreciation

Depreciation is determined by the economic useful life of assets. The minimum depreciation period for movable property is three (3) years while the minimum period for immovable property is thirty (30) years. Depreciation must take into consideration the actual useful life of the asset, as well as its maintenance and working schedules, among other factors.

Donations

Other deductible items include donations:

- Donations to non-profit educational and charitable institutions of Panama, provided that these institutions have been previously approved for such purposes by the corresponding authority. Deductibility is limited to a maximum or cap of one percent (1%) of the donor's

gross taxable income. In the case of individuals, the limitation is set at a maximum of US\$50,000 being considered as a deductible sum.

- Donations to the central government, its institutions, municipalities and community boards.
- Other donations as established by domestic tax law.

Interest and Royalties

- Interest and royalties are deductible expenses, under general principles, and are considered as taxable income for the recipient.
- In the case of payments made to non-resident individuals, or non-resident entities, the resident entity is obliged to withhold income tax at the regular rates, over fifty percent (50%) of the remitted sum.
- Royalties paid by companies located in the Colon Free Zone to non-residents are not taxable, thus not subject to withholding and should not be considered as a deductible expense.

Labor Benefits

Indemnities and other labor benefits are deductible, to the extent that they are not covered by insurance policies.

Representation allowances

- Representation allowances are defined as expenses paid to employees who have to represent the company on events, liaise with clients and provide entertainment to individuals and/or entities linked to the taxpayer's regular activity.
- These expenses must be linked to the production of taxable income, in the normal course of business.
- These expenses may be paid directly by the taxpayer, by means of reimbursement, or by allocating fixed amounts to its employees.
- In the first two instances, expenses must be duly documented.
- When expenses are paid through fixed allocations, the amounts must be added to the individual's gross income, and a ten percent (10%) rate shall be withheld as definitive income tax, up to \$25,000.00. Any excess amount will be taxed at a fifteen percent (15%) tax rate.
- The amount of representation allowances received by an employee is subject to Social Security contributions, like an ordinary salary, but without an education tax.

Salaries

- Salaries paid to employees are fully deductible, provided that they are required for the generation of taxable income for the company.
- Contributions to private pension funds under trusts, in accordance with Law 1 of 1984, are deductible up to ten percent (10%) of the employee's annual gross income.
- In addition, employees might receive a US\$350 food voucher from the employer (deductible as an expense) and will not be considered as salary in kind on behalf of the employee.
- Moreover, a special tax benefit was established for entities hiring disabled or handicapped employees, as well as young individuals, taking into account that:
 - Hiring people with physical disabilities allows the employer to deduct as an expense two-hundred percent (200%) of the salary paid to the employee, up to six (6) months, according to Law 1 of 1992;

- The employer received a tax benefit for initial employment contracts with young individuals in accordance with Law 12 of 2002.
- After the employer's taxable income has been determined, salaries and labor benefits paid to young individuals between eighteen (18) and twenty-five (25) years of age, hired for a one-year contract, may again be deducted, with the minimum wage established by regulations and not set out in the social security system.

Formula for the Maximum Limit on Deductions of Expenses and Costs

- Maximum deductible costs and expenses = taxable income / total income x total cost and expenses.
- The total costs and expenses should not consider the allowance for bad debts, the tax for the notice of operation tax and the technical cost relating to the risk covered by insurance companies.

Special Tax Systems

Some of the most relevant special income tax systems are briefly described below:

Agriculture and Livestock

- Production expenses incurred in connection with a harvest may be deducted either in the fiscal year when incurred or paid, or may be deferred and deducted in the fiscal year during which the crops are sold.
- If a crop is sold in two or more fiscal years, deferred production costs must be allocated on a *pro rata* basis.

Artists, Performers, Musicians, Athletes and Other Professionals

The total revenue received by artistic groups, musicians, singers, athletes, and other professionals coming to the country are taxed at a fifteen percent (15%) fixed rate.

Branches of Foreign Corporations

- Branches of foreign corporations established in the Republic of Panama must keep their accounting records for Panamanian operations separate from head office or other branch records.
- Foreign corporation branches must withhold ten percent (10%) of their total net income, generated in Panama, after taxes.
- This withholding is paid along with annual income taxes.
- There are no special rules governing the taxation of foreign corporation branches, meaning that all general tax rules apply to this type of entity.
- Tax consolidation is not permitted.

Capital Gains

- Capital gains are considered taxable income, except those arising from the sale of shares/securities registered on the Securities Market Superintendency (SMV for its Spanish acronym) or issued by the Panamanian government.
- Therefore, capital gains derived from the sale of either shares or securities, which are not within the exempted provisions, are taxed at a ten percent (10%) fixed rate. However, the buyer or transferee must withhold an amount equivalent to five percent (5%) in advance and remit such amount to the tax authorities within ten (10) business days, following the date of payment of the transaction. The seller or transferor can consider the 5% advance as the definitive tax.

- Capital gains resulting from the sale of real estate property are subject to a ten percent (10%) definitive tax rate (special tax rule discussed later in this chapter). Notwithstanding the 10% definitive tax rate, the seller should pay an advance tax of three percent (3%), calculated on the sales price, and consider this advance tax as definitive.

Civil Partnerships

In the case of civil partnerships used by licensed professionals, the alternative calculation of income tax (CAIR) can be performed at the partnership level, in accordance with the aforementioned rule, unless the taxable income is distributed to the partners. In this case, income tax will be calculated according to the following tax rates:

Partners are not allowed to deduct costs and expenses from such profits.

Construction Companies

Construction companies with operations covering more than one fiscal year can follow the completed contract method, the percentage-of-completion method or a gross-margin method based on payments received.

Net Taxable Income	Tax Rate
Up to US\$11,000.00	0%
US\$11,000.00 to US\$50,000.00	15% on amounts between US\$11,000.00 and US\$50,000.00
Over US\$50,000.00	US\$5,850.00 on the first US\$50,000.00 and 25% on the surplus.

Cruise Ships

As a general rule, tickets and services obtained from companies that operate cruise ships are exempt from income tax, provided the companies have their home port in Panama. International transportation is taxed on the portion related to freight, tickets, cargo and other services with the Republic of Panama as the place of origin or destination.

Film and Audiovisual Industry

- Law 16 of 2012, which supersedes Law 36 of 2007, grants incentives to the film and audiovisual industry.
- Any individual or entity, national or foreign, that carries out filming and audiovisual activities, in accordance with the provisions established in Law 16 of 2012, can register with the National Registry of Incentives (Ministry of Commerce and Industries) and benefit from the tax and migratory incentives provided by the afore-mentioned law.
- Registered entities will be exempt from any national taxes, duties, contributions and fees, which are exclusively related to the film and audiovisual activities, within the designated areas, for a period of 20 years. Some limitations are applicable.

Free Trade Zone Companies (Colon Free Zone and Other Zones)

- Defined as those in which sales are made from the free zone to clients outside Panama, including the transfer of merchandise within the CFZ and the Tocumen International Airport Free Trade Zone or from one free trade zone to another. Export and re-export operations are tax-exempt.
- Domestic (local or internal) operations are those in which sales are destined to the Republic of Panama.
- Profits arising from local sales operations are not subject to any special treatment.

- Companies operating in any free trade zone must disclose activities carried out abroad separately from local or domestic activities in their accounting records.
- Income tax on dividends is withheld whether the earnings distributions are generated from the establishment in a free trade zone, although such withholding would be at a reduced rate.
- Special rules applied to Oil Free Trade Zones.
- Individuals working within a free trade zone are subject to income tax at the regular rates discussed in Chapter 5.

Insurance Companies

Insurance companies, regardless of their place of domicile or of incorporation, are subject to income tax on profits derived from insured risks located in the Republic of Panama, including life, accident, and health insurance policies for residents of Panama.

Interest, Commissions and Other Charges on Foreign Financing

- Interest, commissions, and other financial charges, credited or remitted abroad, are subject to income tax at the regular rates (either for legal entities or individuals) over 50 percent of the amount remitted abroad.
- The amount equivalent to 50 percent of the total amount paid to the foreign creditor, by individuals or legal entities making the payment, is the taxable base.
- Consequently, remittance of interest payments is based on an effective rate of 12.5 percent, for legal entities.

Interest on Fixed-period Bank Accounts

Does not apply to savings accounts.

Interest on Registered Securities

- Interest paid or credited by individuals or legal entities on debentures, bonds, financial instruments, mortgage documents or any other securities not registered before the SMV are taxable at the ordinary rates.
- Interest paid by companies registered with the SMV is subject to a definitive tax of five percent (5%) on the total amount of such interest. The definitive tax must be withheld by the company or entity that pays or credits the interest.
- If the financial instruments were acquired through an organized stock exchange, the interest is exempt from income tax.

International Transportation

- International transportation corporations are taxed, regardless of their place of incorporation or domicile, on income earned from freight, passenger and cargo transportation, or other similar services provided, where the place of origin or the final destination is Panama, or the freight, passengers or cargo are in transit.
- Thus, the former rule for determining taxable income referring to three percent of total gross income is no longer applicable at the taxpayer's discretion.
- Income from the operation of cruise ships, whose home port is in Panama, is tax exempt.

International Telecommunications

Telecommunications companies are subject to the general income tax rate of twenty-five percent (25%) as of January 1, 2014.

Loss Carry-forwards

- Net operating losses (NOL's) for a given fiscal year can be carried forward to each of the next five (5) taxation years, deducting a maximum of twenty percent (20%) of the loss per year.
- The deduction cannot reduce the net taxable income for that year, by more than fifty percent (50%).
- Non-deducted NOL's in a given year cannot be carried forward to the following years, nor do they qualify for a tax refund.
- Any compensation received for the losses (e.g. from insurance), must be deducted from the loss originally reported.
- The right to carry forward losses is not transferable among taxpayers, even in cases of mergers and acquisitions.

Maritime Transportation Companies

Although there are some exceptions, income generated by international maritime transportation companies in respect of freight, tickets, cargo and other similar services is considered as Panamanian-source income, regardless of the place of incorporation or domicile of the company.

Mergers and Acquisitions

Panama allows two types of mergers:

- By absorption ($A+B = A$), and
- By the integration or creation of a new company ($A+B = C$).
- All acts, agreements and operations necessary to carry out a merger will be exempt from income tax, dividend and complementary tax, ITBMS (local VAT), and real estate transfer tax, to the extent that the merger complies with the applicable rules.
- Mergers that do not comply with such provisions should be considered as taxable operations, unless proven otherwise.

The merger agreement between the merging companies must fulfill all requirements set out in Law 32 of 1927 governing corporations, and the merger agreement must be filed with the Public Registry for the merger to become effective.

Non-profit or Non-governmental Organizations (NGO)

To the extent that the NGO complies with its authorized purposes of being a non-profit organization, it will remain exempt from income tax. Furthermore, its beneficiaries can benefit from the donations to such institutions, as long as the NGO is authorized by the DGI to receive tax deductible donations.

Offshore Panamanian Branch

- Foreign companies are permitted to generate or maintain local taxable income.
- This statement relies upon the territorial system that applies in the Republic of Panama, which seeks to tax only income (regardless of the taxpayer's nationality) from a Panamanian source, unless otherwise expressly exempted.
- Therefore, a foreign company may not only generate and maintain local taxable profits, but also be registered as a legal entity in the Public Registry.
- For the purpose of recognizing taxable profits, a corporation must mainly identify taxable events and whether they constitute Panamanian offshore operations. Thus, Panamanian offshore operations are not taxed as set out in section 694, paragraph 2, of the Panamanian Tax Code.

- On the contrary, a foreign company may carry out or complete local operations subject to income tax.

Producers and Distributors of Radio and Television Programs

Foreign companies that produce and distribute radio and television programs are taxed at a rate of six percent (6%), on the total amount paid or credited by local distributors and television companies.

Real Estate Business

- Sellers of real estate must pay a two percent (2%) tax for each transfer of property. The transfer tax is discussed further in Chapter 8.
- In addition to the transfer tax, capital gains are taxable as follows:
 - Sellers of real estate are subject to a special capital gains tax which sets out a special and reduced tax rate.
 - When the seller's ordinary course of business is not the sale of real estate, the applicable tax rate will be three percent (3%). The rate shall be applied on the value of the transfer and the cadastral value, whichever is higher. The taxpayer may opt to consider the 3% advance tax as the definitive capital gains tax.
 - When the seller's ordinary course of business is the sale of real estate, the applicable progressive tax rate ranges between 0.5% and 4.5%, in the case of new housing and commercial properties. The rate shall be applied on the value of the transfer and the cadastral value, whichever is higher.

Reinsurance Companies

- Reinsurance companies are taxed on their Panamanian-source income.
- Premiums and profits from reinsuring foreign risks are not subject to taxes.
- Reinsurance premiums paid by local insurance or reinsurance companies to foreign reinsurance companies are considered foreign-source income and, therefore, are not taxable.

Rental Activities

- Gross income from rental activities includes earnings received either in cash or in kind, and the value of improvements made by the tenant to the property and left for the benefit of the landlord.
- Apartment building owners bear the burden of proof for apartments that were not rented throughout the entire taxation period.

Sale of Securities

- Profits from the sale of bonds, shares, and other securities issued by entities, as well as those obtained from the sale of any other personal property, are taxable at a rate of ten percent (10%).
- The acquisition of public share offerings is subject to the above tax system.
- Where the sale of securities is concerned, the buyer or transferee must withhold five percent (5%) and remit the amount to the tax authorities within ten (10) business days, following the date of payment of the transaction.
- The seller or transferor can consider the advance of 5% as the definitive tax and a tax refund can be requested whenever the advance tax withheld by the buyer is greater than the 10% regular tax rate.
- On the other hand, gains from the sale of shares, bonds, and other securities registered with the SMV are exempted when such income is derived from a stock exchange or an

organized market, or as the result of a corporate merger, consolidation or reorganization, as long as the shareholders receive other shares from the resulting corporation.

- Moreover, the transfer of securities issued or guaranteed by the estate is not taxable.

Withholding Tax on Dividends

- Companies that distribute taxable earnings must withhold the corresponding amount and remit it to the tax authorities within the ten (10) days following the date on which the distribution was authorized.
- The withholding tax is ten percent (10%) for nominal shares and twenty percent (20%) for bearer shares.
- Corporations distributing profits to their shareholders must withhold 10% of such amounts, which result from Panamanian-source income, and five percent (5%) when related to foreign or exempt sources of income.
- If total period earnings are not distributed, or the total period earnings distributed are less than forty percent (40%) of net income, a complementary tax must be withheld over 40% of the net income, after taxes, as an advance on dividend tax, resulting in an effective rate of four percent (4%) over the total net income after taxes.
- The other six percent (6%) will be paid when such dividends or profits are actually distributed.
- Branches of foreign corporations must withhold and pay 10% of their total net income and 20% if the stock of the corporation is issued in bearer form.
- In the case of a corporation with both types of stock, the tax must be paid according to the rates for each kind of stock, unless the dividends distributed were equivalent to less than 40% of the net profits.
- Also, if no distribution is made, the rules for the complementary tax will apply regardless of the type of stock.
- The distribution of profits of non-taxable or foreign source income is subject to a 5 percent dividend withholding tax.
- The earnings distribution derived from export and re-export sales (external operations) of companies operating in the Colon Free Trade Zone is subject to 5% rate on all sources of income (local, foreign and exempt). Loans or credits granted to shareholders and the reduction of share capital for legal entities are considered to be implicit in the distribution of profits.
- Loans or credits granted to shareholders are subject to a 10% withholding tax, regardless whether they are granted by a legal entity under a reduced rate (e.g. Colon Free Trade Zone, Oil Free Trade Zones, Free Trade Zones, APP, etc.).
- Reduction of capital is admitted only when undistributed profits are totally distributed and the dividend tax is paid. Otherwise, an implicit distribution of profits might be determined by the tax authorities.

Withholding Tax on Remittances

Where services and acts are perfected and provided within the Panamanian territory by a non-resident or foreign entity, a withholding tax of 25 percent applies on half of the amount paid to the non-resident beneficiary instead of the full amount (effective rate of 12.5 percent on the total amount).

Moreover, if the payment of the remittance is not taken as a deductible expense by the Panamanian taxpayer, there is no obligation to withhold income tax. However, this exemption is not applicable to Panamanian government institutions, entities in which the government owns at least 51% of the equity, and/or taxpayers at loss.

Notwithstanding the general withholding rule, the 2010 Act introduced the non-registration requirement for foreign beneficiaries as taxpayers before the Directorate General of Revenue in order for the payer to withhold income tax. Otherwise, if such beneficiary abroad is registered with the Panamanian tax authorities as a taxpayer, the withholding is not made and the registered beneficiary must file an income tax return in Panama.

In addition, if a taxpayer is exempted from withholding an amount on remittances by means of a “special law”, such exemption would not become applicable if the beneficiary of the payment abroad can use as a tax credit, in the country of residence, the amount of tax that would have been generated and paid in Panama, if the special exemption did not exist. All individuals or entities exempted from withholding taxes are required to have an opinion, issued by an independent tax expert in the country of origin, indicating whether the withholding tax can be credited or not abroad.



Income Tax for Individuals

Chapter 5



Chapter 5

5

Income Tax for Individuals

Taxable Income

All individuals in Panama, including citizens, residents and non-residents, are taxed only on Panamanian-source income as defined in the Tax Code and Income Tax Regulations.

Panamanian-source income, or the taxable income of individuals, is determined under different rules as compared to legal entities but based on the territoriality principle as well, which defines taxable income as income generated, from any source whatsoever, within the territory of the Republic of Panama, regardless where the contracts are signed or where the amounts are paid.

Based on the tax provisions, income in the form of cash, in kind, or in value arising from personal services performed under an employment relationship, the practice of a profession or trade, and all types of services rendered, carried out or exercised within the territory of Panama are subject to income tax.

Tax Residency and Tax Rates

All individuals who prove that they remained in the country for more than one hundred eighty three (183) days in a calendar year, either continuously or non-continuously, or who have a permanent residence and recognize this as the center of their vital economic or family interests, are considered as residents for tax purposes, regardless of their immigration status.

Residents for tax purposes are subject to income tax on their wages and other forms of income according to the following regular progressive tax rates:

Net taxable income	Income tax payable
Up to B/. 11,000.00	Exempt
More than B/. 11,000.00 up to B/.50,000.00	15% rate on amounts exceeding B/.11,000.00 up to B/.50,000.00
More than B/.50,000.00	B/. 5,850.00 for the first B/.50,000.00 and 25% on excess amounts

Examples:

1. If net taxable income is B/. 10,000, income tax is zero.
2. If net taxable income is US\$45,000, income tax will be calculated as follows:
 $(45,000 - 11,000) \times 15\% = \text{B/. } 5,100.$
3. If net taxable income is B/. 60,000, income tax will amount to B/. 8,350 calculated as follows:
 $(60,000 - 50,000) \times 25\% + 5,850$

Non-resident taxpayers are those individuals who remained outside of the country for a maximum period of one hundred eighty-three (183) consecutive or non-consecutive days in a

calendar year. Non-resident employees are subject to income tax at a flat rate of 15% on their gross income (wages and salaries), plus the education tax of 2.75%.

In-kind income

In-kind benefits arising from services performed in Panama are fully taxable in accordance with the income tax law when such services were performed under a labor relationship and are related to the generation of taxable income in Panama.

Notwithstanding the above, stock option plans and similar compensation plans are not deemed as “in-kind salary”.

Housing allowances and the imputed value of housing directly provided by the employer are fully taxable. The imputed value is determined by the market price (which is normally the cost charged for the housing). Where the employer bears the costs of utilities (e.g., water, electricity, etc.), this results in additional income tax. Social security contributions are also payable on housing benefits.

Fuel is considered an in-kind salary. However, when the fuel allowances are granted to certain employees (such as drivers, messengers, sales representatives and the like), these amounts will not be considered as in-kind salary.

Taxable Benefits

- Food and fuel allowances;
- Club memberships and subscriptions to publications;
- Vehicles for personal use;
- School tuition and educational allowances;
- Housing and utilities allowances;
- Personal debt payments;
- Insurance premiums;
- Non-business mobile phone;
- Clothing allowances;
- Reimbursements of taxes; and
- International service premiums.

In-kind Benefits Deemed as Non-taxable Income

Moreover, special tax treatments are available for certain benefits. The following items are not considered to be in-kind payments to the employee:

- Stock option plans;
- Business meals;
- Pension fund contributions ;
- General benefits provided to employees;
- Transportation provided for business purposes;
- Quotas for business or professional organizations;
- Training and education related to the business;
- Insurance premiums, such as life and health insurance, pensions and employee automobile insurance when the vehicle is not a payment in kind;
- Reimbursements of business expenses;
- Travel allowances related to the business, except for vacations; and
- A mobile phone for business purposes.

Representation Allowances

Representation allowances could be granted to management or trusted employees and may not exceed the person's normal salary.

For income tax purposes, representation allowances are not cumulative with salaries and other taxable income and, therefore, are not only subject to special tax rates but the employees who are receiving expense allowances, in addition to their salaries, are not obliged to file an income tax return. Representation allowances are subject to withholding at the source and do not qualify for any deductions.

Tax rates for representation allowances

Net taxable income:	Income tax payable:
Up to B/.25,000.00	10%
More than B/.25,000.00	B/.2,500.00 for the first B/.25,000.00 and a rate of 15% on amounts exceeding B/.25,000.00.

Exemptions

Citizens, residents and non-residents are not taxed on exempt income, which includes:

- The amounts received from pension and retirement funds in accordance with Law 10 of 1993 when the individual begins to receive periodic payments, as long as the cessation of employment results from an employee's retirement or permanent resignation.
- There is a tax exemption on gross annual income of B/. 350,000 for individuals working specifically in agricultural and livestock activities.

Personal Deductions and Non-deductible Expenses

Taxpayers are eligible for the following deductions from taxable income:

- Married couples filing jointly - US\$800 annually;
- Medical expenses incurred within Panama, if duly substantiated, such as medical insurance premiums and the sums paid for hospital and medical expenses not covered by insurance;
- Interest paid on mortgage loans for acquiring, constructing, or improving the principal residence of the taxpayer in the Republic of Panama, up to a maximum of B/. 15,000 per year;
- Interest on loans for the education of the taxpayer or his/her dependents in the Republic of Panama, or on loans granted by the Institute for Education and Improvement of Human Resources (IFARHU), a governmental entity;
- Donations to qualified institutions (based on limitations for legal amounts);
- Dues paid to non-profit organizations, associations, or societies.

Non-deductible Expenses

The following items are not considered as expenses or disbursements incurred in the generation of income or in the maintenance of the income source and, therefore, are non-deductible expenses:

- Personal expenses for the taxpayer and his/her family's needs;

- Expenses incurred in construction work or improvements made to increase the value of any personal or real property when such construction work or improvements are subject to depreciation or amortization;
- Prior year expenses;
- Amounts paid for recreational trips, festivities, entertainment and donations (except for advertisements and announcements);
- Any other expenses which, although deductible, cannot be verified satisfactorily upon request by the Directorate General of Revenue.

Tax Compliance

In the case of wages and salaries and other remuneration received under an employment relationship, the employer is responsible for withholding the income tax according to the progressive tax rate.

Individuals with only one employer or only one salary as their source of the income are not obliged to file an annual income tax return.

Individuals with other taxable income not subject to withholding at the source or those with more than one employer are obliged to file an annual income tax return by March 15 following the end of the taxation year. A one-month filing extension can be requested. The payment deadline is March 31 following the end of the taxation year, with no extension allowed.

Late payments will trigger interest of approximately 1% monthly as well as a 10% surcharge on the tax payable. Late filing is subject to a fine of B/. 100.

Those individuals who receive not only wages and salaries but also forms of taxable income other than salaries can deduct not only the personal amounts but also, according to the general rules, those expenses incurred within the fiscal year that are directly related to the generation or preservation of such other income.

Expatriate Taxation - Visa

The visa for foreign nationals from specific countries which have friendly, professional and economic relationships with and investments in the Republic of Panama (“Visa - Países Amigos”) does not grant holders any exemption from paying taxes or making social security contributions.

Nonetheless, this type of visa is frequently recommended by law firms exclusively for migration and employment purposes, since this kind of visa and work permit only has to be requested once (after it has been granted to the expats, no renewals are required). Consequently, the expats will have a definitive visa and labor permit with no expiration date (permanent labor status and residency).

On the contrary, foreign executives holding a special temporary visitor’s visa, known also as the “executive visa”, which is suitable for personnel of international companies and banks who have a monthly salary of at least one thousand US dollars (US\$1,000) derived from sources located outside of the Panamanian territory, or non-Panamanian-source income, are exempt from income tax when the payment is made by the foreign head office of the company.

The special temporary visitor’s visa is targeted towards those foreign nationals working in Panama for an offshore business. Therefore, the holders of a special temporary visitor’s visa

would be exempt from paying income tax as long as the compensation is received directly from the head office located abroad.

Moreover, according to the Multinational Company Headquarters (SEM) System, the holder of the migration permit for Permanent SEM Personnel will be eligible for an income tax exemption, provided that the compensation is received from abroad.

Also, foreign personnel holding a SEM Permanent Personnel Visa will not be required to register for Social Security purposes and are not subject to pay the related contributions, unless they apply for permanent residency in Panama.



ITBMS

Chapter 6



Chapter 6

6 ITBMS

Tax on the Transfer of Tangible Personal Property and the Provision of Services (ITBMS)

ITBMS is an indirect tax applicable to the transfer of movable property (including imports) and to the services rendered within the Panamanian territory. It works as a value-added tax (VAT) and is a major source of income for the Panamanian government, along with income taxes and import duties.

Items and Services Taxed with ITBMS

Transactions subject to ITBMS include:

- The transfer of movable goods to a recipient granting ownership or proprietary rights over the goods, with the possibility of using the goods for economic purposes.
- The provision of services rendered within the Panamanian territory, with or without deliverables, which generally include the leasing of movable and immovable goods, entertainment events, domestic and international air passenger transportation, accommodations and lodging, etc.
- The importing of tangible goods or merchandise used either for personal consumption, charity, educational, scientific or commercial purposes or for the transformation, improvement or production of other goods and the achievement of other legal objectives.

Following the country's territoriality principle for income and other taxes, ITBMS will be applicable only if the transaction has taken place within the territory of the Republic of Panama, regardless where the contract was signed, where the transaction was agreed upon, or the place of domicile or residence or the nationality of the parties involved in the transaction.

Tax Base and Rates

The tax base will be different according to the transaction taking place, but in general the tax base will be the net sale price of the good or service. For the transfer of goods, ITBMS will be applicable to every transfer until the good reaches its final destination. The reimbursement of expenses is not subject to ITBMS tax.

ITBMS RATES			
0%	7% Regular rate	10%	15%
Medicine Food Books	Goods Services	Alcoholic beverages Accommodations & Lodging	Tobacco products

The tax authorities are allowed to request the payment of this tax during the five (5) years following the month when the tax was due.

Exceptions and Exemptions

The following transactions will not trigger the ITBMS tax:

- Transfers, contributions or the division of matrimonial property under prenuptial agreements.
- Expropriations, sales and services performed by the government, except for those transactions performed by state-owned industrial, commercial or financial entities.
- Goods allocated in ordinary or special trials, including the division of property trials.
- The transfer of negotiable documents and securities.
- Payments, including interest paid and received, in respect of financial services provided by entities legally authorized to do so. Commissions for banking and financial services are not included.
- Payments and interest paid to pension funds, severance funds, mutual funds, and other savings tools.

Some exemptions include the following,

- **The transfer of movable goods:**
 - Agricultural products in their natural state;
 - Food products;
 - Crude petroleum, diesel, light diesel, marine diesel, gasoline, flight gasoline, natural gas, oil fuel with low viscosity, intermediate oil fuel, oil fuel, bunker C, LPG, jet fuel, kerosene, and asphalt. Lubricants, oil lubricants, and lubricant grease are not included;
 - Newspapers, magazines, copybooks, pencils, and other articles used exclusively for education;
 - Medicinal and pharmaceutical products.
- **Services:**
 - Services related to human health;
 - The leasing or sub-leasing of real estate exclusively for the purpose of providing housing or accommodation to the lessor for a period of more than six (6) months;
 - Services associated with education or educational entities;
 - Government loans;
 - Transportation, except for passenger airline tickets;
 - Electrical power;
 - Gambling in casinos and racetracks;
 - Insurance and reinsurance;
 - Internet access service provided to residential households and educational entities recognized by the Ministry of Education;
 - Stock exchange activities;
 - Retail sales of food in commercial premises in which no alcoholic beverages are sold;
 - Professional services that are provided to persons domiciled abroad who do not generate taxable income in Panama, as well as legal services provided to international commerce vessels.

Taxpayers and Non-taxpayers

Individuals or entities that import taxable goods, transfer movable goods or provide services to or within the Panamanian territory are liable for collection from the end-consumer and for payment of this tax. Because of Panama's territoriality principle, non-residents will also be

subject to charge ITBMS tax on their services and to remit the tax accordingly to the National Treasury.

Individuals or entities that have not received during the previous year an average monthly gross income of less than US\$3,000 and a net annual income of less than US\$36,000 will not be considered as taxpayers for the next year, following a proper assessment by the tax authorities.

The ITBMS tax collected shall be remitted to the tax authorities by filing Form 430 monthly before the 15th of each month. Individuals providing professional services are permitted to file their return and remit the ITBMS tax on a quarterly basis.

The ITBMS tax paid by a taxpayer on the purchase or importing of goods as well as on services received from others may be credited to the ITBMS withholding taxes, but shall be divided and applied according to the different types of transactions: 100% taxable, mixed, and exempted.

Withholding Agents

Individuals and entities are considered as withholding agents for purposes of the ITBMS tax charged to customers, since they are in charge of remitting the amounts to the National Treasury. However, in 2015 the tax authorities introduced new types of ITBMS withholding agents, which will be responsible for withholding the ITBMS tax for their vendors or service providers:

- a) Government and public sector entities
- b) Payers to foreign service providers
- c) Entities without legal status or joint ventures
- d) Individuals or entities that, according to the tax returns filed for the previous year, disclosed purchases of goods and services above US\$5,000.000.00
- e) Companies involved in the management of debit and credit cards

Withholding agents are obliged to withhold an amount equal to 50% of the ITBMS tax billed in the invoice by the vendor or service provider, except for those paying professional services to non-resident service providers. The payer is obliged to withhold 100% of the ITBMS tax which is considered to be included in the total price of the invoice provided that the services were rendered within the Panamanian territory. Withholding agents must file a monthly report to the tax authorities to disclose their purchases and ITBMS tax withheld that will be remitted to the tax authorities.

Withholding agents are not required to withhold 50% of the ITBMS tax in the following cases:

- Transactions between the same category of withholding agents;
- Purchases up to US\$ 500.00 paid through petty cash;
- Purchases paid with corporate credit cards.

Individuals or entities that disclosed purchases of goods and services for more than US\$5,000.000.00 should be aware that this threshold can be amended by the tax authorities annually. The tax authorities will publish a list of the entities and individuals designated as withholding agents in the Official Gazette at the beginning of September of each year. Such withholding agents will be required to commence their withholding duties at the beginning of the following taxation period. Once the tax authorities have appointed an entity or individual as a withholding agent, no appeal or complaint can be submitted and the obligations as a withholding agent will remain in effect for the subsequent years regardless whether the annual purchase threshold that tax authorities might establish for that given year is met. Due to the specific

characteristics and technical features of this tax, each particular case should be explored further.



Other Relevant Taxes

Chapter 7



7 Other Relevant Taxes

Selective Consumption Tax (SCT)

A selective consumption tax (ISC as per its abbreviation in Spanish) was introduced in 2005. This is basically an excise tax on the importing of specific goods (such as luxury vehicles, motorcycles, jewelry, and firearms), alcoholic beverages/liquors and all tobacco derivatives (cigarettes and cigars) or on the initial transfer or sale by local manufacturers of these products (such as sodas, wines, and beers). The ITBMS (VAT) is excluded from the tax base for SCT purposes.

The following goods and services are subject to this tax:

- Automobiles with a CIF value of over US\$8,000.00 (some exceptions apply);
- Outboard motors larger than 150cc, yachts, sail boats, ships and recreational or sports watercraft, jet-skies, vessels and aircraft for non-commercial use, as well as helicopters;
- Jewelry and firearms;
- Cable, microwave and satellite television services;
- Mobile telephone service, including prepaid mobile phone service;
- Prizes won in slot machines operated by private enterprises specializing in games of chance;
- Taxpayers manufacturing or importing such products or the individual or company that provides the afore-mentioned services;
- Taxpayers must charge the tax and remit the sums collected to the National Treasury within the first 15 days following the end of the filing period and within three days after the customs declaration has been filed, in the case of imports;
- The tax base is the price agreed upon for the goods or services. In the case of imports, the tax base is the CIF value plus all import duties.
- The SCT is based on Law 45 (1995).
- Sugary beverages

Notice of Operation (License Tax)

- An annual tax is levied, based on the net worth of the company at a rate of two (2) percent with minimum and maximum sums, as stated in the income tax return. Net worth is understood as the difference between total assets and total liabilities. Refer to Section 1004 of the Tax Code and Executive Decree 539 of 2011.
- Except for those individuals or firms operating in the Colon Free Zone or any other free zone or free trade zones, or in an established special economic area, all individuals or firms engaging in commercial or industrial activities (either manufacturing or construction) are required to obtain a business license referred to as a notice of operation (*aviso de operación*) in accordance with Law 5 of 2007 (as described in Chapter 2), and pay tax on net assets.

- Thereafter, the annual tax is based on the net assets of the entity, which is equivalent to two (2) percent of the net assets and ranges from a minimum amount of US\$100 up to a maximum of US\$60,000 on a regular basis.
- Amounts due to foreign head offices or affiliated companies are expressly excluded from the tax base, and they should not be considered in the formula for calculating the total liabilities of such a local company.
- Executive Decree 539 of 2011 states that persons with less than \$10,000 of invested capital are exempt from paying tax.
- However, based on exceptional commercial measures, the notice of operation is not required for those companies operating within free zones although the tax is nonetheless levied with different maximum amounts. This type of taxation applies to companies operating in the Colon Free Zone and other free trade zones, or any other special economic areas such as Multinational Enterprise Headquarters (SEM, as per its acronym in Spanish), and Panama-Pacific Special Economic Areas, which are required to pay at point five percent (0.5%) of net assets, from a minimum of US\$100 to a maximum of US\$50,000.

Education Insurance Tax

- Both employees and employers must pay an education tax. Employers must deduct 1.25 percent from their employees' salaries and pay an additional 1.50 percent.
- Self-employed individuals must pay the total 2.75 percent of their annual income subject to income tax.
- Non-resident taxpayers performing services in Panama are also subject to the tax.
- This tax is deductible from taxable income for both employees and employers.
- Withholdings are paid on a monthly basis to the Social Security Administration, together with social security contributions and income tax.
- Individuals must add real estate sales in order to calculate the educational tax on their income tax return.

Stamp Tax

- In Panama, official or stamped paper costs eight US dollars (US\$8) per page and it must be used for administrative petitions, certificates, and notarized documents.
- Commercial papers and documents, such as contracts, cheques and other negotiable documents must pay a stamp tax by submitting a declaration form within 15 days after the end of the month following the transaction or by other authorized means.
- The amount of stamp tax depends on the value of the document, and on whether the document is a cheque, negotiable instrument, landing permit, bill of lading, or any other document.
- Contracts and documents must be taxed at a rate of ten (10) cents for each US\$100 of the value stated in the document.
- Receipts of money, bills of sale and services and legal recourse are exempt.
- The stamp tax can be printed using a postal meter.
- Taxpayers can also pay this tax every month, quarter, or semester by filling out a form.

Import Duties

- All imports are subject to import duties unless specifically excluded by law or through incentive contracts with the government.
- Import duties must be paid within three working days from the day that the import documents are presented.
- Rates vary according to the local availability of items and tariffs applied in each case.

- The tax base is defined as the cost, plus insurance and freight (CIF) charged to the importer.
- In the case of goods imported by air, or when the CIF value is unknown, the same amount is determined by adding 15 percent to the freight on board (FOB) value.
- In some cases, specific duties, such as amounts per kilogram or linear foot, are maintained.
- Sworn import declarations are processed through customs brokers.
- The Executive Branch (through the Council of Cabinet) grants the authorization to increase or decrease import duties.

Tax on Insurance Premiums

- All insurance operations in Panama are subject to a tax levied on the issuance of insurance policies.
- The tax is payable by the insurer, while the taxpayer is the person subscribing the policy.
- The tax is levied at two (2) percent of the premium for all insurance sold in the Republic of Panama covering local risks.
- An additional tax of five (5) percent is applicable to fire insurance premiums, whose total tax percentage is seven (7) percent, five (5) percent of which is assigned to fire departments in Panama.
- The stamp tax is calculated on the amount of premiums involved.

FECI (or one percent tax on loans)

- Applicable to local personal and commercial loans, for more than five thousand dollars (\$5,000.00), granted only by banks and financial institutions, would be subject to a withholding of one percent (1%) rate on the amount that serves as the basis for calculating interest (Interest Compensation Special Fund or FECI).

Municipal Taxes

- Municipalities must follow specific rules under the Panamanian Constitution and Law 109 of 1973. Taxes are based on the type of activity and the gross income amount or the sales volume.
- Taxes may be assessed by municipalities, among other taxes, on automobile licenses, buildings and improvements, sidewalks, streets and municipal land.
- Also, most commercial and industrial activities are subject to municipal taxes, from small businesses and workshops to power-generating companies.
- Private piers, for instance, generate twenty thousand US dollars (US\$20,000) per month of tax in Panama City.
- The Municipality of Panama has its own clearance certificate ("paz y salvo municipal"). It costs one US dollar and is required for the following purposes:
 - Signing contracts with the municipal administration;
 - Obtaining a new automobile license each year;
 - Receiving a license or permission to operate profit-oriented businesses within the city.

Tax on Banking Institutions

- A special tax is levied on all banks established in Panama regulated by Law Decree 9 of 1998 and also on trading houses.
- These taxes are transferred to the Superintendency of Banks for its operations.
- Payment is due within the first 90 day-period after the end of the taxation year.

ANNUAL TAX ON BANKING INSTITUTIONS*

Type of financial institution (PAB)	Amount of tax (US\$)
Generally licensed banks	
Up to \$100 million in total assets	\$75,000
From \$100 million to \$200 million in total assets	\$125,000
From \$200 million to \$300 million in total assets	\$175,000
From \$300 million to \$400 million in total assets	\$250,000
From \$400 million to \$500 million in total assets	\$375,000
From \$500 million to \$750 million in total assets	\$450,000
From \$750 million to \$1,000 million in total assets	\$500,000
From \$1,000 million to \$2,000 million in total assets	\$700,000
More than \$2,000 million in total assets	\$1,000,000
During their first year of operations, the new generally licensed banks are asked to pay 50 percent of this annual tax.	
Internationally licensed banks	\$75,000
Banks promoting investments and micro-financing activities	\$30,000
Currency exchange	\$10,000
*Legal base: Section 1010 of Tax Code	



Real State Property

Chapter 8



Chapter 8

8

Real Estate Property

Different Taxes on Real Estate Property

Three different types of taxes apply to real estate property: the Real Estate Tax, the Capital Gain on Transfer Tax, and the Transfer Tax.

Real Estate Tax (IBI)

The Real Estate Tax is a direct tax which consists in taxing real estate located within the Republic of Panama. The tax base depends on the total value of the real estate, plus all improvements. Real estate transactions at prices above the appraised value automatically increase the value of such properties for tax purposes.

In 2017, the Real Estate Tax was overhauled, with the tax base being significantly reduced. These tax cuts will begin to take effect in 2019. Real estate values will be established by the National Land Administration Authority. They will take into account the market value increase and calculate the 60 per cent. One of the new characteristics of this law is the new distinction made between Family Tax Patrimony and the Primary Household. The Family Tax Patrimony establishes a system whereby a family consisting of a married couple and children have a different tax treatment. On the other hand, under the primary household system, an individual, or persons who are not legally married, have their house as their primary place of residence.

Family Tax Patrimony	Primary Household
Corresponds to real estate intended for permanent use by the property owner for housing purposes with his/her family, living under the same roof. Family is understood as the concept that, for this purpose, is established in the Family Code to build a family patrimony.	It will be property that is used permanently by the owner of the real estate, for residential purposes, among other residential real estate and that does not constitute a family patrimony.
It can be owned by an individual or companies and also, regardless of the existence of a mortgage lien on the real estate property or of a guaranteed trust.	
In case the real property is in the name of a Private Interest Foundation or trust, the names of the beneficiaries of said property must be certified by means of an affidavit.	

The reform bill established thirteen types of real estate that are exempted from this tax:

1. Government real estate and real estate owned by municipalities and municipal associations.
2. Autonomous and semi-autonomous government real estate.
3. Real estate intended to be used for religious purposes.
4. Real estate intended to be used for charity or social assistance, or by non-profit organizations.
5. Real estate exempted according to international treaties or agreements in which the Republic of Panama has been a party to the contract, and approved by law.

6. Real estate with a value below US\$120,000.00 (Family Tax Patrimony and Primary Household).
7. Other Real estate with a value below US\$30,000.00.
8. Real estate belonging to social organizations, which are non-profit operations.
9. Real estate intended for agricultural activities and whose value does not exceed US\$350.000.00.
10. Individuals or companies that offer private education services. They can deduct their real estate tax to zero, by offering permanent scholarships to Panamanian students. Private hospitals also have this option.
11. Real estate intended to be for public use.
12. Real estate belonging to persons with a disability. Such real estate must be the person's primary place of residence.
13. Real estate that consists of land and/or improvements, according to what is established in the special laws for the corresponding term.

The new bill established a different combined progressive rate, which is divided into two sections: real estate which is intended to be used as a primary place of residence or house or a familiar patrimony, and other real estate (i.e. commercial, industrial, and other residential real estate). The real estate tax shall be paid in three instalments: the first no later than April 30th, the second on August 31th, and the last one on December 31th. The new bill gives the taxpayer the opportunity to have a ten per cent discount in the scenario that the tax is paid in the first two months of the year. This applies to both individuals and companies.

The combined progressive rate for the primary place of residence is as follows:

Tax Base	Tax Rate	Amount to be paid
\$0 - \$120,000	0.00%	US\$0
\$120,000 - \$700,000	0.50%	US\$0 on the first US\$120,000, with excess amounts being taxed at the rate of 0.50%, up to \$700,000.
Amounts exceeding \$700,000	0.70%	US\$4,900 on the first US\$700,000, with excess amounts being taxed at a rate of 0.70%

On the other hand, the combined progressive rate for the other type of real estate as follows:

Tax Base	Tax Rate	Amount to be paid
\$0- \$30,000	0.00%	US\$0
\$30,000- \$250,000	0.60%	US\$0 on the first US\$30,000, with excess amounts being taxed at a rate of 0.60%.
\$250,000- \$500,000	0.80%	US\$150 on the first US\$250,000, with excess amounts being taxed at a rate of 0.80% up to \$500,000.
Amounts exceeding 500,000	1.00%	US\$4,000 on the first US\$500,000, with excess amounts being taxed at 1%.

Preferential Interest Rates

Amendments to Law 3 of 1995 pertaining to preferential interest rates have also been made. The government created what is called the preferential variance. This is the difference between the reference rate and the lower rate. This preferential variance will not exceed 4% for real estate mortgages and the related financing represents more than \$40,000.00 but no more than \$120,000.00. The government will cover the full amount of this preferential variance. For example, if the Interest Rate for a Home Mortgage with a value of \$110,000.00 is 6.5%, the debtor will only have to pay 2.5%.

Tax on the Transfer of Real Estate (ITBI)

The two (2) percent tax levied on the transfer of real estate, whichever is higher, is based on:

- The sale price stated in the official deed; or
- The officially assessed property valuation.

The official property value is calculated on the registered land value, plus the value of the improvements made to the property. Also, an amount equivalent to five percent (5%) of the property value, plus improvements, for each calendar year between the acquisition date and the selling date is added.

Exemptions

- The initial sale of a residential property is exempt from this tax if the buyer uses the property as a personal place of residence and if the sale takes place within two years after obtaining an official occupancy permit;
- Exemptions exist for donations made to the State and to relatives within the first degree of consanguinity (parents to children or children to parents) as well as between spouses.
- Real estate transferred to trusts.

False declarations on the transfer value of the real estate property will be considered as fraud by the tax authorities, for both the seller and the buyer, and both can be subject to stiff penalties.

With regard to Law 5 of 2006, the two percent ITBI tax is deductible from income tax, but only for real estate companies or individuals doing business involving real estate (having sold more than ten properties).

Capital Gains Tax

If the taxpayer's usual business does not include purchasing and selling real estate properties, the capital gains tax on real estate transfers will be applied at a rate of 10%. The seller has the obligation to pay a 3% advance on the 10%, which is equivalent to the capital gain.

Nevertheless, the taxpayer can opt to pay 3% of the total transfer value. When the 3% advance is greater than the amount resulting from application of the 10% capital gain tax, the taxpayer can obtain the excess amount in return.

Withholding Agents

There are now new withholding agents, which include generally licensed banks, financial entities, cooperatives and the other institutions that grant financing for the acquisition of housing or real estate in general or by way of credit secured with real estate.

The withholding does not apply to real estate consisting in the family tax patrimony or the primary household of taxpayers.

This obligation to serve as a withholding agent does not generate a joint and several liability for these entities. However, agents are obliged to notify taxpayers regarding the balances still to be paid.

The Directorate General of Revenue will grant a tax credit to these entities for the costs incurred to implement systems to act as a withholding agent.

Power Generation Companies

The maximum amount to be paid annually is modified to take this tax into account. Prior to the amendments, the maximum amount to be paid by this industry was US\$25,000.00 per year. However, with the new amendments this limit has been increased to US\$ 50,000.00 per year.

Exemption for New Improvements

The new changes to state properties that are exempt for new improvements made for housing or commercial purposes and special laws will remain in effect until the term granted by the corresponding law.



Traditional Areas for Doing Business

Chapter 9



Chapter 9

9

Traditional Areas for Doing Business

Panama encourages investment from both foreign and national investors, offering equal constitutional protection and non-discriminatory laws and regulations. Furthermore, there are a number of taxes and financial incentives for companies that choose to set up operations in Panama.

Micro, small and medium ('MSM') businesses

For purposes of Law 33 of 2000, as amended by Law 72 of 2009, micro, small and medium businesses (hereinafter, "MSM businesses or enterprises") are defined as those enterprises whose annual gross income or invoicing ranges between US\$150,000 and US\$2,500,000 as shown in the chart below:

MSM businesses	
Enterprises	Gross income or invoicing
Micro	Up to US\$150,000
Small	From US\$150,001 to US\$1,000,000
Medium	From US\$1,000,001 to US\$2,500,000

The afore-mentioned regulation establishes a special system for these types of commercial enterprises, in regards to financial, administrative and tax matters.

Tax Incentives

- For micro businesses, the alternative calculation of income tax (CAIR) introduced into the tax system in 2005 is not mandatory and will not be applied; such businesses are also exempted from income tax for their first two years of operation. Small businesses are also excluded from the alternative calculation, because this only applies to medium-sized businesses whose taxable income is greater than US\$1,500,000.
- For MSM businesses or enterprises, the portion of taxable income attributed to annual gross income up to US\$100,000 is treated in the same way as for individuals or natural persons (i.e. amounts are paid based on individual income tax rates instead of corporate tax rates).
- If the annual gross income is between US\$100,000 and US\$200,000, MSM businesses are required to apply the corporate income tax rate. However, they are not subject to complementary income tax on dividends or to dividend tax.

In order to benefit from the tax measures discussed above, the Panamanian Tax Code (article 699-A) states that:

- The MSM enterprise should not be the result of a business that was fragmented into different legal entities, nor should it be a subsidiary, affiliate or business controlled by another legal entity;
- Annual gross income of the MSM business should not exceed US\$200,000;

- The enterprise's shares, stocks or ownership stake should be nominative and shareholders should be individuals.

On the other hand, any micro or small business that has been granted benefits under Law 9 of 1989 (i.e. former micro and small business incentive law) will continue to enjoy such benefits in accordance with the terms and conditions for which they were granted.

Agricultural Sector

The Ministry of Agricultural Development is responsible for the agricultural sector, which benefits from general tax incentives as well as specific export-oriented benefits. According to the Panamanian Tax Code, the following exemptions are granted to agricultural activities:

- Annual gross income of less than US\$350,000 is totally exempt from income tax, and there is no obligation to file an income tax return;
- Total exemption from real estate tax on farms or properties used for agricultural or livestock activities, having a cadastral value under US\$350,000;
- A special income tax on the transfer of real estate property used for agricultural purposes or activities, having a three percent fixed rate for capital gains;
- Total exemption from income tax on sums donated to non-profit research agricultural business institutions.

In addition, the Interest Compensation Special Fund (called FECI as per its Spanish acronym) aims to benefit the agricultural sector according to Law 4 of 1994, which also offers an interest rate discount on local loans for agricultural and livestock activities.

Executive Decree 9 of 2009, which amends Executive Decree 74 of 2008, was introduced with the purpose of helping to eradicate the growing worldwide food crisis. This Executive Decree offers interest discounts on financing for the production of certain food products such as rice, corn, kidney beans, meat, and fresh milk. Moreover, the Superintendence of Banks created top interest discounts of 3.5 percent on loans granted for the qualifying agricultural sector and export agro-industrial sector, as well as a 4 percent discount on loans granted for the production of the afore-mentioned food products (Resolution FECI 053-2008).

Agricultural activities, livestock production and exports

- Law 2 of 1986 establishes incentives for agricultural and livestock production, as well as exports.
- Activities that are covered within the scope of the benefits granted by this law are: (1) production of food, forest and agricultural raw materials; (2) commercial raising of cattle, hogs, poultry and other animals; (3) processing of the above-mentioned products utilizing no less than 50 percent of local raw materials; (4) production of fertilizers and other chemicals for agricultural use, even if no local raw materials are used; and, (5) the financing of equipment, goods and animals for agricultural and livestock production and processing.
- Tax incentives are granted by means of Decree 51 of 1990, to banks and financial institutions providing credit facilities and loans aimed at improving the agricultural, livestock and agricultural industry sectors.
- Revenues from interest and commissions earned from such loans are exempt from income taxes, provided that: (1) such loans are used exclusively in the financing or refinancing of investments in these sectors; (2) the payment term of the loan must be no less than three years, including a grace period of no less than one year for the payment

- of capital; (3) the loan generates interest at a rate no greater than the market rates; and
- (4) the lender is a bank or credit institution.

Industrial Sector

Since the 1950s, the Panamanian Government has shown a continued commitment to attract foreign direct investment (FDI) for industrial activities. For these purposes, the Republic of Panama has granted a number of tax measures (including exemptions, targeted tax deductions, tax credits and tax rate reductions) designed to attract economic investment.

Certificate to foment industry (or CFI)

Law 76 of 2009 creates the CFI, a certificate to promote the manufacturing, agro-industrial and marine resources processing industries. The certificate is only available to certain types of enterprises that meet the requirements established by law. These qualifying entities are eligible to receive a CFI recognizing 40% of the amounts invested in research and development. The beneficiary of the CFI can apply the credited amount to pay all national taxes, fees or contributions, with the exception of:

- Withholding taxes.
- Dividend or complementary tax.
- Consumption tax on fuel and oil products.
- Any taxes, fees or contributions that correspond to previous tax periods, before the CFI was issued.

Types of Systems

- Enterprises registered with the Official Register for National Industry (ROIN), that have signed a contract with the government, or that are entitled to derive benefits from the tax incentives system until its scheduled expiry;
- Enterprises not registered with the ROIN were subject to a revised extension until 2007 as a result of World Trade Organization (WTO) rules.

Industrial benefits

- Under Law 11 (2008), enterprises continue to be subject to a special system if they:
 - 1 Are registered with the Official Register for National Industry (ROIN); or
 - 2 Have a signed contract with the government under the aegis of Cabinet Decree 413 of 1970; or
 - 3 Are entitled under a Contract for Industry Promotion.
- The primary benefit of this law was the extension of ROIN up to December 31, 2015. However, Law 25 of 2017 extended the date until December 31, 2020, without the need to file a petition.

Export-oriented Companies

Export-oriented companies are governed by Law 28 of 1995 and Law 26 of 2001. These laws created a preferential rate import tax of three percent (3%) for costs, insurance and freight (CIF). This applies to specific raw materials, intermediate goods and capital assets, regardless whether the importers are registered with the Official Register for National Industry.

The Panamanian Tax Code establishes special import duties, as follows:

- Customs repayment shall permit the investor to obtain a reimbursement for all taxes paid at the time of importing the merchandise used in the process of producing the exported goods, at the time of export;

- An exporter who claims the benefit shall receive a refund of the taxes paid at the time of import;
- Replacement of inventories with a customs exemption should allow the importing, with the exemption of import duties, of equivalent merchandise, that is similar in kind, quality and technical characteristics, to the legally imported merchandise and that should be utilized to obtain products that previously were permanently exported;
- The temporary admission of goods for active finishing should allow the investor to receive, within a customs territory, the suspension of import duties and taxes, in addition to a guarantee bond for the amount of the respective import duties and taxes, for merchandise to be exported. This applies for a determined period, after having been processed, manufactured or repaired.
- Temporary admission of goods for passive finishing allows the investor to export, for a determined period of time, domestic or national merchandise, for processing, manufacturing or repair abroad, and later to be re-imported with a total or partial customs exemption from import duties and taxes.

Pharmaceutical Industries

- Law 28 of 1995 states that supplies, packaging materials and raw materials for national pharmaceutical industries needed for the manufacturing of medical products shall be declared free from import taxes and duties, as well as local VAT (ITBMS, for its Spanish acronym);
- Local purchases of packaging materials used by manufacturers to package medicines shall be exempt from the ITBMS;
- Medicines and pharmaceutical products are exempted from the ITBMS;
- Furthermore, transfers by importers and manufacturers of food, pharmaceutical products or medicinal products for human consumption shall be likened to those exporters for the purposes of applying for a *Certificado con Poder Cancelatorio*, or *CPC* tax credit.

Unfair Business Practices

- Under Law 45 of 2007, which supersedes Law 29 of 1996, a regulation has been adopted that addresses antitrust, unfair business practices and antidumping measures. This regulation was introduced in order to modernize the Panamanian legal system in accordance with the requirements of the World Trade Organization (WTO).
- Unfair business practices include monopolies, subsidies, grants and dumping.
- The main objective is to protect the national industry and production against monopolistic practices and uncompetitive foreign trade activities that threaten the development of national industries.
- The antidumping measures are designed to protect the national production from massive foreign imports of similar or equivalent goods.
- Antidumping measures can be adopted by increasing tariffs, establishing contingency rates, implementing restrictions on the amount of imported goods, and any other measure that complies with international agreements signed by the Republic of Panama.

Fossil Fuel Operations

Law 8 of 1987 promotes and regulates:

18. The exploration and exploitation of oil fields, asphalt in its natural state, natural gas and other fossil fuel activities;
19. Refining and transportation of fuel by pipeline;
20. The storage, marketing and export of exploited or refined substances.

The Ministry of the Presidency, through the National Secretariat of Energy, is the entity in charge of granting exploration permits for geological, geochemical, and geophysical exploration.

- Concessionaires assume all the risks, liabilities, and costs by supplying capital, machinery, equipment, materials, personnel, and technology;
- Partial or total assignment of rights and subcontracting are allowed provided that the National Secretariat of Energy grants appropriate authorization for this;
- Petroleum free trade zones are described in Chapter 12. Please refer to this chapter for the importing of hydrocarbons and trade regulations.

Tax Benefits

The tax benefits for fossil fuel operations are as follows:

- During the period of operation, contractors shall pay a minimum of 15 percent and a maximum of 30% (liquid hydrocarbons) and a minimum of 5 percent and a maximum of 15 percent (gas hydrocarbons) on the net production of such products, in accordance with the terms of the agreements.
- Contractors are granted a total exemption from import duties on machinery, equipment, parts and any other items deemed necessary for the performance of the activities referred to in the contract.
-
- Special depreciation schedules for machinery and equipment (12.5% annual cap).
- Special carry-over provisions for income tax purposes.

Maritime Registry

Since its creation in 1925, the Panamanian Maritime Registry has experienced tremendous growth.

Law 8 of 1925 created the National Merchant Marine, when the open registry system was adopted and nationality and residency restrictions were eliminated.

Since then, the Panamanian Maritime Registry accepts ships belonging to Panamanian citizens and foreign nationals alike, provided that all legal provisions in effect are respected, especially those governing the administration of vessels, safety and pollution control standards, technical criteria and fiscal matters.

The Panamanian Maritime Registry offers ship owners the following advantages:

- An open registry policy, which allows any individual or company, notwithstanding their nationality or place of incorporation, to become eligible to register ships under the Panamanian flag;
- Total exemption from income taxes on income derived from the operation of vessels engaged in international trade;
- Minimum tonnage not required. However, vessels that are 20 years old or older will have to pass a special inspection in order to obtain a permanent navigation patent;
- A provisional ship registration valid for six months may be obtained in Panama through a lawyer, or in ports where an authorized Panamanian Consul is present;
- Dual registry, as long as this is allowed by the country which granted the vessel's original registration;
- Flexible regulations to contract crews to operate the vessel;

- The Bareboat Charter System - this system allows a foreign vessel to register in Panama for a two-year period without losing its previous registration. A certificate of consent from the country where the vessel was originally registered will be required.

Law 55 of 2009 covers maritime commerce and replaces the Commercial Code section referred to and Law 57 of 2008 deals with general maritime trade.



Special Economic Zones and Systems

Chapter 10



1. Colon Free Zone (CFZ)

Since its creation in 1948, the Colon Free Zone (CFZ) has been a segregated free trade area for wholesale operations. Currently more than 3,000 companies operate in this area, with the most important activity being product re-exports.

The Colon Free Zone is located at the Caribbean entrance to the Panama Canal and the Expanded Panama Canal and approximately an hour and a half by highway from the airport and one hour from Panama City.

It is the largest free zone in the Americas and the second largest in the world, as well as the first container distribution center in Latin America, offering the world a unique place for international commerce and becoming the leading free zone in the hemisphere and one of the largest and most important global logistics centers. Also, the CFZ is an institution with ISO 9001-2008 certification.

Goods (except firearms or petroleum products) may be imported, stored, modified, repackaged, and re-exported without being subject to any customs regulations, and those goods entering the CFZ are exempt from import duties. A surveillance service fee is charged by customs authorities for the custody of exported goods. The fee charged varies depending on the exported goods.

Commencing operations in the Colon Free Zone (CFZ)

- To operate from the Colon Free Zone, companies must obtain authorization from the CFZ Administration (an autonomous government institution).
- This means that no business license (notice of operation) is required. However, an “operating key,” which is the number that identifies a company in the Colon Free Zone and that allows it to carry out its operations according to its stated commercial activities, must be obtained.
- There are three types of operating keys, namely:
 - User company
 - Represented company
 - Storage in a public warehouse
- Companies do not need to comply with any minimum investment requirements.

Permitted activities in the Colon Free Zone (CFZ)

- Import;
- Export;
- Re-export;
- Manufacturing;
- Sale, commercialization and distribution;
- Refining and processing of goods;

- Operations, transactions, negotiations or incidental activities appropriate to the establishment and operation of international free trade zones.
- The provision of services relating to aviation and airport operations, including the transportation, handling and warehousing of cargo in general;
- Construction of ports, docks, boatyards, ports or places of loading and unloading;
- SEM entities, companies incorporated under the City of Knowledge regime and call centers can set up offices within the Colon Free Zone.

External Operations

The following activities, also known as “export activities”, are considered external operations and are therefore exempt from corporate income tax: (1) Sales of local or foreign merchandise for export or re-export; (2) transfers of merchandise to be exported, within the CFZ or from one free zone to another; (3) logistical services related to export activities, such as storage, bonds, internal moving of merchandise and cargo, invoicing, re-packaging, etc., when the results of these services are seen abroad.

Internal Operations

Activities intended for the local Panamanian market (secondary customs territory), also known as local or domestic operations, will be subject to income tax:

1. Sales or transfers of goods from the CFZ (primary customs territory) to the rest of the customs territory within the Republic of Panama, either directly or through an intermediary or consolidator.
2. The disposition or transfer of real estate and the provision of services to individuals or legal entities located within the Colon Free Zone and other free zones that exist or are created in the future.
3. Leasing and subleasing activities.
4. Services such storage and warehousing, the internal movement of goods and cargo, billing, collection, repackaging and similar services provided to individuals or legal entities, when the merchandise or cargo is destined for the customs territory within the Republic of Panama (secondary customs territory).

The provision of services to individuals or legal entities located outside or within the territory of the Republic of Panama is considered to represent internal operations subject to income tax.

Tax Treatment and Incentives Granted to Companies Within the CFZ

- No income tax on profits derived from external operations; services provided to persons located abroad are not considered external operations.
- Income tax rate of 25% over the net income derived from internal operations.
- Dividends are subject to a dividend tax at a reduced rate of 5% regardless of the source of the income (external or internal operations).
- The transfer of goods within the CFZ and the logistical and ancillary services related to the cargo are not subject to ITBMS (local VAT). In addition, companies established within the CFZ are exempt from taxes on the re-exporting of capital.
- Royalties paid to companies incorporated abroad are not taxable for the beneficiary, but the expense is not deductible for the recipient.
- There are no consular fees, or any other charges, levied on shipments destined to the Free Zone, or on shipments from this area to consignees abroad.
- There is free movement of goods and an exemption from import duties.

- Municipalities are not permitted to collect taxes or any other charge for goods entering or leaving the CFZ. However, companies are subject to a municipal improvement tax of 2% on the value of the improvement.
- Entities established within the CFZ are subject to capital gains tax on the transfer of securities as well as on movable and immovable properties.
- Even though no notice of operation is required (formerly referred to as a business license), companies are subject to an annual equity tax commonly known as the Operation Notice Tax at a tax rate of 0.5% on the amount of capital, with a minimum tax of US\$100 up to a maximum of US\$50,000.
- Staff working within the CFZ pays income tax at regular rates, subject to the territoriality principle as discussed in Chapter 5.

2. Free Trade Zones (FTZ)

The free trade zones are special export-oriented areas with a particular tax and labor system mainly based on Law 32 of 2011. The FTZs are free zones for the establishment and development of industrial, commercial and service enterprises.

Any individual or legal entity willing to register with the Registry of Companies established in the FTZ must be duly authorized to operate and carry out the permitted activities within the FTZ. In other words, a company can only be established within a free trade zone by means of a User License duly granted by the FTZ National Commission of the Ministry of Commerce.

Only the following activities can be carried out within the FTZ: services, manufacturing, assembly, logistical services, high tech services, the processing of finished or semi-finished goods, scientific research centers, environmental services, specialized centers for the provision of healthcare services, centers of higher learning, general services to users within the Free Trade Zone. Import and export activities not subject to value-added processes are expressly prohibited.

The tax incentives granted to companies established in the FTZ are applicable to external operations only (export operations), which cover the transfer of all types of merchandise or goods and the provision of services to any natural or legal entity located abroad or established within a special free trade area. On the contrary, activities destined for the local Panamanian market (secondary customs territory) will be subject to income tax and ITBMS, as well as import taxes.

Although, in principle, exempt from all direct and indirect taxes, companies established in FTZs will be required to pay the following taxes:

- Income tax and ITBMS on local leasing and subleasing activities, as well as internal operations.
- Dividend tax, at a rate of 5% and complementary tax, at a rate of 2%.
- Annual tax, at a rate of 0.5% on the company's capital, with a minimum of US\$100.00 and a maximum of US\$50,000.00.
- Selective consumption tax.
- FECl, except on loans guaranteed by bank deposits.
- Social security contributions.

Labor and employee migration system:

- The employer may rotate employees between different positions, as long as working conditions are not diminished.
- Overtime may not exceed three-hours per day and shall be remunerated by way of a flat 25 percent increase in the hourly salary; and
- Furthermore, there is flexibility to fix vacation periods according to production cycles.
- Employment relationships may be terminated based on market fluctuations.
- Free Trade Zones are subject to a special migration system.
- Staff working within the CFZ pays income tax at regular rates, subject to the territoriality principle as discussed in Chapter 5.

3. Baru Free Zone

Law 29 of 2010 establishes a Special Economic Area in the District of Barú, Chiriquí Province. In addition to tax incentives, this law includes migration and labor incentives.

The main tax incentives granted under this system regime include: an exemption from import taxes in respect of any finished goods, materials, equipment, furniture, accessories, appliances, services used in operations; an exemption from all taxes in respect of all types of products introduced into the area for agro-industrial activity (excluding vegetable oils and fats) and oil processing; an exemption to have a Notice of Operation and an exemption from the Stamp Tax; ITBMS (local VAT); real estate taxes and real estate transfer taxes.

4. Oil Free Trade Zones (OFTZ)

- Law 8 of 1997 and Executive Decree 36 of 2003 establish a national policy regarding hydrocarbons in Panama and included a chapter dedicated to oil free trade zones (formerly known as petroleum free zones) where companies are granted tax benefits.
- According to Law 8 of 1997 and Executive Decree 36 of 2003 companies duly authorized to operate in an OFTZ are exempt from all direct and indirect taxes, levies, duties, fees and rights related to the transfer of movable and immovable property, the purchase of equipment and supplies, raw materials, machinery, tools, accessories and supplies and all goods required for import, export and re-export operations of oil and derivative products.
- Within any Oil Free Trade Zone, individuals or corporations, whether Panamanian or foreign nationals, may carry out the following operations, among others, under a special tax free system: introducing, storing, manufacturing, bottling, refining, purifying, mixing, marketing, transporting, transferring, pumping, processing, transforming, selling or in any other way disposing in the domestic market, exporting, re-exporting, providing and, in general, operating and managing crude or semi-processed oil or any of its by-products.
- The sale of oil and its derivative products intended for the local Panamanian market (secondary customs territory) will be subject not only to income tax and ITBMS (local VAT) but also import taxes.
- The tax incentives granted to companies established in an OFTZ are applicable only to external operations, as well as other activities expressly exempted in Cabinet Decree 36 (2003), among others.
- Companies can import, re-export, store, trade and sell oil products to ships in transit through the Panama Canal.
- Crude oil and petroleum-derived products can enter and exit petroleum free zones without paying income tax, import tax or any other tax (except when destined for Panamanian customs territory).

- Export and re-export sales operations are exempt. This includes sales made to ships in transit through the Canal or those sales made to ships and aircraft on international flights that use Panama's port and airport facilities.
- For consumption purposes, power generation companies are totally exempt from import tax when acquiring crude oil and derivative products, even when those products are introduced within the customs territory.

5. City of Knowledge and the International Technological Park (or Clayton)

Law Decree 6 of 1998 approved the contract law contract for the City of Knowledge, which is a foundation created to promote educational and scientific research within an area formerly used as a military base (Clayton). The International Techno-Park of Panama is located in the City of Knowledge and its objective is to host innovative businesses that produce, assemble, process or render services for high tech products destined for sale in the local or international market. This area is provided with the following tax exemptions:

- Import tax upon materials and equipment related to projects;
- ITBMS;
- Real estate tax;
- Taxes on funds related to projects remitted abroad;
- Taxes on equipment related to innovative enterprises with high technology standard goods and services;
- Also, private, non-profit foundations may settle in this special area in order to accomplish a social mission, such as education or research.

6. Tocumen International Airport Logistics Zone

The Tocumen International Airport is an international air terminal managed through a corporation that is wholly owned by the Panamanian state. To potentiate Panama's role as a logistical platform, the board of directors of Aeropuerto Internacional de Tocumen, S.A. decided to register the airport as a free trade zone. The Cabinet Council approved this decision through Cabinet Resolution No. 102, dated May 20, 2014.

Resolution No. 7, dated April 19, 2016, authorized the registration of Tocumen International Airport as a free trade zone that will offer tax, migratory and labor benefits, as well as investment and business stability to the entities that wish to operate from this free trade zone. Regulations on these matters have not yet been issued.

The development of the Tocumen International Airport Logistics Zone began in 2018 and is expected to be completed within a period of eighteen (18) months. This zone will focus on logistics and value-added manufacturing activities, specifically perishable products, pharmaceutical products, e-commerce, and spare parts.

7. Old Quarter ('Casco Viejo')

Founded in 1673, after the former capital Panama Viejo burnt down and was looted during a pirate attack, Casco Viejo (Spanish for Old Quarter), also known as Casco Antiguo or San Felipe, was once the hub of Panamanian culture and civilization over three centuries.

Casco Viejo is not only the historic district of Panama City designated a World Heritage Site by the United Nations Educational, Scientific and Cultural Organization (UNESCO) in 1997 but is also one of the most attractive colonial zones for tourism in Latin America, with a wealth of historical locations, museums, trendy coffee houses, gourmet restaurants, boutique hotels, and some of Panama's hottest clubs and bars.

Restoration of this incredibly beautiful World Heritage Site became a trendy development in the last decade, when incentives for the Old Quarter were introduced by means of Law Decree 9 of 1997, which granted special tax incentives for the restoration of historical monuments and buildings located in “Casco Antiguo”.

More specifically, in order to continue encouraging the recovery of "Casco Viejo", Law 136 was enacted on December 31, 2013 to update "the applicable tax system for the rehabilitation and enhancement of the Historic Monumental Complex of the Old Town of Panama City".

Law 136 of 2013 renews the incentives granted by Decree Law 9 of 1997, since many had expired in 2007. Recently, Law 53 of 2017 modified Law 136 of 2013, extending the incentives for social interest projects and, most importantly, introduced an extension of the period to begin the investment plan or the incentivized activities for owners or investors up to ten (10) years after the enactment of the law. In fact, the amendments extend some incentives beyond 2030, as follows:

Tax incentives for financing activities

- Financial entities which grant mortgage loans will receive a tax credit equivalent to the difference between the regular and preferential interest rates.
- This benefit will last throughout the term of the loan, but will not be transferred if the loan is extended or refinanced.
- Over and above the tax credit, any amount not used in a taxation year will be applicable for up to three (3) following tax years or even could be transferred to another taxpayer.

Tax incentives for property owners and investors

- Individual or corporate income can qualify for a tax deduction in respect of the total amount donated for the construction, restoration, expansion, maintenance, illumination or improvement of parks, historical walls, green spaces and churches within the “Casco Antiguo” (in accordance with the current legislation governing Panama’s historical heritage). There is a total exemption on import duties pertaining to the equipment and materials used in construction and restoration activities, and to equip establishments within the historical area, provided that those materials or equipment are not produced or are minimally produced in Panama and are not imported for resale to third parties.
- A ten-year income tax exemption, from the date of issuance of the occupancy permit of built, rebuilt or restored property, in respect of profits derived from commercial activities or the sale or transfer of any property within the historical area.
- A thirty-year exemption of real estate tax on land and improvements from the date on which the occupational permit was granted, provided that the permit was obtained while the law was in effect.
- The initial transfer of a built, rebuilt or restored property from the date of enactment of the law will be exempt on the 2% tax on transfer of real estate.

Tax incentives for tenants

- A person renting a property intended for housing within Casco Viejo may consider as a personal deduction in his or her income tax return the amount paid during following five years from the date on which the occupancy permit was granted.

Tax incentives for public parking lots

- Individuals or legal entities, whether as owners, promoters or landlords, will be exempt from income tax, for a period of ten years, on profits derived from public parking lots within the historical area from the date of issuance of the occupancy permit.

8. Call Centers

Law 54 of 2001, modified by Law 52/2018, provides tax benefits to call centers established in Panama for commercial operations by foreign investors, treating them as “Free Trade Zones” and establishing the registry before the General Directorate of Free Zones of the (MICI).

Companies that operate under a Call Center Concession, granted by the Public Services National Authority (ASEP, by its Spanish acronym), are exempted of Direct Taxes, Indirect Taxes, Contributions, Duties regarding its operations. This exemption is conditioned to the Company having a minimum of five (5) employees, seventy per cent (70%) of its expenses must be related to its operations, and some annual regulatory filings required by law.

Other tax incentives granted to call centers include:

Tax and import fee exemptions on raw materials, semi-manufactured products, reinvestments and the purchase and sale of equipment, construction materials, machinery, spare parts, tools, accessories, packaging materials and all goods or services required for their operation. Exemption from the notice of operation (capital) or property taxes.

Exemption from income tax on certain services related to storage and warehouse services, high technology companies, scientific research centers, centers of higher learning, health and environmental services, among others.

According to the Law, call centers must be based in Panama and must own an operating concession for commercial export purposes, granted by the ASEP. Call centers can be registered in the MICI’s General Directorate of Free Zones and thus benefit from the incentives of the law governing special economic areas, discussed in the following pages.

9. Other Economic Zones in Panama

Business incentives in Panama predominantly focus on certain business activities and are focused on specific locations or zones, as outlined above. In addition to other zones mentioned, the following special zones are also closely regulated.



Panama- Pacífico Area

Chapter 11

Chapter 11

11 Panama-Pacifico Area

Panama-Pacifico Area (APP)

Through a government agency created for the Panama-Pacifico Area (*Agencia Panama-Pacifico*) and a private Developer¹ (London & Regional), the APP was developed in order to offer real estate opportunities under the aegis of Law 41 (2004), which creates and regulates this special area.

The Panama-Pacifico Area (hereinafter, “APP” for its Spanish acronym) is a tax-free area with a special customs, labor and immigration system. Its purpose is to increase the trading of goods, services and capital, promoting investment and employment.

Location

The APP is located in the former Howard US Air Force Base on the Pacific coast of Panama (west of the Canal).

Scope of Business

Unlike the CFZ, which is mainly involved in import and export operations, the APP has an extremely broad scope of business, and Law 41 of 2004 states that individuals or entities that set up operations in the APP will be allowed to carry out all types of activities as long as these are not expressly prohibited by law.

Tax System

As established in Section 58 of Law 41 of 2004, the APP offers broad tax benefits with regard to any activities, businesses, services, operations or transactions performed within the area, such as:

- An exemption for import duties and taxes on any type or class of merchandise, products, equipment, services and other goods in general, that are introduced into the Panama-Pacifico Area;
- An exemption for the ITBMS (local VAT) in respect of all types of merchandise, products, equipment, and other goods in general Services rendered, by entities registered under the APP are exempted from ITBMS as well.
- An exemption from the stamp tax;
- An exemption from the notice of operation for companies registered for the APP before December 31, 2016.²

¹ According to Section 3, paragraph 8, of Law 41 of 2004, Developer of the Panama-Pacifico Area is defined as “individual or entity, national or foreigner, of recognized solvency and experience, which has entered into a Developer Agreement, through which it assumes obligations of development, investment, guidance, promotion and administration of a part or of the entire Panama-Pacifico Area, in order to obtain the best use of resources and the promotion of it [...]”.

² Companies registered for the APP as of January 1, 2017 are subject to the annual Operation Notice tax at the reduced rate of 0.5% on capital (minimum US\$100.00 - maximum

- An exemption from property tax, as well as the real estate transfer tax, until December 31, 2029;
- An exemption from any export or re-export taxes and duties on any type or class of merchandise, products, equipment, goods or services.
- An exemption on withholding tax on remittances to foreign creditors regarding interest, commissions, royalties and other financial charges generated by financing or refinancing.

Notwithstanding the above, there are several “incentivized” activities that are exempted from the payment of the following additional taxes, which are specified under Section 60 of Law 41 of 2004. These exemptions will be extended to the external and internal operations of the individuals and entities duly established under the APP system. The additional benefits are as follows:

- An exemption on income tax in respect of the net taxable income earned from every incentivized activities by the law, except Shared Services activities. These type of activities are taxed at a five percent (5%) tax rate. An exemption on the dividend tax and complementary tax.
- An exemption on withholding tax on remittances regarding the payment of commissions, royalties, technical assistance services, or any other service.
- An exemption on import taxes and duties, as well as the ITBMS (local VAT), for companies that provide regulated services.

The incentivized activities that can be carried out within the APP and that qualify for the above tax benefits are as follows:

- Shared Services Activities;
- The direct and indirect transfer of shares, stock and securities of entities registered under the APP system;
- The transfer of goods and merchandise, as well as services provided to vessels crossing the Panama Canal and headed for foreign ports, or to vessels sailing between any Panamanian port and a foreign port, unless the transfer is made by the manufacturer or a member of the manufacturer’s economic group;
- The transfer of goods and merchandise, as well as the provision of services to aircraft that use Panamanian airports, with destinations to foreign airports, unless the transfer is made by the manufacturer or a member of the manufacturer’s economic group;
- The provision of services related to aviation and airports, including transportation, handling and storage of air cargo in general, and the repair of aircraft or aircraft components, as well the manufacturing of such products;
- The manufacturing of high-tech products, components or spare parts;
- Call center services for commercial use;
- The receipt, processing, storage and broadcasting of digital data and information. The up linking of radio, television, audio, video and/or data signals, and also research and development in the area of digital resources and applications to use in Intranet networks or the Internet;
- The importing, exporting and re-exporting of merchandise and other goods, multimodal and logistic services,

APP has a special customs system that allows companies located in this area to introduce all

US\$50,000.00), regardless of the activities carried on (i.e. the above applies either to incentivized or non-incentivized activities).

types of merchandise and goods into the APP, without limitations, and that exempts these companies from paying taxes, import duties and other tax contributions, except for those set out in Law 41 of 2004.

Merchandise can be sold to other companies within the APP. All types of merchandise and equipment will be allowed to enter the APP without prior consent from any authority, except for imports that may be subject to restrictions or that are prohibited altogether.

If products are imported into the Panamanian fiscal territory (Panamanian territory outside the APP), they will be subject to payment of all corresponding taxes and applicable tariff regulations. Merchandise, products or equipment that enter the APP from the Panamanian fiscal territory will be treated as an export.

The APP has special labor regulations and, although it is based on the Panamanian Labor Code, the APP is more flexible, particularly in the following areas:

- Unlike the rest of the territory, labor contracts must be in written form. Verbal agreements are not allowed.
- The labor system is designed to allow 24 hours of operation, at competitive rates.
- Overtime is subject to a 25% premium on hourly wages.
- Employees working on their days off receive a 50% premium.
- Employers and employees are free to agree on weekly days off; the APP labor system does not consider Sundays as mandatory days off.
- Companies in the APP can remain open on Sundays and national holidays.
- Agreements between employers and employees, regarding vacations, should be provided to the representatives of the Ministry of Labor in the APP.
- Employees may be required to work in different positions, as long as their salaries are not reduced and their role remains significant.
- Decreases in sales volumes, service demand, cancellation of purchase orders or services requested are considered valid reasons to terminate a labor contract, as long as the employer requests authorization to do so.
- Employers may hire foreign personnel as long as they do not exceed 10% of the total workforce, or 15% in the case of specialized workers.
- The Ministry of Labor may grant labor permits to foreigners representing more than 15% of the workforce, if they are hired specifically to train Panamanian personnel. Such employees may receive a visa for a period up to three years.
- The representatives of the Ministry of Labor in the APP may inspect companies in order to verify compliance with the applicable labor regulations. Companies that breach said regulations will be subject to fines up to US\$100,000.00 and, should they become repeat offenders, the fine may be raised up to US\$250,000.00.

The APP has special immigration regulations. Foreign workers must apply for an APP Employee Visa. Foreign employees who are awarded said visa will have the right to reside in the Republic of Panama or in the APP, and to work exclusively for companies operating under the APP system. APP Employee Visas may be issued under the following terms:

- Employees included within the ordinary 10% of foreign employees, valid for up to five (5) years;
- Foreigners hired by companies under the APP system, or by the Developer or the Operator of the APP, as specialized technical or administrative personnel, which do not represent more than 15% of ordinary (non-foreign) employees, valid for up to three (3)

years, which can be extended up to five (5) years, as long as the individual continues to work for such company;

- Foreigners hired by companies operating under the APP system, or by the Developer or the Operator of the APP, as specialized technical or administrative personnel, representing more than 15% of the ordinary employees, valid for up to three (3) years;
- Foreigners hired under the category of “trustworthy” employees, in charge of running offices and directing transactions with effects that take place outside of the country, will be issued a visa according to the applicable domestic legislation;
- Foreigners who work for companies with fewer than 10 employees will be issued a visa according to the applicable domestic legislation;
- Foreigners who invest a sum of at least US\$250,000.00 in companies in the APP, or in Developers or Operators within the APP, will have the right to request an APP Investor Resident Visa, which allows the foreigner to live in Panama for up to five (5) years, to leave and enter the country freely (without limitations) and to have a Panamanian Identity Card, as a legal resident;

The above-mentioned visas will be extended to the applicant’s spouse and children. These children can be either underage and of legal age, as long as they depend economically on the applicant, have not yet reached the age of twenty-five (25), and are currently single without children. Visas will also be available to the applicant’s parents, as long as they are older than sixty-two (62) years of age.

In the event that a person with an APP Employee Visa ceases to work for the company that hired him or her, the visa and the work permit will be immediately revoked.

The recipients of all the above-mentioned visas, except those who have an ordinary 10% Foreign Employee Visa, will be entitled to import, exempt from all taxes and duties, all types of domestic and personal articles up to US\$100,000. They will be required to maintain a registry of such items.

Recipients of the above-mentioned visas will also be required to pay income tax as well as make Social Security contributions. In addition, they are required to report their current domicile and/or any changes thereto to the immigration and labor authorities, and to comply with any other obligations established by APP legislation or by any other regulations that may be issued by the government. The companies in the APP must make sure that these obligations are met by their foreign employees.

Legal Stability

Any company operating within the APP will automatically obtain legal stability for a period of ten (10) years, from the time of registration for the APP, securing all rights and benefits granted to such company, in accordance with Law 54 of 1998, which establishes the *Legal Stability of Investment System*.

The Legal Stability system will apply to:

- New provisions that may change the rights already granted to the registered company.
- The national tax system (indirect taxes are excluded from legal stability).
- The municipal tax system (stability for the first five (5) years). Once concluded, another five (5) year period of stability will be granted in accordance with the municipal tax system in effect at the time.
- The customs system.
- The labor system.

Notwithstanding the above, if a new provision, regulation or law improves any right or benefit granted to an APP company under the Legal Stability system, the improved right or benefit is applicable.

Furthermore, APP Companies will not be subject to the ordinary process for obtaining Legal Stability, as they will be subject to an expedited process.



Headquarters of Multinational Enterprises (HME) or SEM

Chapter 12



Chapter 12

12

Headquarters of Multinational Enterprises (HME) or SEM

Legal System for HMEs or SEMs

Law 41 adopted on August 24, 2007 created a special system for the establishment and operation of Headquarters of Multinational Enterprises, or SEMs as per the acronym in Spanish. The primary objective of the law is to promote investments, employment and technology transfers, as well as make Panama more competitive in the global economy.

Law 41 aims to attract multinational corporations to set up offices in Panama for the purpose of providing intra-group services to head offices, affiliates, subsidiaries, or associated companies located abroad. A SEM Commission has been created to authorize permanent licenses, which are granted for an indeterminate period of time, provided that the holder of the license does not commit any of the infractions set out in the SEM regulation.

Definitions

- To qualify as a SEM, services must be provided from the Panama Headquarters to the head office/parent company abroad, its subsidiaries, affiliates or associated companies;
- Law 41 defines multinational enterprise (ME) as a legal person whose head office/parent company is in one country and commercial operations are taking place in different countries or different regions of such countries, and which decides to establish a branch, affiliate, subsidiary or associated company in Panama, for the purpose of doing business as part of commercial transactions within the region.

Types of Enterprise

- The SEM may be set up, either as a foreign company registered in Panama or a Panamanian company owned by the multinational enterprise, its subsidiaries or affiliates;
- Law firms or companies rendering services directly to clients or enterprises that are not interrelated cannot become a ME or subject to the SEM regime.

SEM License

One of the main conditions for a SEM license is that the total assets of the corporate group are greater than or equal to US\$200 million, or have at least Seven Subsidiaries In order to certify this, the following documents (among others) should be provided to the SEM Commission: 1) consolidated financial statements of the corporate group and 2) the bank's reference letter. Additional information such as the commercial activities of the corporate group, an estimate of the initial investment, job placement projections, general information about the SEM and its headquarters would be required.

Furthermore, it is also important that the applicant company includes within its Articles of Incorporation (in the company's purpose section) a brief description of its main objectives and its interest to establish itself as Multinational Headquarters in Panama.

Services

The SEM is expected to provide the following services (or a combination thereof) described below:

- Technical Assistance, finance or administrative, or other support services, included, but not limited to financial management services, risk analysis, credit analysis, due diligence, compliance, document archiving.
- Direction and/or management for geographical operations (in a specific area or globally) of a company within the group of companies: strategic planning, business development, management of personnel training, management of operations and/or logistics;
- Logistics and/or storage of components or parts of manufacturing products;
- Technical assistance not only for the companies of the EG but also for the clients for products and services of the EG;
- Financial management, including treasury to EG;
- Accounting of the EG;
- Preparing blueprints that form part of the design and/or construction that constitute the ordinary course typical of the business activity of the head office company or any of its subsidiaries;
- Processing electronic data of any activity including consolidations for the EG operations and network operations;
- Advice, coordination and follow-up for EG goods and services, marketing and advertising;
- Support for operations and research, as well as EG goods and services development;
- Other analogous services previously approved by the Cabinet Counsel according to Law 41.

Tax System

The SEM license is granted along with the following tax exemptions:

- Tax on the transfer of tangible goods and services provided to persons located abroad who do not generate taxable income in Panama; however, acquisitions of goods and services in Panama are to be taxed, as are imports. This exemption is based on service exports.
- Reduced five percent (5%) Income tax associated with services provided in Panama to entities abroad that do not generate taxable income within Panama.
- Notwithstanding the corporate income tax exemption referred to above, a withholding tax is to be applied over one-half of revenues paid by a local company to the SEM from the performance of services which have impacts on the generation or maintenance of the Panamanian-source income of the local company when such revenues are considered as a deductible expense. The effective tax rate is 5%.
- At the end of the fiscal year, the SEM must file an income tax return and report its tax-exempt income along with the income tax paid as withholding tax.
- No tax credit is allowed for losses resulting from operating costs and expenses.

Migratory system and other special considerations

- Personnel of the SEM shall be granted a visa for Permanent Personnel of Headquarters of Multinational Enterprises to live and work in Panama, for up to five years, which can be extended.

- Temporary personnel shall be granted a three-month visa to work at a SEM providing technical training or services to the SEM.
- Foreign employees with a SEM Visa would not qualify for either the 10% or 15% rate; therefore, the limitations stated in Section 17 of the Labor Code (general rule) would not be applicable.
- Housing and transportation expenses as well as any other compensation in kind will be exempt from local income tax, provided such funds come from abroad.
- Moreover, holders of a SEM Visa will be exempt from taxes on the importing and introduction of their household items into the Panamanian territory. The above exemption is applicable only the first time such personnel enters within the Republic of Panama.
- After five (5) years of holding a SEM Visa, the individual, can opt to get a Permanent Residency in the Republic of Panama, but will be subject to Income Tax, and Social Security Taxes.

SEM Annual Report

Companies registered under the SEM system must submit, to the Technical Secretariat of the Commission of Licensing of the Multinational Company Headquarters, an annual report containing the statistics relating to operations within the national territory. This Secretariat will determine the information that the report must include and this information will be included in a form that should be completed by all SEM companies.

Furthermore, the SEM License is granted indefinitely, as long as the holder of the License does not commit any of the infractions established in the SEM regulation. The competent authorities will be able to impose fines and penalties, which could include cancellation of the License.

Other Considerations

A tax agreement may be negotiated between the SEM and tax authorities in order to consolidate the enterprise profits and to pay income tax on revenues arising in other countries.



Working Conditions and Visas

Chapter 13



Visas

Foreign nationals planning to work for a local company will require a work permit from the Ministry of Labor and Employment Development. Under Panamanian immigration law, there are different kinds of visas that authorize an alien to either visit or reside in Panama, as long as the immigrant meets the requirements established in Law Decree 3 of 2008 (and subsequent amendments and regulations).

Law Decree 3, which supersedes Law Decree No. 16 of 1960, took effect on August 27, 2008 and establishes four categories of foreigners:

21. Non-residents;
22. Temporary residents;
23. Permanent residents; and
24. Foreigners under protection of the Republic of Panama.

The category of “non-residents” includes the following categories:

- Tourists - when visiting Panama, foreigners are allowed a stay of ninety days;
- Passengers and crew in transit;
- Marines;
- Other aliens such as crews on sailing ships and yachts, short-stay visitors, domestic workers, performers or show workers, visiting relatives of these non-residents and employees of the aviation companies located in Panama.

Additionally, temporary residents may enter the country for employment purposes, special political reasons and other matters (e.g., education, cultural, religious, humanitarian and family reasons). This category of foreigners and their dependents are allowed to reside with a one-year permit renewable for up to six years.

Moreover, permanent residents are those foreigners that enter the country for economic and investment reasons, special political reasons, demographic matters, international agreements and other subcategories of aliens whose main purpose is relocating to Panama on a permanent basis. Initially, a renewable two-year permit is granted.

Where special political matters are concerned, for temporary residents and permanent residents, the **immigration regulation** recognizes visas for the following:

- Enterprises hired by the Panama Canal Authority (ACP) ruled by Law 45 of August 31, 1999;
- The Panama-Pacific Special Economic Area (former military base of Howard) ruled by Law 41 of July 20, 2004;
- Export processing zones governed by Law No. 25 of November 30, 1992;

- Call centers governed by Law No. 54 of October 25, 2001;
- The film and audiovisual industry ruled by Law No. 36 of July 19, 2007;
- Headquarters of multinational enterprises (HME), governed by Law No. 41 of August 24, 2007;
- The Colon Free Zone, governed by Law No. 8 of April, 2016;
- The City of Knowledge, governed by Law Decree No. 6 of February, 1998.

Within the special policy category, the migratory regulation recognizes the following visas:

- Treaty of Amity, Commerce and Navigation between the Republic of Panama and the Republic of Italy, governed by Law No. 15 of February 1, 1966 and Resolution 4803 of March 30, 2012;
- National Foreigners of Specific Countries who maintain Friendly, Professional, Economic and Investment Relations with the Republic of Panama, governed by Executive Decree No. 416 of June 13, 2012;
- Professional Foreigners, governed by Executive Decree No. 804 of October 10, 2012;
- Diplomatic Qualification and Members of International Organizations of countries that maintain friendly diplomatic relations with the Republic of Panama, who have stopped providing their services in their respective positions.

Tourist Visa Requirements

- Most foreigners initially enter Panama with a tourist visa or a tourist card, which allows them to stay in the country for a 90-day period.
- Such period may be extended up to 60 days, at the discretion of the competent authority, when changing the category.
- Almost all Latin Americans and U.S. citizens are allowed to enter Panama with a tourist card.
- At present, tourist cards can be obtained from almost all airlines flying into Panama, while the tourist visas are issued by the Panamanian Consuls.
- All foreigners who stay in Panama for more than 90 days must be registered at the Immigration Office and need an exit permit to leave the country.
- All foreigners authorized to reside temporarily in Panama will need a re-entry permit to travel abroad and return to the country. The permit may be valid for one or multiple trips.

Resident and Work Visas

The most common visas for business people are immigrant visas, temporary visas and the temporary visa for special visitors.

- An immigrant visa is recommended for foreigners who intend to reside permanently in Panama while working or doing business.

Residence permits for work reasons apply to:

- Foreign personnel hired by private companies representing less than 10% of ordinary staff.
- Foreign personnel hired as experts or technicians and representing less than 15% of ordinary staff.
- Staff recruited as press, radio or international television correspondents and remunerated abroad.

- Foreign nationals contracted by companies under the Marrakesh Agreement.
- Sports professionals.
- Employees of aviation companies based in the Republic of Panama.
- The investor's visa, an immigrant visa that is available to foreigners who wish to invest in commercial, financial and industrial activities.
- A temporary visitor's visa applies to technicians, specialists, students, and other aliens who will remain in Panama temporarily for up to six years.
- A temporary visa for special visitors, also known as the "executive visa", is suitable for personnel of international companies and banks who have a monthly salary of at least **five thousand US dollars (US\$5,000)** which comes from sources located outside of the Panamanian territory or non-Panamanian-source income.
- Since 2005, the temporary visa for special visitors is provided to foreigners working in Panama for an offshore business and provides an income tax exemption.
- Starting in 2007, other types of visas became available to business people: the visa for permanent personnel working in headquarters of multinational enterprises (up to five years) and a visa for temporary personnel of such headquarters (up to three months). The visa is also available for dependents.

Temporary Special Visitor's Visa

The temporary special visitor's visa is based on Cabinet Decree 363 of 1970 and Migration Services, which grant this type of visa to expatriate executives with a minimum salary of US\$5,000 who work in Panama for an offshore business.

The visa has been available for all foreign executives who entered Panama to work for international companies (or for Panamanian subsidiaries of said companies that carry out business operations outside of Panama).

This special visa is granted for one year and can be extended for up to six years. The visa is available even after August 27, 2008 (the date when new immigration requirements commenced per Law Decree 3 of 2008).

Visas for Pensioners and Annuitants

According to Law 9 of 1987 and its corresponding amendments, the following visas are issued based on pension or annuity income:

- The tourist pensioner visa;
- The retired annuitant visa.

The main features of these types of visas are as follows:

- Having a retirement pension or a private retirement fund;
- The tourist visa is not compatible with an immigrant visa;
- The tourist pensioner visa is for persons receiving a pension of at least five hundred US dollars (US\$500) per month, plus one hundred US dollars (US\$100) per each dependent;
- The retired annuitant visa is for those receiving a monthly income of at least two thousand US dollars (US\$2,000), coming exclusively from interest earned during a five-year period from an account held at the National Bank of Panama or the Savings Bank of Panama.
- In the case of a tourist pensioner visa, the pensioned status should be proven with legal documentation. In addition, the competent authorities shall confirm the pension status of foreigners with their companies (including private pensions);

- In the case of a retired annuitant, the visa gives the foreign retired annuitant the right to obtain a special Panamanian passport;
- All aliens applying for any Panamanian visa are required to submit the following documents: police records for themselves, their spouse, and all dependents over age 18, medical certificates expiring within less than three months, marriage and birth certificates for the children, four photos, a declaration of personal background, a valid passport expiring within not less than six months and a legal copy of their passport.

Investment is widely welcomed and expressly authorized. Therefore, business operations under said status are allowed; however, employment is prohibited without authorization.

The following exemptions are granted concerning employment and tax payments:

- Working exemptions: when rendering specialized services to the government which are not provided by Panamanians; when doing business, the person invests significant sums in an enterprise and is previously authorized by the Ministry of Labor; when he/she is a board member of owned companies (self-employed);
- Tax benefits of having a visa to reside in Panama are: import duties exemption for domestic goods and vehicles, no fees relating to the acquisition of the visa, and tax-exempt income upon pension or annuity due to foreign source income.

Holders of Certain Tourist Visas

Citizens of any country who hold visas from either the United States, Canada, Australia, the United Kingdom or any country of the European Union have no need to request a Panamanian visa to enter into Panama as a tourist, as long as the holder of such a visa has already entered the country that granted the visa. Instead of requesting the visa, the applicant will purchase a tourist card at a cost of US\$30.

Discounts on the Basis of Age

According to Law 6 of 1987 (as amended), any individual, citizen or foreigner, who is fifty-seven (57) years of age if female, or sixty two years (62) of age if male, will be offered discounts by service providers and retailers. Some of the discounts are:

- A 50 percent discount on admission to recreational or entertainment activities such as theaters, movies, sports and several public shows;
- A 25 percent discount on air fares;
- A 50 percent discount when staying in hotels from Monday through Thursday and 30 percent from Saturday through Sunday;
- A 25 percent discount on individual food consumption invoices (of first and second-class restaurants);
- A 15 percent discount on fast food establishments;
- A 25 percent discount on electricity services, residential telephone and water supply repairs (certain restrictions may apply);
- A 20 percent discount on the value of drugs obtained;
- A 15 percent discount on private hospital services;
- A 20 percent discount on professional and technical services;
- A 50 percent discount on commission expenses and closing transactions for personal or commercial loans;
- A 15 percent discount on the maximum interest rate allowed by law, to be charged by banks or credit institutions;

- A 20 percent discount on coffins and urns for retirees, pensioners or senior citizens;
- Exemption starting one percent over the rate applied to all local personal or business loans above five thousand US dollars (US\$5,000);
- Total exemption from payments to the Public Registry when registering a board of directors, certifications, and new legal entities of non-profit organizations for retirees, pensioners or senior citizens;
- Real state tax freeze on the property in the house that is in the person's name and is the only house.



Labor Legislation

Chapter 14



14 Labor Legislation

Labor contracts

The Labor Code states that labor contracts must be in writing and the employer, employee and labor authorities must each have a copy; otherwise, any facts or circumstances alleged by an employee will be presumed to be true, unless the employer can prove otherwise beyond a reasonable doubt.

The most important features are the following:

- The contract may be for an indefinite or a definite period of time, or for a specific project.
- An employee can be hired for a probationary period of three months, provided that the type of service requires special skills and that this has been expressly written in the contract.
- The maximum term for a definite-period contract is one year.
- A definite period contract becomes indefinite, if the employee: (1) continues working after the definite period expires; (2) continues working after the specific project for which the employee was hired is completed; or, (3) when successive contracts for a definite period or contracts for a specific project are negotiated.
- Employees cannot waive their rights when entering a contract, nor can these rights be diminished.
- Any provision, act, or declaration of the employee that provides or implies lessening or relinquishing any right is considered null and void, even if stated in the labor contract or in any other agreement.
- The division of the enterprise, into diversified or separate companies, does not affect employees' rights. The concept of an economic conglomerate prevails, so that employees can furnish claims against the employer.
- Local legal advice should be sought before making any decision concerning labor law.

Salaries

Work Permits

Foreigners wishing to work in Panama must obtain authorization, in the form of a work permit, from the Ministry of Labor and Employment Development.

- Work permits are valid for one year and may be renewed.
- Firms employing foreign personnel must maintain a certain proportion between local and foreign workers.
- Local personnel are defined as Panamanians, foreigners married to Panamanians, and foreign employees with at least 10 years of legal residency in Panama.
- Employers are allowed to hire up to 10 percent of foreign employees from the total number of administrative workers, and up to 15 percent in the case of specialized or technical personnel.
- Exceptions can be made under special conditions.
- Corporations established in Panama exclusively to supervise operations or transactions carried out abroad are exempt from these ratio requirements.

Salaries and Minimum Wages

- Salaries can be fixed by unit of time (month, fortnight, week, day or hour), task, or by a specific job.
- Salaries include any money, gratuities, bonuses, premiums, commissions, profit sharing, and any other income or benefit employees receive as payment for their work such as representation expenses and in-kind salary.
- Employees must be paid at least twice a month.
- The government established minimum wage rates based on the hourly wage, economic activity, company size and region.

Work Day

According to the Labor Code, four different work shifts are established. These are as follows:

- Day shift, consisting of a maximum of eight hours; from six hours to eighteen hours (6:00 a.m. to 6:00 p.m.) with a maximum of 48 hours in a week;
- Night shift, consisting of a maximum of seven hours; from eighteen hours to six hours (6:00 p.m. to 6:00 a.m.) with a maximum of 42 hours a week;
- Mixed shift, consisting of seven and a half (7-1/2) hours including both the day shift and the night shift, with a maximum of 45 hours a week. A mixed shift with more than three night shift hours is considered to be a night shift;
- Rotational shift, for companies required to employ personnel during different hours according to the companies' activities and needs.

For the night, mixed, and rotational shifts, employees receive the same payment as for the day shift, even though their working hours are shorter. A working day consists of the total time the employee cannot use freely, when at the service of the employer.

Overtime

Hours worked in excess of the maximum hours defined above must be paid as overtime.

Overtime rates are as follows:

- Twenty-five (25) percent premium for hours worked during the day shift;
- Fifty (50) percent premium for hours worked during the night shift, for hours worked in excess of a mixed shift initiated in the day period, or for work performed on any days off (i.e., Sunday);
- Seventy-five (75) percent premium for hours worked in excess of the night shift or a mixed shift initiated in the night period;
- A hundred and fifty (150) percent premium for hours worked on a holiday or national day of mourning and an additional day off must be provided and paid. Hours worked in excess of the regular shift on a holiday must be paid at the same rates as above, in addition to the 150 percent premium;
- An employee cannot be required to work overtime except under special circumstances (e.g., export industries) or by a written contract;
- Three hours per day and up to nine hours per week are the maximum legal overtime hours;
- For overtime in excess of this limit, the employee is entitled to receive a 75 percent premium.

Export industries and small businesses have special dispensations regarding overtime. These companies pay a single 25 percent premium on regular salary for overtime, and 50 percent for work performed on holidays or days of mourning.

National Holidays and Days of Mourning

Twelve days are legally considered national holidays or days of mourning.

National Holidays	
Month	Day
January	1 (New Year's Day) 9 (Martyrs Day)
Mardi Grass	One day in February or March
Good Friday	One day in March or April
May	1 (Labor Day)
November	3 (Independence Day) 5 (Independence Day, Colon only) 10 (Shout for Independence Day) 28 (Independence Day from Spain)
December	8 (Mother's Day) 25 (Christmas Eve)
Every five years	July 1- 2014 (Presidential inauguration)

Note. Consider August 15th (Foundation of Panama City, Panama City only), November 4th (Flag Day), and December 24th (Christmas Eve) as feasible public holidays but not labor-free holidays.

Vacations

- Employees are normally entitled to one month (30 days) of annual vacation every year.
- Annual vacation is accrued at the rate of one day for every eleven (11) days of work.
- The employee may not waive annual vacation in exchange for payment.
- However, it can be accumulated for up to two years by mutual agreement, but there is a minimum rest period of 15 days during the first period.
- The thirty-day period can be divided into no more than two equal parts.
- Employees working for companies established in export processing zones might enjoy annual vacation in advance, even if not earned, provided that the operating cycle demands it.

Leaves and Benefits

Sick leave, maternity leave, the thirteen month bonus and worker's compensation are outlined below.

Sick Leave

- Paid sick leave or disability leave must be provided for each employee when required, up to one and a half days per month, or 18 days per year.
- Sick leave can be accumulated for up to two years, and may be enjoyed entirely or in part during the third year of service.
- If additional sick leave is required, employees covered by the social security agency may receive an additional period of leave.

Maternity Leave

- Female employees are entitled to special benefits under Panama's Labor Code. Once pregnant, they can be dismissed only for cause with judicial assent. This same privilege is extended for one year following childbirth.
- Maternity leave must be granted for at least 14 weeks, six weeks before delivery, and eight weeks after childbirth. While on maternity leave, no communications or actions, sanctions or measures provided in the Labor Code can be taken by the employer.
- The social security agency provides a subsidy to cover female employees for this period. The employer must pay the difference between this subsidy and the employee's salary.

Thirteenth Month Bonus

- All employers must pay their employees a special bonus called the thirteenth month bonus. This bonus is estimated as one day of salary for every twelve (12) days of work.
- The thirteenth month bonus is paid in three equal installments: on April 15, August 15, and December 15 of every year.
- Sums paid for the thirteenth month bonus are subject to social security contributions for the employer and are not subject to any other type of withholdings except for the employee's personal income taxes and social security contributions.
- The education insurance tax is therefore not withheld.

Workers' Compensation

- All employers must enroll their employees in the social security system, which includes workers' compensation.
- This is an additional premium paid depending upon the risks involved in the activities performed.

Termination of Employment

Either an employee or an employer can terminate a working relationship. There are six ways to end an employee-employer relationship:

- By mutual consent.
- Upon expiration of the agreed term or upon conclusion of the work.
- Upon the death of the employee, or dissolution of the employer.
- With a justifiable cause (as defined in the Labor Code).
- Upon resignation of the employee, and
- Upon a unilateral decision of the employer, subject to the formalities and limitations established in the Labor Code.

Relevant issues:

- Exceptions are provided for temporary workers, domestic workers, apprentice workers with less than two years of service, and agents with less than five years of service.
- In this case, the employer must either provide a thirty-day notice or one month of severance (equivalent to one month's salary).
- Employees who wish to resign must give at least a 15-day notice.
- Technical workers must give at least a two-month notice.
- If the termination is by mutual consent, it must be in writing and should not involve the waiving of any of the employee's rights.
- This document must be submitted to the General Director of Labor, at the Ministry of Labor and Employment Development, in order to be valid.

- Non-compliance with this requirement can result in reinstatement within the next thirty calendar days, with the payment of all accumulated unpaid salaries.
- Resignation by the employee must be ratified before the Ministry of Labor and Employment Development, which has the authority not to ratify said resignation if it implies waiving any of the employee's rights.
- The Ministry of Labor and Employment Development must also authorize the termination of collective labor relationships.

Seniority Premium

- When a working relationship ends, the following items are relevant: seniority premium, justified causes and premiums for unjustified cause.
- Employees, who leave an employer for any cause, are entitled to receive a lump sum payment equivalent to one week of salary for each year employed.

Justified Causes

The Labor Code allows an employer to dismiss an employee for disciplinary reasons, no-fault reasons, or economic reasons. In the latter case, the employer must obtain previous approval from the labor authorities and pay an indemnity to the dismissed worker.

Justifiable causes for dismissal of an employee for disciplinary reasons include:

- Deceitful representations regarding the employee's special skills;
- Disobedience;
- Engaging in acts of violence;
- Absenteeism;
- Use of alcohol or drugs on the job;
- Theft;
- Damage inflicted upon the company's physical or intellectual assets;
- Sexual harassment; and
- Low productivity according to standard evaluation systems.

Some no-fault reasons include:

- The firm's closure resulting from an act of God;
- Imprisonment of the worker;
- Retirement;
- Permanent disability or loss of capacity to exercise a profession.

Economic reasons include:

- Bankruptcy;
- Insolvency;
- Reduction in sales causing a reduction in the company's activities;
- Cancellation of requests or orders, decrease in production activities or in sales.

Premiums for Unjustified Causes

- As previously mentioned, any employer who dismisses an employee without legal cause is liable for payment of a compensation premium.
- This lump sum is based on the indemnity tables.
- For employees hired after August 14, 1995, it will consist of three point four (3.4) weeks for each year employed, for the first ten years.

- For the subsequent years, it will be set at one week for each year of employment.
- Indemnities are subject to income tax based on a special procedure, but not to social security or education tax.

Labor Unions

Panamanian labor laws recognize the right of employees to form or join unions. Workers also have the right to strike in order to protect or improve their working conditions.

Collective agreement conflicts may be submitted totally or partially to arbitration. New companies established after October 1990 are not forced to sign collective bargaining contracts during the first three years of operation.

Severance Fund

Law 44 of 1995 states that employers must create a severance fund for the payment of seniority premiums and the indemnifications resulting from unjustified dismissals or justified resignations concerning contracts for an indefinite period.

- The severance fund must be created through a trust.
- Contributions to the severance fund will be made totaling one point ninety-two (1.92) percent of the payroll as a seniority premium and covering five (5) percent of the monthly quota (meaning 0.327 percent) to which the employees would have a right in the event of an unjustified dismissal or justified and filed resignation.
- Interest and other payments will be made on behalf of the employer.
- The employer will be able to make withdrawals from the fund if there is a surplus with regards to current labor liabilities.
- Contributions to the severance fund are deductible.
- Employees can make individual contributions to the severance fund, through an individual account.

The following will be charged to the severance fund:

- Seniority premiums;
- Termination of employment due to unjustified dismissal, after a statement from the corresponding authority has been made;
- Justified resignation of the employee declared by a competent authority;
- Termination of employment by mutual agreement that includes partial or total delivery of the indemnification for unjustified dismissal.

Minimum Wage

Executive Decree No. 75 from December 26, 2017, which sets the new Minimum Wage Rates throughout the National Territory, was published in Official Gazette No. 28433-A (government news bulletin) dated December 27, 2017.

The national territory is segregated by regions – districts, as follows:

- Region 1: Panama, Colon, San Miguelito, David, Santiago, Chitre, Aguadulce, Penonome, Bocas del Toro, La Chorrera, Arraiján, Capira, Chame, Anton, Nata, Las Tablas, Bugaba, Boquete, Taboga, San Carlos, Chepo, Guarare, Los Santos, Pedasi, Dolega, San Felix, Barú, Boquerón, Portobelo, Donoso, Santa Isabel, Santa Maria, Parita, Pese, Atalaya, Changuinola, Chiriquí Grande.
- Region 2: Remainder of the country's districts.

Entities employing ten (10) or fewer staff are considered a small business so as to differentiate them from large enterprises. However, entities that employ 10 staff and fall under any of the following categories are indeed considered small businesses (exceptions): agriculture, livestock, service or retail enterprises require 10 employees; otherwise, manufacturing companies require 15 employees or less and agro-industrial companies require 20 employees or less to be considered small businesses.

The chart below provides some examples for minimum hourly rates (depending on the region, area of economic activity and company size, existing throughout the country.

Economic Activity	Region 1	Region 2
Agriculture, cattle ranch, hunting, forestry		
Aqua-culture		
Small business	1.53	1.53
Large business	1.87	1.87
Fishing (domestic)		
Artisans	2.15	2.15
Industrial	2.36	2.36
Agro industries		
Small business (agriculture)	1.53	1.53
Large business (agriculture)	1.87	1.87
Small Business (processing)	2.20	1.85
Large business (processing)	2.72	2.24

Economic Activity	Region 1	Region 2
Mining		
Sand extraction activities	2.85	2.85
Mining	2.97	2.97
Manufacturing industries		
Small business	2.20	1.85
Large business (16 employees or more)	2.85	2.35
Distillation, rectification and mixing of alcoholic beverages; manufacturing of paints, varnishes and coating products	2.85	2.40
Manufacturing of cement and/or concrete	3.14	2.99
Sugarcane processing	2.85	2.85
Repair, maintenance of machinery and Refrigeration equipment	2.85	2.31
Electricity supply, gas, steam, air conditioning	3.14	3.14
Production of ice	2.72	2.24
Water supply, sewerage, waste management and sanitation activities	3.14	3.14
Sewerage	2.85	2.35
Collection, waste treatment and disposal	2.85	2.35
Processing and waste material recovery	2.72	2.24
Construction	3.14	2.95

Economic Activity	Region 1	Region 2
Wholesale trade and commission		
Products and sub-products derived from sugarcane	2.72	2.72
Fuel tanks	2.72	2.23

Economic Activity	Region 1	Region 2
Retail		
Small business	2.26	1.87
Large business (11 or more employees)	2.72	2.23
Fuel stations	2.72	2.23

Economic Activity	Region 1	Region 2
Free trade zones, Special regime zones	3.47	2.32
Colon Free Trade Zone	3.17	

Economic Activity	Region 1	Region 2
Hotels		
Small business	2.26	1.87
Large business (11 or more employees)	2.72	2.23
Franchise hotels and resorts; Hotels with over Boarding houses and residential accommodations	2.85	2.34

Economic Activity	Region 1	Region 2
Restaurants and bars		
Small business	2.20	1.85
Large business (11 or more employees)	2.85	2.34

Economic Activity	Region 1	Region 2
Transportation (average)	2.85	2.34
Cargo transport in special regime zone	3.14	2.32
Transportation by water or by air	2.85	2.32
Port workers	3.27	3.27
International airports	3.47	3.47
Bus drivers	3.14	3.14
School bus drivers	2.72	2.24
International flight cabin crew	4.45	4.45
Storage, deposits and post office/mail	2.72	2.23
Communications network	2.85	2.85
Editing activities	2.85	2.35
Production of television and radio programs	2.85	2.34
Production of movies, videos, sound, movie theaters and news agencies		
Telecommunications, radio and television broadcast	3.14	3.14
Camermen	3.14	3.14

Economic Activity	Region 1	Region 2
Financial and insurance activities	3.17	3.17
Pawnshops	2.77	2.77
Real estate activities	3.14	2.80
Malls (with over 50 stores)	3.14	3.14
Administration activities and support services (rental activities)	2.85	2.85
Rental of motor vehicles	3.14	3.14
Internet cafe activities	2.59	2.41
Employment agency activities	2.85	2.85
Travel agencies	2.85	2.24
Buildings and landscaping services	2.72	2.72
Landscape maintenance services	1.92	1.92
Administration offices, business support	2.72	2.72
Security and research activities	2.72	2.72

Economic Activity	Region 1	Region 2
Business support activities	2.68	2.68
Professional, scientific and technical service	2.72	2.72
Veterinary services	2.72	2.23
Law firms and audit firms (14 employees or less)	2.64	2.64
Lawyers	3.34	3.34
Television, radio and newspaper journalists	3.12	3.12
Air transport mechanics	4.45	4.45
Land transport mechanics	3.12	3.12
Water transport mechanics	3.47	3.47
Teaching (administrative staff)	2.85	2.32
Social services related to human health	2.85	2.32
Health clinics and hospitals	3.14	2.34
Health technicians	3.14	3.14
Art, entertainment and creativity	2.85	2.85
Gambling activities and casinos	3.34	3.34
Gyms	3.14	3.14
Other services	2.85	2.32
Non-profit organizations	2.72	2.23

Computer repair and maintenance	2.72	2.72
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Economic Activity	Region 1	Region 2
Repair and maintenance of domestic use items		
Small business	2.20	1.84
Large business (11 or more employees)	2.72	2.29
Residential buildings (over 10 stories) and tenants	3.14	3.14
Individual property associations		
Spas, esthetician clinics	3.14	3.14
Activities of extraterritorial organizations and bodies	2.85	2.85

For domestic service, the decree regulating the monthly minimum wage is as follows:

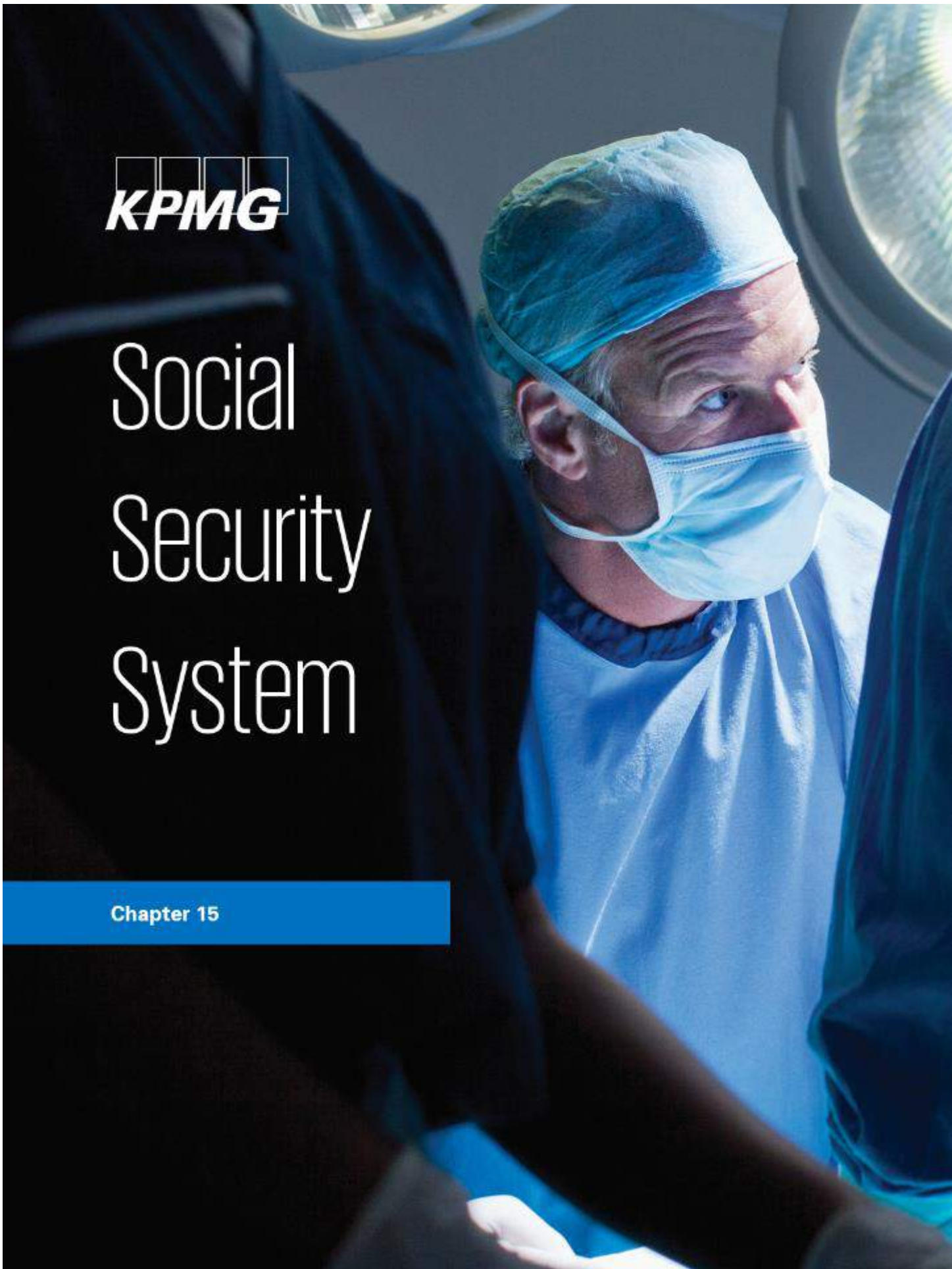
- US\$ 275.00: Panama, Colon, San Miguelito, David, Santiago, Chitre, Aguadulce, Penonome, Bocas del Toro, La Chorrera, Arraiján, Capiira, Chame, Antón, Nata, Las Tablas, Bugaba, Boquete, Taboga, San Carlos, Chepo, Guarare, Los Santos, Pedasi, Dolega, San Félix, Barú, Boquerón, Portobelo, Donoso, Santa Isabel, Santa Maria, Parita, Pese, Atalaya, Changuinola, Chiriquí Grande.
- US\$250.00: Remainder of the country's districts.

As a reminder, the regular working week is 48 hours (full-time) which could be lower depending on evening part-time hours worked or a combination of day and night shifts, as well as simply working fewer hours than the maximum amount.



Social Security System

Chapter 15



This chapter summarizes the social security system. It discusses both the employer and employee contributions and taxation matters (e.g., deductions and withholdings). Details regarding the old age retirement pension are also provided.

Social Security Levies

The social security system in Panama replaces many of the employee benefits normally provided by private insurance in other countries.

Highlights

- Management of the social security system is provided by the Social Security Administration Agency ("*Caja de Seguro Social*").
- It not only provides retirement benefits, but also health, dental, maternity, disability, and death benefits. Therefore, the cost of employee benefits may be reduced, although the coverage provided does not differ from private insurance coverage.
- For workers, there are two legal systems: mandatory enrollment and voluntary enrollment.
- All employees working for the government, individuals or enterprises operating in the national territory, including foreign nationals, are subject to the mandatory social security system.
- The social security system grants benefits to the insured and this person's dependents.

Mandatory Affiliation and Enrollment

- Every company organized to carry out activities in Panama must apply for an employer's registration number from the Social Security Administration, six days after starting operations and hiring workers. Employers that do not register their employees during such period will be subject to a fine of between \$100 and \$ 2,000.
- Employers must be registered with the Social Security Administration and employees must also be enrolled.
- Mandatory enrollment includes dependent workers (employed by others, working for another person or on behalf of another person) as well as independent workers (autonomous or self-employed workers) with a gross income over nine thousand six hundred US dollars (US\$9,600) a year. Such individuals must be less than 35 years of age.
- Nationality is not considered; what is relevant is that the service be performed within the Panamanian territory (including diplomatic and consular assignments).
- It is mandatory for all employers to deduct social security quotas, as well as income tax and social security contributions, from employee salaries, including the quotas and contributions as an employer.

Self-employed Workers

- There are two categories created by law: taxpayer self-employed workers and non-taxpayer self-employed workers. Both are only responsible for fees.
- In addition, the mandatory enrollment for a self-employed person who is less than 35 years of age is established by Law 51 of 2005. Beginning in January 2007, this mandatory system governing social security pensions for independent workers is based on 52 percent of a person's income, paid through the Directorate General of Revenue of the Ministry of Economy and Finances.
- Non-taxpayer self-employed workers. Persons, who earn less than nine thousand six hundred US dollars (\$9,600) in annual gross income can retain their voluntary affiliation status (e.g. informal, eventual, domestic workers).
- Salaries and fees received by a worker at the same time pay quotas for each category of income.

Social Security Payroll

In August 2012, the Social Security Administration implemented a technological platform called the Income and Economic Benefits System (SIPE as per its acronym in Spanish), which allows employers to carry out all the transactions related to income and economic benefits through the system.

The SIPE platform grants benefits to the employers, including the following:

- Declare labor activities such as affiliation, employee input and output notices.
- Completion and filing of the monthly payroll for the employee's declaration from the 1st to the 25th day of the following month.
- Notices such as maternity leaves, vacations and other leaves for sickness/disabilities.
- Salary reports duly signed with the digital signature upon receipt of the invoice.
- Accreditation of the quotas for individuals and employment histories.
- Faster processing for benefits requested, such as benefits for sickness, professional risks, the elderly, disabilities or death or other than the benefit entitlement.

Withholdings (or contributions)

- Part of the Social Security income to cover benefits is made up of mandatory payroll withholdings paid by employees and employers.
- Moreover, employers pay a rate between 0.42 percent and 7.00 percent of salaries to cover workers' compensation, depending on the activity.
- Employers must pay contributions every month. Delayed payments will result in penalties determined as follows:
 - Within the first 10 calendar days, a penalty equivalent to 2% of the amount owed.
 - Within the next 10 days of delay, a penalty equivalent to 5% of the amount owed.
 - Within the next days until 30 days of delay, a penalty equivalent to 10% of the amount owed.
 - More than 30 days of delay, a penalty equivalent to 15% of the amount owed.
- In addition to the above-mentioned penalty, interest at the rate of 1% monthly will be levied.
- Collection of premiums from employers is subject to a 20-year statute of limitations period.

Meaning of Salary for Labor Law Purposes

Salary is understood as all remuneration without exception, in cash or in kind, received by the employees as a retribution for their services, including the following:

1. Occasional and permanent commissions;
25. Paid vacations;
26. Occasional or permanent bonuses;
27. Director fees (per diem) exceeding 25 percent of the monthly salary;
28. Production premiums exceeding 50 percent of the monthly salary and representation expenses;
29. Additionally, in 2006, withholdings became applicable (gradually) over a portion of the representation expenses, as follows.

Social Security and Representation Expenses

With respect to representation expenses, effective July 1, 2008, the total social security contribution increased due to a change in the tax base – which changed from twenty-five percent (25%) to fifty-five percent (55%) in force through June 2010.

- Effective July 1, 2010, representation expenses are taxed at 100% by the Social Security Authority – according to Law 51 of December 27, 2005. Refer to chart below.
- Representation expenses are taxed at 55% for social security contributions as of July 1, 2008.

Representation Expenses	
Time period	Taxable income
From 07/01/2006	25%
From 07/01/2008	55%
From 07/01/2010	100%

Income Not Considered as Salary

The following sources of income are not considered salary, and therefore, are not subject to social security contributions:

- The three installments of the thirteenth month bonus;
- Severance notices;
- Termination indemnities;
- Profit-sharing that benefits 70 percent of an enterprise's employees as a minimum. Hence, no withholdings are made from profit-sharing benefits granted to employees, provided that these benefits include no less than 70 percent of the workers and do not exceed or replace the total annual salary;
- Dividends (as long as they do not replace salary);
- Gratuities or Christmas bonuses equivalent to less than one month of salary;
- Seniority premiums;
- Travel and food allowances;
- Production premiums not exceeding 50 percent of one month of salary.

Simulation Actions

The Social Security Administration may begin investigations in order to confirm compliance with the obligations in the following cases:

- Payment of a per-diem amount to employees who do not perform any executive or director-level position.
- Payment of allowances to employees who, due to the nature of their positions, do not have to work outside their working area or office.
- Payment of fixed production premiums to employees, where such premiums are related to an increase in employee productivity.
- To hire an employee to perform professional services when the employee is economically dependent on the employer or is legally subordinated to the employer.
- To hire an employee under a different employer than the one that effectively is receiving the services from the employee.
- Leasing contracts or the rental of equipment, agreed upon based on a percentage of commission, as long as the intention is to falsify the provision of services.
- The use of legal persons that do not have a proper operating structure, with the purpose to avoiding the payment of employee – employer quotas.
- When it is proven that an economic group is avoiding the solidary payment of the employer – employee quotas.
- When it is proven that, in the case where the employee or independent worker is obliged to pay quotas, an amount less than the one collected is reported as salary or fees.
- When another act simulates or covers up the payment of salaries or professional fees with the purpose of avoiding compliance with obligations.

Quotas and Payments

Subject to changes introduced by Law 51 of 2005, quotas increased in January 2006. Furthermore, it is understood that both cash income and in-kind income, for both dependent and self-employed workers, are subject to quotas.

- Higher percentages have been approved for regulating the social security system.
- Self-employed workers are required to make pension contributions when they are less than 35 years of age.
- Thus, the progressive schedule chart applies to both employees and employers.
- Quotas and percentages vary. The employee-employer quota continues to apply at a rate of 7.25 percent for employees through December 2007 and has been established at eight percent for three years since 2008. This changed to nine percent in 2011 and changed again to (9.75 percent in 2013).
- For employers, it continued at 10.75 percent of the salaries paid through December 2007, and changed to 11.50 percent for the next two years, effective in January 2008. It then increased to 12 percent in January 2011 (for two years) and changed to 12.25 percent on January 2013. Employers must pay an additional quota to contribute to the health and maternity program. This percentage is already included in the following chart.
- Self-employed workers pay quotas on 52 percent of their annual gross fees, as follows: 9.5 percent in 2007, 11 percent in 2008, 12.50 percent in 2012, and 13.50 percent in 2013.

For comprehensive social security quotas (either withholdings or contributions), the chart below indicates what employers, employees and self-employed workers are required to pay.

Social security quota percentages (rates)

Social Security Quotas			
Time periods	Employees	Employers	On 52% of self-employed revenues
2006	7.25%	11.00%	0.00%
2007	7.25%	11.25%	9.50%
2008	8.00%	12.25%	11.00%
2009	8.00%	12.00%	11.00%
2010	8.00%	11.75%	11.00%
2011	9.00%	12.00%	12.50%
2012	9.00%	12.00%	12.50%
From 2013	9.75%	12.25%	13.50%
XIII Month Bonus***	7.25%	10.75%	-

Thirteenth Month Bonus

As per the table, employers are responsible for 10.75 percent of the social security contribution for bonuses paid (on the 15th day in April, August and December). Additionally, employees are responsible to contribute 7.25 percent of bonuses paid into the social security system.

Disabled, Retired Persons and Subsidies

The quota to be paid from a pension fund by the Social Security Administration is 6.75 percent of the monthly pension - due to disability, advanced age, death or permanent disability. Temporary disability or maternity leave compensation were paid out as follows: 7.25 percent through December 2007; eight percent through December 2010 for three years, nine percent through December 2012 and changed to 9.75 percent beginning in January 2013. These contribution percentages and timeframes apply to employees as well.

Note. Law 51 of December 27, 2005 was the provision enacted to manage social security matters. This law had been subject to the second administrative regulation (in order to determine the scope of its measures and definitions, among other important issues) through a resolution effective from June 1, 2006.

Social Security Benefits

The benefits, except for the payment of subsidies, cover the spouse of the insured, children up to eighteen (18) years of age (age 25 if they are students), disabled children and parents (under certain conditions).

Medical and Dental Care and Hospitalization

- The Social Security Administration grants medical, surgical and dental care, prescription drugs, and hospitalization services to those insured as well as a subsidy in the case of temporary disability when an insured employee is unable to work.
- An insured employee is entitled to medical care which becomes effective when the employee starts working.
- Hospitalization services are available once an insured person has made at least two monthly payments within the first four months of employment.

- After involuntary termination of employment, a worker is entitled to medical care, for three additional months, or one year if the employee has already paid social security for 15 years.

Disability Subsidy

- Payments under the temporary disability subsidy are based on 60 percent of the monthly salary earned by the employee, and 1.25 percent of the monthly base salary for each month of payments withheld in excess of \$180.
- The minimum amount of the subsidy is US\$255, and the maximum US\$1,500 per month.
- To be eligible for benefits, an employee should meet either of the following requirements: (1) declared disabled by the Social Security Administration; (2) have paid social security for a minimum of three years; and, (3) at the time of becoming disabled, have an accumulation of no less than half of the required premium payments (which should be accumulated three calendar years prior to the disability).
- If the insured person has credited a minimum of 180 payments at the time that the disability occurs, the requirement involving accumulation of payments is no longer valid.
- Any insured person, who has not fulfilled the requirements mentioned at the time of the disability, is entitled to an indemnity.
- Every disability pension is provisionally granted for a maximum of two years.
- If the disability continues after two years, the pension is for life, but subject to the Social Security Administration's periodic review, which will determine if the disability will continue.

Maternity Leave

- During the course of pregnancy, childbirth, and post birth, insured female workers are entitled to any prenatal and obstetrical care, as necessary.
- In addition, insured women who have paid social security for a minimum of nine months during the year preceding the seventh month of pregnancy will receive maternity payments from the Social Security Administration, for six weeks prior to giving birth and an additional eight weeks following childbirth.
- The amount of the weekly subsidy or benefit will increase to the middle weekly salary over which the individual would have contributed during the last nine months of contributions.

Workers' Compensation (Occupational Hazards)

- Occupational hazards are defined as accidents and illnesses to which workers are exposed as a result of their duties.
- Workers' compensation premiums are established in proportion to the amount of salaries paid. They are based on the company's industry and its inherent risks.
- In the case of accident or illness, the insured person has the right to receive any necessary medical, surgical and hospital treatment, and obtain medical supplies and other therapeutic treatments, as required.
- In addition, the insured is entitled to the normal supply, repair, and renewal of any orthopedic or prosthetic apparatus, if these treatments are deemed necessary due to the injury suffered.
- In the case of permanent disability, the insured person is entitled to a sum, which is established according to a disability scale, up to a maximum of 60 percent of the monthly salary.
- If the insured person dies on account of an occupational hazard, the person's beneficiaries are entitled to a pension.

Death Benefits

- In the case of the insurer's death, those surviving the deceased are entitled to a pension if the deceased fulfilled the withholding requirements (for disability or if the deceased paid social security for a minimum of 3 years).
- Moreover, if the insured person was disabled or was receiving an old-age pension on the date of death, the beneficiaries are entitled to a pension.
- A surviving spouse is entitled to 50 percent of the disability or old-age pension received by the insured as of the date of death. This pension is payable for five years.
- However, if after this period elapses, the widow is disabled, has reached normal retirement age, or is in charge of minor children receiving a family allowance, the pension will continue to be paid for life (in the first two instances), or until the children are 14 years of age (or 18 if they are students). The surviving spouse's pension is suspended if the spouse remarries.
- If there are no surviving spouse or children, a pension on a lesser scale is payable to the deceased worker's mother and father (under certain conditions).
- If the deceased worker has not fulfilled the withholding requirements, the worker's survivors are entitled to an indemnity.

Funeral Subsidy

To help cover funeral expenses associated with the death of an insured person, whether active or retired, the Social Security Administration pays a fixed amount of US\$300.

Retirement Pension

The objective of the retirement pension is to replace, within certain limits, the salary no longer received by the insured upon retiring.

- A new system became effective as a result of Law 51 of 2005.
- Age requirements and the number of quotas are requested.
- The minimum age for obtaining a pension is between 55 and 60 years (depending on gender).
- Effective January 1 of 2008, to be entitled to receive an old-age pension, women must be 55 years of age and men must be 60 in order to apply for a special retirement pension (substantially lower than the standard pension).
- Generally, women must be 57 years old and men must be 62 as minimum ages, in addition to having paid social security for at least 20 years.

Old-age retirement pension

Old Age Pension	
Date	Quotas
Until 12/31/2007	180
From 01/01/2008	216
From 01/01/2013	240

The minimum number of quotas is 180 to become eligible for an old age retirement pension through December 2007. The quotas increased to 216 paid quotas from January 2008 and to 240 quotas from January 2013.

Maximum Amounts for Retirement Pensions

- Until December 2006, the maximum amount for a pension was US\$1,000 per month. However, if a person contributed to the pension for a period of no less than 25 years, and earned an average salary of no less than US\$1,500 during 15 years, the maximum amount is US\$1,500.
- Since January 2007, the maximum amount was set at US\$1,500 unless the requirements to qualify for US\$2,000 were met.
- If the insured person has not paid social security for the full 20 years upon completing the minimum age required, and wishes to retire from employment, the insured person may ask to be granted an indemnity (lump sum amount).
- Prior to December 2009, the monthly base salary for calculating the old age pension was the average salary received during the insurer's best seven years in which social security was paid.
- Effective January 2010, the average salary will increase to the insurer's best ten years.
- The amount of the monthly old age pension is equal to 60 percent of the monthly base salary, plus 1.25 percent for withholdings collected in excess of 20 years.
- When the insured fulfils the requirements for old-age pension at a normal age and continues working, an additional two percent will be applied for every year.
- In addition, a family allowance of US\$20 is paid to the spouse or companion and US\$10 for every child under the age of 18.
- This family allowance is limited to a total of US\$100 per month.
- The amount of the pension plus the family allowance cannot exceed 100 percent of the base salary used to estimate the pension, with a minimum monthly benefit of US\$175 and a maximum of US\$2,000.
- The minimum amounts will be revised every three years or before, and if the financial situation allows for this, the pensions may be increased.
- When the insured person has paid for at least 30 years and the average monthly salary is no less than US\$2,500 during a 20-year period, the maximum pension will be US\$2,500 per month.

If an employer has not paid social security withholdings due to bankruptcy or insolvency (which allows the employee to a complete old-age pension) the employee may cancel the corresponding debt.

Working After Retirement Age

The Supreme Court decision that was highlighted is generally applicable to the public and private sectors. However, there are regulations in the labor code (not addressed in this court decision) that employers from the private sector may apply.

A decision from the Supreme Court of Justice makes clear that it is not necessary to stop working in order to obtain an old-age pension.

The court decided that various phrases contained in two articles of the Social Security Law (Law 51 of 2005) were unconstitutional. The court determined that various phrases violated the constitution which protects the right to work, the freedom to pursue any profession or trade and the right to acquire private property in accordance with the law.

In this way, it is understood that upon satisfying the age requirement and amount of contributions (when applying for an old age pension), the policyholder rights are advanced to an

acquired category (which becomes part of the estate of the policyholder). This is guaranteed by the Constitution; the policyholder has to stop working to benefit from the pension.

Expatriates

Panama's Social Security authority (*Junta Directiva de la Caja de Seguro Social*) approved Resolution 34, 498 -2007-J.D. of March 23, 2007 implementing the General Regulation for Registering with the Social Security System (*Reglamento General de Afiliación e Inscripción en el Régimen de Seguridad Social*). We briefly discuss the provision in the Regulation that concerns international executives.

Article 21 of the regulation expressly states, "Every employee whose salary is paid from a foreign source or who possesses a special temporary visitor's visa (*visa de visitante temporal especial*) is exempted from mandatory participation in the social security system, in line with the provisions of Cabinet Decree 363 of December 17, 1970 and Decree 236 of 16 June 1971." Although a new migration system was enacted in 2007, the status of this special visa has not been modified.

Cabinet Decree 363 of December 17, 1970 contains the rules determining the temporary residence and visa status of executives working for international companies doing offshore business in Panama. Decree 236 of 16 June 1971 regulates the Cabinet Decree by further stipulating the qualifications for coverage under the Cabinet Decree.

The new rules provide clarity concerning the obligations of qualifying international executives with regard to Panama's social security system.

The Social Security Authority expressly acknowledges that, generally, any international executive with such special visa need not participate in the Panamanian social security system, and her/his employer should not make salary deductions for social security contributions. The new migration rule (Law Decree 3 of 2008) does not address the social security status as the social security matter is governed by its own set of rules (Resolution of Affiliation).



Tax Authorities

Chapter 16



16 Tax Authorities

Taxation Administrative Court of Appeals (TAT)

According to Law 8 of 2010, the *Tribunal Administrativo Tributario* (TAT) has been called to attend appeals emerging from the governmental or administrative controversies. This administrative tax court of appeals, the second and final administrative level for taxpayers, replaced a former agency and deals with tax litigation coming solely from the Directorate General of Revenue which manages the majority of national taxes, except for customs duties and social security contributions. Municipal taxation is also dealt with separately. The TAT decisions might be revised by the Third Chamber of the Supreme Court of Justice.

General Directorate of Revenue

The General Directorate of Revenue of the Ministry of Economy and Finances (known as DGI, as per the acronym in Spanish) is the government institution in charge of overseeing and collecting revenues, services, rights, taxes, tolls, fees, duties, and excise taxes for the state, except for those referred above.

Since January 2006, it has been in charge of collecting social security contributions from self-employed workers to assist the Social Security Administration (CSS).

Reimbursements and Payments

- Any individual or legal entity required to pay income tax must file an income tax return.
- The deadline is March 15 for individuals and March 31 for legal entities with fiscal calendar periods.
- Legal entities with different fiscal periods should file their tax returns within one (1) month after the closing of their authorized special fiscal year.

Taxpayers may apply for an extension of up to one month with the Directorate General of Revenue prior to the deadline for filing the tax return. However, the income tax assessed for the taxpayers should be paid by March 31, at the latest.

The taxpayer must pay the corresponding interest and penalties if there is a balance due at the time of filing the tax return. The return must include an affidavit of income obtained during the preceding taxation year, dividends or earnings that were distributed to shareholders or partners, as well as interest paid to creditors.

Various Scenarios

- In the event where a taxpayer requested an extension for filing the income tax return, such extension will expire on April 15 for individuals and April 30 for legal entities;
- As a reminder, individuals with balances are required to pay income tax, which expires on March 31. This is the case even if the taxpayer missed the March 15 deadline to file the mandatory income tax return or request an extension;

- Likewise, for legal entities: the payment term expires the same day as the deadline to file their income tax return or an extension – which is March 31. Legal base: Section 710 of the Tax Code

Income Tax Return

- The extension to file a tax return is limited to one month.
- A fine is levied for the filing of amended returns whenever they are filed more than 12 months after the filing of the original return: This fine is between US\$100 to US\$1,000.
- Individuals or legal entities established in the Colon Free Zone must file a tax return for income derived from internal and foreign operations. Nevertheless, only local operations are subject to Income Tax.
- Credits are deducted from future tax liabilities, or may be transferred or assigned to other taxpayers.
- Each employer must remit to the tax authorities a report on the total annual amount of wages, remuneration, or salaries paid to each permanent or temporary employee and the amount of tax withheld.
- Taxpayers must report the amounts of fees and commissions paid to other persons for professional services as well as rent and representation expense payments with their annual income tax return.
- Tax returns must be prepared using special forms provided by the income tax authorities. Failure to submit such a form on time does not relieve the taxpayer from the obligation to prepare a tax return.
- Additionally, tax returns must be prepared electronically with special software provided by the tax authorities.

Providing a false affidavit can result in fines of between two to five times the amount of tax avoided or imprisonment from two to five years.

Legal Entities

In the case of legal entities, sworn declarations must be signed by the legal representative, the general manager or the chief financial officer. When the legal representative of the company has operating duties at the time, this person's signature as legal representative should be replaced by that of the treasurer, the secretary, or another member of the board of directors who do not have operating duties within the enterprise. The signatories of this declaration are severally liable for its accuracy.

Disputes

Examination of Returns, Assessments and Appeals

- Returns are filed with the DGI electronically (www.DGI.gob.pa).
- A certificate of receipt is issued to the taxpayer as evidence of filing. If the DGI, after auditing a tax return, decides that more tax is owed, an assessment is issued through a resolution.
- A taxpayer may request an administrative review of the assessment from the General Directorate of Revenue in writing, within 15 days following receipt of the assessment.
- If the request for appeal is rejected, the taxpayer shall appeal with the *Tribunal Administrativo Tributario* (TAT). If the appeal is also rejected, the taxpayer may file a claim before the Supreme Court of Justice (Third Chamber). At this level, the decision is final. All evidence admissible under the Procedural Code is also valid in tax matters.

Priority of Amounts Owed to the National Treasury

The law establishes that amounts owed to the National Treasury have precedence over any other debts, except for the following: (1) amounts secured by a mortgage , (2) salaries and compensation owed to workers, (3) social security premiums and, (4) special cases anticipated in the Civil Code.

Penalties and Interest

- Late payment penalties consist of a 10 percent surcharge.
- In addition, interest at the rate of two (2) percent over the reference market rate set by the Superintendency of Banks, applicable per month of fraction, is charged on late payments for tax liabilities applicable in certain cases. This market reference rate will be set according to the rate charged for commercial loans, by local commercial banks six months prior.
- The General Directorate of Revenue is allowed to reach agreements to settle overdue tax debts.
- The 10 percent surcharge can be avoided if the taxpayer: (1) pays voluntarily, (2) pays within 15 working days following the notice of collection or, (3) pays within 15 working days as of the day of service of the corresponding resolution.
- If, as a result of a tax audit, a balance becomes due, and at the same time the taxpayer maintains credits with the National Treasury, such a balance will not be subject to the surcharges. Neither would it be subject to interest up to the amount of the credit owed by the Treasury to the taxpayer.

Payment of Taxes

All checks for the payment of taxes must be certified. Taxes may also be paid through the national banking network, which is widely used.

Compensation and Assignment of Tax Credits

Since the 1991 Tax Reform, the DGI has been able to authorize the compensation of liquidated and outstanding tax credits which originated since January 1, 1992, against equally liquidated tax debts of non-prescribed periods. It starts with the oldest (and even if the tax debt and the tax credit originate from different taxes), provided that they are administered by the Directorate General of Revenue. Similarly, the taxpayer is allowed to transfer liquidated and outstanding credits which have originated since January 1, 1992 in order to offset the tax debts of the assignee.

Seizures and Attachments

The Directorate General of Revenue is given the power to order, along with the service of the resolution requiring the payment of a tax debt, the seizure, confiscation or attachment of any of the taxpayer's properties, in order to guarantee the collection of taxes and fiscal debts.

Coercive Collection of Debts (changes to procedures, see Law 33-2010)

In the event that legal action must be taken to collect taxes and import duties, an additional 20 percent surcharge is imposed. The Executive Branch may hire agents for the collection of overdue payments and taxes when the debt is at least two years old.

Tax Evasion

Simulation of losses and other misrepresentations aimed to obtain an illicit benefit, incentive, exemption, reduction, deduction, or tax credit is considered tax evasion In 2019, Law 70, which

established prison sentences for tax payers, which are found guilty of evading taxes, for a higher amount of \$300,000.00.

Filing Requirements

An income tax return must be prepared and countersigned by a certified public accountant when the taxpayer's net worth exceeds US\$100,000 or when the yearly sales volume of the taxpayer exceeds US\$50,000.

Cessation of Business Activities

Individuals and legal entities no longer subject to income taxes because of cessation of business activities must submit tax returns and final balance sheets, within the following thirty days. Taxpayers must pay taxes up to the time of cessation of business. The debt of an estate is subject to taxes due by the deceased.

Statutes of Limitations

- Assessments for additional income tax issued after three years following the date of filing of the tax return are null and void, and the taxpayer is under no obligation to pay them.
- However, the statute of limitations for collecting income tax is seven years from the last day of the year in which taxes were due.
- For individuals and entities responsible for withholding income taxes, the statute of limitations is 15 years from the date the tax should have been withheld.

Issuance of Documents and Forms

Tax Clearance Certificate

A tax clearance certificate ("Paz y Salvo Nacional") indicates that the taxpayer has paid the income tax, the tax on transfer of tangible personal goods and provision of services, the education tax and/or social security contributions to either the National Treasury or the Social Security Administration.

A tax clearance certificate is required for the following:

- Payments by the National Treasury, Municipal Treasury and others except for employment compensation;
- Annual revision for commercial vehicles;
- The sale of tickets and permission to leave the country to travel abroad (only for non-permanent residents);
- Added by Law 51 of 2005, a tax clearance certificate for the social security obligation is also due when a business ceased operations as well as when applying for a business contract with the government or any of its autonomous or semi-autonomous institutions;
- Tax clearance certificates are issued for a specific period of time.

Invoicing

- Copies of issued invoices can be stored in magnetic files, digital files or other technological methods whenever they are requested by a taxpayer and authorized by the Directorate General of Revenue.
- Legal entities and independent professionals are obliged to use fiscal equipment ("Equipos Fiscales") to issue invoices to their customers and clients (Exceptions apply).
- The Free Zones form is discontinued and it is replaced with the "Income Tax Return - Special Systems", which must be used by taxpayers in the following categories:
- Colon Free Zone (Law Decree 18 of 1948);
- Tocumen International Airport (Law 23 of 2003/Cabinet Decree 30 of 2003);

- Petroleum Free Zones (Law 8 of 1987);
- Tax Free Zones (Law 32 of 2011);
- Panama Pacific Special Economic Area (Law 41 of 2004);
- City of Knowledge (Decree Law 6 of 1998);
- Any other system that has specific taxation measures.

Please note that additional reports that must be submitted to the tax authorities – refer to the Directorate General of Revenue:

1. Certification of interest on mortgage loans (residential without preferential interest) - By lenders/credit companies;
30. Retirement funds, pensions and benefits report - By entities;
31. Insurance companies report – certification of medical expenses of policyholder - By policy providers;
32. Report of purchases and importing of goods and services - By legal entities and natural/individual persons according to gross income and/or total assets totaling between US\$1 million and US\$3 million, respectively;
33. Non-filer report (according to gross income and/or total assets of US\$1 million and/or US\$3 million, respectively).

Taxpayer Identification Number (TIN) or RUC

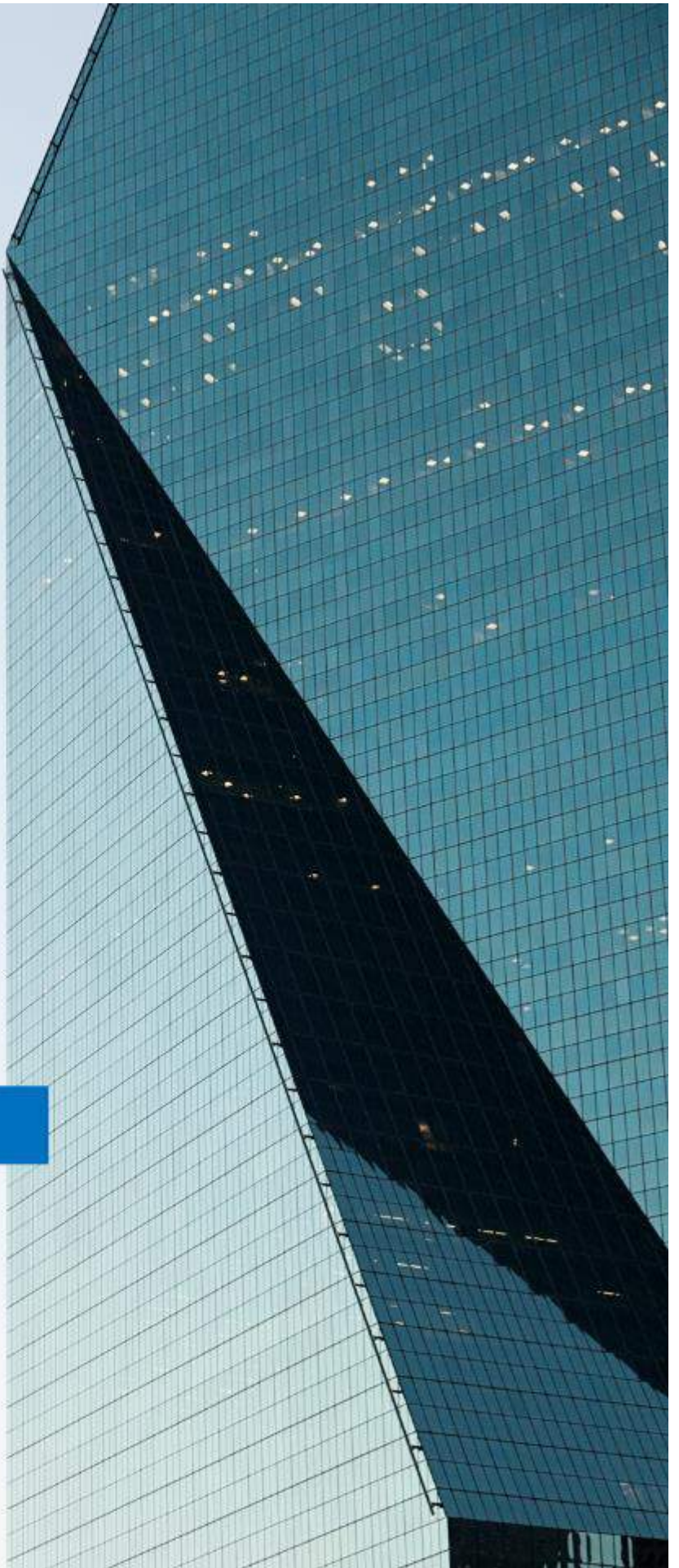
- Every individual or entity that pays taxes must apply for a taxpayer identification number (TIN) by filing the TIN form, or RUC by its initials in Spanish. This stands for Taxpayer Unique Record number in accordance with Law 76 of 1976.
- For an individual, a TIN refers to the Panamanian tax identity number with the Civil Registry or the passport number.
- For a legal entity, a TIN refers to the Panamanian tax identity number related to the Public Registry.
- Also, a taxpayer number (TN) is given to foreigners, either individuals or entities, including joint ventures.
- Should this be needed in Spanish, a TN is called NT (*número tributario*).

*Executive Decree 539 of 2011 states that any payment shall be applied to the oldest debt.



Financial Sector

Chapter 17



17 Financial Sector

Banking System

Decree-Law 9 of 1998, which reformed the banking system established by Cabinet Decree 238 of 1970 and created the Panamanian Superintendency of Banks (*Superintendencia de Bancos de Panamá* - SBP for its acronym in Spanish), was updated and modified by Decree-Law 2 of February 22, 2008, later amalgamated by means of Executive Decree 52 of April 30, 2008, in order to comply with international regulatory standards and to make the banking sector more competitive.

Panama as an International Banking Center

Panama's geographic location, which helps position it as an international commercial center, and the growth of the Eurodollar market, are some of the most important factors contributing to the country's emergence as an international banking center.

Banking Facilities

For more than 40 years, Panama has quickly grown as an international banking center. The country has eighty eight (88) banks, of which forty-eight (48) are under a general license, twenty-seven (27) are under an international license, and thirteen (13) are representation offices. Seventeen (17) of these institutions are Panamanian-owned banks, as well as two (2) governmental institutions (owned by the State) and the remaining banks have foreign operations.³

The Panamanian Superintendency of Banks

The SBP is the entity responsible for overseeing and managing the banking system, including the prevention of money laundering in the banking system and the financing of terrorist activities. The entity is also entrusted with the protection of consumer rights.

The SBP is an independent institution, but is subject to supervision by the General Comptroller of the Republic of Panama (*Contraloría General de República de Panamá*). The SBP is integrated by the Superintendent and five members of the Board of Directors, which are chosen by the Executive Branch.

The following are some of the SBP's responsibilities:

- Authorize and issue licenses to engage in banking activities;
- Determine, at an administrative level, the interpretation and scope of legal banking provisions;
- Periodically set forth the legal reserves and the percentage of liquidity applicable to banks;
- Carry out inspections of banks, so as to determine their financial situation and compliance with regulatory provisions;
- Intervene, when necessary, in the affairs of banks, appointing a trustee who will assume the administration thereof; and

³ Information extracted from the statistical report issued by the SBP dated May 2017.

- Sanction any breach of banking regulations.

Foreign supervisory entities may request information and carry out inspections of branches and subsidiaries of foreign banks in Panama, in which they exercise consolidated supervision. Information that is obtained in this manner is kept strictly confidential and cannot be disclosed without prior authorization from the SBP.

Licenses to Engage in Banking Activities

Except for official Panamanian banks, no individual or entity can engage in banking activities without prior authorization from the SBP.

The SBP issues three (3) types of licenses depending on the intended activities of the banking institution:

- General license: issued to banks organized under the laws of the Republic of Panama and authorized branches of foreign banks to engage in local and offshore banking activities, as well as in other activities, as authorized by the SBP;
- International license: issued to banks organized under Panamanian laws and authorized branches of foreign banks to conduct, from an office established in Panama, transactions that are completed or carried out outside Panama, and to engage in other authorized activities;
- Representation license: issued to foreign banks for the establishment of a representation office in Panama, and to engage in other authorized activities.

There are no restrictions on the type of services that can be offered, as long as they are within the scope of normal banking business practices.

In addition, banks are obliged to pay annually a Regulation and Supervision Fee, which will depend on the type of license:

- General license: Thirty thousand US dollars (US\$30,000.00), plus thirty-five US dollars (US\$35.00) per million, or fraction of a million, of the assets of the bank, up to a cap of one hundred thousand US dollars (US\$100,000.00).
- International license: Fifteen thousand US dollars (US\$15,000.00).
- Representation license: Five thousand US dollars (US\$5,000.00).

Capital Requirements

- Every bank doing business in Panama, under a general license, must meet the minimum requirement of ten million US dollars (US\$10,000,000.00) of paid-in or assigned capital established by the SBP.
- Banks engaged exclusively in offshore business (banks with an international license) must deposit two-hundred fifty thousand US dollars (US\$250,000.00) in the National Bank of Panama and have a minimum paid-in capital of three million US dollars (US\$3,000,000.00), to guarantee the proper fulfillment of their obligations under the banking license.
- Licensed banks (either general or international license) cannot reduce capital from the minimum amounts set out above. The SBP must authorize any reduction to capital.

Liquidity Reserve Requirement

Every bank holding a general and international license (the latter if the SPB is its original supervisor) must maintain a legal reserve of cash assets not exceeding 35 percent of its gross local deposits (excluding deposits from related entities).

Bank Tax

Aside from any income tax or any other tax obligations for banks, there is an annual bank tax which will depend on their assets and type of license:

General License	Tax per annum
Up to US\$100 million in total assets	US\$75,000
More than US\$100 million up to US\$200 million in total assets	US\$125,000
Over US\$200 million up to US\$300 million in total assets	US\$175,000
Over US\$300 million up to US\$400 million in total assets	US\$250,000
Over US\$400 million up to US\$500 million in total assets	US\$375,000
Over US\$500 million up to US\$750 million in total assets	US\$450,000
Over US\$750 million up to US\$1,000.00 million in total assets	US\$500,000
Over US\$1,000 million up to US\$2,000 million in total assets	US\$700,000
Over US\$2,000 million in total assets	US\$1,000,000

During its first year of operations, banks with a general license will pay fifty percent (50%) of the annual tax.

International License	US\$75,000
Development and micro-finance banks	US\$30,000

Superintendency of the Securities Market

Law 67 of 2011 creates the Superintendency of the Securities Market (*Superintendencia del Mercado de Valores* – SMV for its acronym in Spanish). In addition, the unified text of Decree-Law 1 of 1999 regulates the securities market in the Republic of Panama.

As indicated in the unified text of Decree-Law 1, the SMV is an autonomous governmental institution, with its own patrimony and administrative independence. The SMV is composed of the Superintendent, who acts as the legal representative of the institution and is in charge of management of such and of a Board of Directors, which acts as its ultimate consultative, regulatory and policy-making body.

The Superintendent and the Board of Directors must comply with ethical standards in order to avoid conflicts of interests and unethical practices. Decisions made by the SMV may only be contested for reconsideration and appealed before the Board of Directors, within a period of 5 days following the date of its notification.

Law-Decree 1 regulates the following areas, among others:

- Investment fund managers;
- Investment advisors;
- Securities brokerage firms;
- Forex (FX) trading;
- Credit rating agencies;
- Pension funds;
- Investment corporations (mutual funds); and
- Self-regulated organizations.

Brokerage entities must, however, comply with the following regulations:

- All equity of the brokerage entity must be issued in a nominative form and the holder must be declared to the SMV;
- Change of ownership must be authorized in advance by the SMV;
- Banks with an international license may obtain a license from the SMV, in order to address, from their office, securities-related transactions, including those registered with the SMV;
- Earnings from transactions processed in Panama, sold between effective owners from abroad and completed overseas, will not be considered as income earned within the Panamanian territory for income tax purposes;
- The bookkeeping, records and financial statements of these entities must meet the requirements and regulations issued by the SMV;
- Transactions for registered securities that are traded outside a stock exchange must be reported to the SMV as well as to investors;
- Brokerage entities must keep all assets of their investors in investment accounts, according to the regulations of the SMV;
- The SMV will regulate confidentiality, ethical standards, conflicts of interest and investment advice;
- The SMV, in order to comply with Law-Decree 1, may request the appointment of a compliance officer for each brokerage entity;
- Brokerage entities and brokers must obtain a license from the SMV, in order to perform any type of securities transaction in the country.

Law-Decree 1 establishes the following rules concerning stocks, bonds, shares and any other securities:

- Each public offering or sale must be registered with the SMV;
- Any offering or sale to individuals living in Panama will be considered as an offering within the country, whether it has been made from Panama or from abroad;
- Public offerings or sales in Panama, to investors living abroad, are to be regarded as public offerings not made within the country;
- Offers exempted from registration with the SMV include: (1) offerings made or guaranteed by the State, (2) private placements, (3) offerings made through institutional investors, (4) corporate transfers and (5) offerings or sales made exclusively to employees of the issuer;
- The law decree also regulates both the securities exchange seat, and the administrator involved in any securities exchange activity.

Tax Incentives

- No income tax, income tax on dividends or complementary tax is imposed on gains or losses resulting from the transfer of securities issued by the State.
- Gains and losses on the transfer of securities registered with the SMV may not be taxed if such transfer is made:
 1. through a stock exchange or another organized market; or
 2. as the result of a corporate merger, consolidation or reorganization, as long as the shareholder receives only other shares from the surviving or affiliated corporation.
- Income derived from shares registered with the SMV will be taxed at a five percent (5%) standard rate; the entity paying said interest must withhold the total amount. The income will not be considered for taxation purposes and there is no obligation to include it in the annual income tax return.
- No stamp duty is required for shares registered with the SMV, or any other document related to contracts, subscriptions, sale, payment, transfers or exchanges of these type of assets.
- Capital gains derived from a non-exempt transfer of securities shall be taxed at a ten percent (10%) fixed rate. Nonetheless, in these transactions the transferee or purchaser must withhold a five percent (5%) advance on capital gains, from the total value of the transaction. The general rule on capital gains tax is applicable to this transaction (please refer to Chapter 4).

Capital Requirements

Stock exchanges must have paid-in capital of no less than one million US dollars (US\$1,000,000), free of encumbrances and the confidentiality of their operations must be assured. Also, stock exchanges must post a report of all transactions, stock exchanges, prices, volumes and any other statistical data of interest to investors and the general public at the end of each day.

Audited Financial Statements

Audited financial statements prepared by an independent public accountant must be submitted to the SMV at the end of each fiscal year.

Trust Operations

One of the legal advantages of trusts is the protection provided to assets. Tax benefits granted to trusts include:

- No taxes are levied upon the transfer of trust assets located abroad and from non-taxable sources in Panama.

- Money deposited by individuals or legal entities whose income is not from a Panamanian source or taxable in Panama is not taxable.
- Shares or securities of any type, issued by entities whose income is not from a Panamanian source, are not subject to tax in Panama.

As per Law 1 of 1984, regulated by Law 21 of 2017, trust regulations include supervision from the SBP. In addition to the commercial license granted by the Ministry of Commerce and Industries, trust activities must be subject to a fiduciary license issued by the SBP. The word “trust” or its derivatives in any language can be used only by individuals or companies authorized by the SBP to carry out such operations.

Local Finance Companies

Finance companies, although small, are part of Panama’s financial center, and contribute to the economic development of the country by providing financial resources through loans and credit facilities to the public.

- The Ministry of Commerce and Industries authorizes the operation of these companies, which must obtain a commercial license and must have a minimum paid-in capital of US\$500,000, according to Law 42 of 2001.
- Local finance companies are regulated separately from banks, insurance companies, cooperatives, pawnshops, mutual fund companies and furniture companies.

Financial Leasing Activities

Financial leasing activities are conducted by licensed banks and non-banking companies authorized by the Ministry of Commerce and Industries. Some of the benefits granted are:

- Depreciation over the number of years covered by the leasing contract, with a minimum of three years;
- Deductibility of expenses inherent to the leasing contract, such as insurance premiums;
- For vessels and aircraft engaged in international trade, the income from the lease will not be considered as taxable income in the Republic of Panama;
- At the end of the contract, the lessee has the option to depreciate the asset according to its residual value;
- The value of the lease will be considered a deductible expense for the lessee as long as the leased asset is utilized in the production or maintenance of the source of taxable income;
- The amounts paid by the lessee are not subject to ITBMS (local VAT).

The lessor must normally be engaged in leasing contracts and be the owner of the leased goods. Goods such as ships, aircraft, machinery, equipment, vehicles and any other movable goods capable of being specifically described can be the subject of leasing contracts. The contract must be signed for a term of no less than three years.

International leasing contracts are also granted incentives such as total exemption from income taxes, as well as stamp and sales taxes. Parties involved can also agree on changing a local contract into an international contract, or vice versa.

Money Remittance Houses

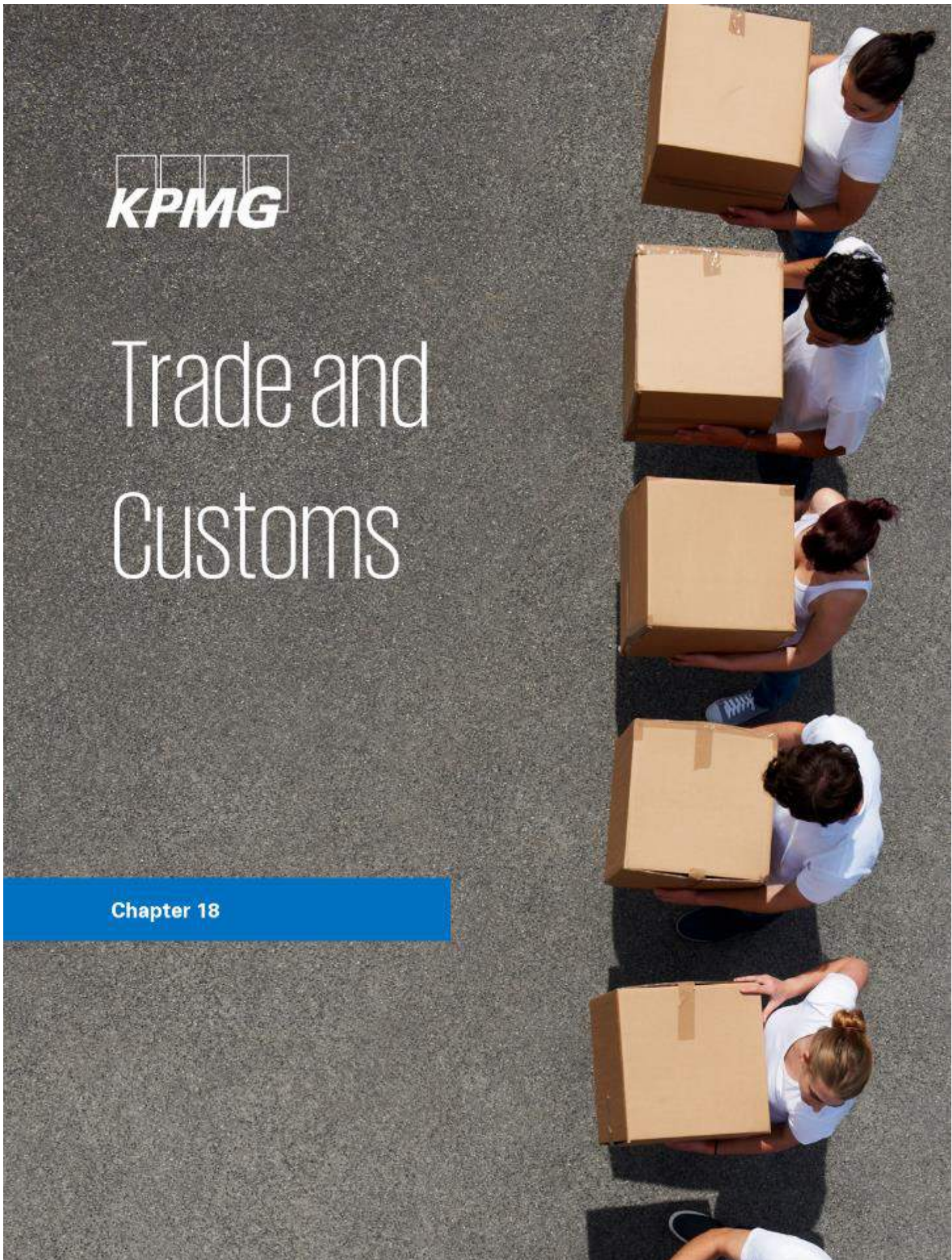
Remittance of money through a company established appropriately is fully regulated by Law 48 of 2003. This law requires a minimum capital of fifty thousand US dollars (US\$50,000.00) to start operations in Panama, as well as a US\$50,000 performance bond in favor of National Treasury. Furthermore, a commercial license is required plus a fee of one thousand US dollars

(US\$1,000.00) for the issuance of an authorization certificate by the Ministry of Commerce and Industry.



Trade and Customs

Chapter 18



18 Trade and Customs

Under Law 26 of April 17, 2013 "Incorporating the Republic of Panama into the Subsystem of Central American Economic Integration", the common agreement of the Central American countries is adopted, whose purpose is to establish the basic customs legislation of the Parties according to the requirements of the Central American Common Market and the regional integration instruments, in particular the Convention on the Central American Tariff and Customs System.

Entry and Exit of Goods and Forms of Transport

- The entry and exit of persons and goods and forms of transport from the customs territory can only be carried out in the places, routes and schedules authorized by the customs authority.
- The forms of transport and the types of merchandise that cross the borders of Panama or authorized sites will be under customs control when entering and leaving the customs territory.
- Travelers and carriers who introduce goods through any form of transport will present them and immediately report them to the customs authority.

The deadlines for reporting the entry of goods

a) Goods entering the territory by sea: notification of arrival forty-eight (48) hours in advance.

b) Goods entering the territory by air, must be transmitted at least two (2) hours in advance. If the time of transport between the ports of departure and destination is shortened, the transmission must be made at least in an advance of such deadlines.

- Customs authorities establish a tariff for the customs maritime monitoring service. This fee will be canceled by the captain or representative of the shipping agency to the ship prior to shipping to the customs authority.
- The customs authority may adopt the following control measures during the receipt of the transport:
 1. Inspection and registration of transport forms,
 2. Closing and sealing of compartments with goods,
 3. Review of customs documents, and
 4. Permanent surveillance of transport.

Transshipment

- The canal area, composed of the maritime port terminals of the Panama Canal in the Pacific Area and the maritime ports of the Province of Colon, allows for international trade of goods and is considered as a sole primary zone of special jurisdiction within the customs territory.

- The Administrative Rate of Transshipment Service (TAST in Spanish), which amount is five dollars and 00/100 (\$5.00), is established and applicable for each container, trailer, semi-trailer or vehicle (in case of piece goods), that moves transferred goods between at least two (2) of the customs port enclosures within the canal area considered as the sole primary zone of special jurisdiction.
- All goods intended for transshipment can remain within the customs enclosures up to three (3) months; after such term, they will be declared abandoned.
- The containers subject to transshipment by road will be inviolable. However, the customs authorities or any other appropriate authority may exercise authority to open shipments for safety reasons.

Special Service - for Customs Control and Monitoring

- The Special Service for Customs Control and Monitoring, a division of the customs authority, ensures the application of the customs provisions, and controls, monitors, supervises, and inspects the commercial operations subject to customs regulations and all customs operations concerning foreign trade in the country, as well as the entry and exit of goods to or from the customs territory and the zones or separate areas or those with special regulations.
- All individuals or legal entities are required to hire the Special Customs Control and Monitoring Service, and set up guarantees for the amount of a month of salary equivalent to each year of contracted service.
- The rates of the Special Customs Control and Monitoring Service are as follows:
 - a) The service of one public employee will cost US\$1,000.00 per month; and
 - b) Additional public employees will cost US\$ 800.00 per month.

Simplified Procedure for the Dispatch of Household Goods

- The Declaration of Goods for the import and export of articles for non-commercial domestic use will be drawn up by the reporting parties, who will not pay customs duties.
- Automotive vehicles, or machinery, equipment, tools or accessories for offices, laboratories, consultancies, factories, are not considered as household goods and customs duties must be paid.
- For unaccompanied baggage provided for in sections 113 and 114 of the Central American Single Customs Code, the application must be submitted to the customs authority, with a copy of the transport document and a photocopy of the owner's passport.

Dispatch System with Guaranteed Global Payment

- The dispatch system of goods with guaranteed global payment is made for goods that enter the national customs territory under the system for importing goods for consumption, temporary admission or any other customs system.
- Either the natural or legal persons that want to accept the system of guaranteed global payment must submit an application before the Technical Procedure Department of the National Customs Authority and have a guarantee valid for more than sixty (60) days following the last extension given, with the purpose of allowing the Authority to carry out collection.
- Requirements to accept the dispatch system with guaranteed global payment. The application, in order to accept the dispatch system of guaranteed global payment, must be accompanied by the following documents:

- c) Application issued by the Customs Broker or its Legal Representative;

- d) Authenticated copy of the identification card or personal passport if the applicant is a natural person;
- e) Authenticated copy of the Articles of Incorporation;
- f) Copy of the identification card or passport of the legal representative;
- g) Description of the goods withdrawn under the system of Global Guarantee;
- h) Statistical chart that reflects the customs destination for the goods from the requesting person or company, estimated to be the six (6) last months from the date of the application. Either natural or legal persons, that do not have customs destination registry, must submit a viability study which shows the economic impact that will be generated by the activity in order to determine the guarantee amount, dully endorsed by the Authorized Public Accountant;
- i) Certificate of non-customs fraud and free of charges before the Inspector General of Taxes;
- j) Authenticated copy of the Operation Certificate, if applicable; and
- k) Company's certificate of registration in the Public Registry, in the case of a legal person.

Category of Goods	Applies Guaranteed Payment
a) tourism	NO
b) shows	NO (Only if it has customs personnel for its safekeeping)
c) leisure and sports	NO
d) professional equipment and material	NO
e) human aid	NO
f) educational, religious, and cultural	NO
g) scientific	NO
h) performance of public works	YES
i) state	NO
j) containers and transportation	NO
k) units and forms of transport and spare parts for their repair	YES
l) commercials	YES
m) films and other material for the playback of sounds and images	YES
n) aircraft, rented in due time or with an option to purchase	YES
o) authorized by specific standards, international agreements, or customs service.	Conditional

Tariff Exceptions

- The following are exempted from payment of import customs duties:

- l) Imports by the State for the acquisition of food, medicine, sports equipment, hospital equipment, materials, equipment, the delivery of aid, laboratories, ambulances, mobile clinics, similar technological equipment and similar educational material for use in educational centers, as well as donations received by the state, municipalities, and municipal councils;
- m) The donations to non-profit private organizations intended to cover services concerning healthcare, food, the delivery of aid, technical assistance, charity, medical assistance, education, scientific and cultural research, as long as they have signed agreements for human and social aid and cooperation with State institutions;
- n) The import of goods by virtue of the contracts or international agreements pertaining to economic integration expressly established and celebrated in the Republic of Panama and confirmed by the National Assembly;
- o) Imports by the members of the diplomatic corps recognized in the Republic of Panama for their personal use and according to the treaties and regulations under the International Law for strict reciprocity;
- p) Educational equipment and material, and other items necessary for the development of teaching in official, particular schools, which will be granted when the following conditions are met:
 - 1. When the purchase of those items is made with the funds belonging to educational centers or parents' associations; and
 - 2. When the related item is not produced in the country and falls into the following categories:
 - i. Technical teaching equipment, laboratory, audiovisual, music, and teaching demonstration models;
 - ii. Badges and trophies for cultural, sports contests;
 - iii. Graduation rings for students; and
 - iv. Other convenient, indispensable items by judgement of the Ministry of Education.
- q) Medical equipment, instruments, and devices, machinery and construction materials destined and made for hospitals, that are not produced in the country, and necessary for the construction, expansion, reconstruction, and operation of hospitals or clinic-hospitals that have the capacity to provide service to twenty or more patients hospitalized simultaneously;
- r) Motor vehicles, educational, technological material, and other items necessary for the development of pastoral activities that are carried out by the Catholic Church, and the traditional, historic churches such as Lutheran, Anglican, Evangelical, Methodist, Adventist, Greek Orthodox, Baptist, Jewish, Muslim, Buddhist, and the Jehovah's Witnesses;
- s) The equipment, devices, and other accessories for the control, support, and safety intended to the Ministry of Safety, the Service of Institutional Protection, the Council of National Safety, and other institutions that perform activities to ensure public safety;
- t) Those protected by either special or contract laws, as long as the goods subject to the exemption must be linked to the activity or event developed.

Reimbursement of Customs Duties

- When missing goods are detected, or an error concerning weight, quantity, measurement, or value stated has been made causing the payment of additional taxes, a refund of the excess taxes can be requested from the customs authority.
- The request for excess taxes paid can be submitted to the respective regional customs administration, within a period of 4 years from the date of registration.
- The refund of customs duties will apply in the following cases:
 - u) Imported goods found to be defective or not in conformity with the specifications agreed to at the time of import and returned to the supplier;
 - v) When missing goods are detected or an error is created in relation to weight, quantity, measure or declared value that causes a higher tax payment;
 - w) Goods that have been incinerated or exported definitively;
 - x) When the merchandise is defective or destroyed by an accident or external causes; and
 - y) In the cases provided for in the Free Trade Agreements in force in the Republic of Panama.



Appendix

Investment in Panama

Appendix

KPMG in Panama

KPMG is the global network of professional services firms of KPMG International. Our member firms provide audit, tax and advisory services through industry-focused, talented professionals who deliver value for the benefit of their clients and communities. With over 189,000 people worldwide, KPMG member firms provide audit, tax and advisory services in approximately 152 countries.

KPMG in Panama was established in 1958 and is rapidly becoming one of the largest professional services firms in the local market.

We are part of KPMG Central America S. A. (KCA), a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative.

In Panama, we operate with 17 partners and over 330 specialized and customer service-focused professionals from different branches grouped into multidisciplinary teams which seek to address the specific needs of the Panamanian market through deep knowledge of the local regulatory framework and continuous training.

Why KPMG?

- We lead by example — At all levels we act in a way that exemplifies what we expect of each other and our member firms' clients.
- We work together — We bring out the best in each other and create strong and successful working relationships.
- We respect the individual — We respect people for who they are and for their knowledge, skills and experience as individuals and team members.
- We seek the facts and provide insight — By challenging assumptions and pursuing facts, we strengthen our reputation as trusted and objective business advisers.
- We are open and honest in our communication — We share information, insight and advice frequently and constructively and manage tough situations with courage and candor.
- We are committed to our communities — We act as responsible corporate citizens by broadening our skills, experience and outlook through work in our communities and by protecting the environment.
- Above all, we act with integrity — We are constantly striving to uphold the highest professional standards, provide sound advice and rigorously maintain our independence.

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