

Country Guide

Panama

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1. Overview

1.1. Government and Tax System

Panama is a presidential republic. Under the Constitution,¹ the government is divided into three branches, as follows:

- the executive, with the president as both chief of state and head of government, who is elected by simple majority popular vote for a five-year term;
- the legislature, consisting of a unicameral National Assembly comprising 71 seats, with members elected by popular vote for a five-year term; and
- the judiciary, with the Supreme Court of Justice as the highest court.

The tax authority is the General Directorate of Revenue (*Dirección General de Ingresos*, or DGI), a subordinate body of the Ministry of Economy and Finance. The power to tax rests with the national government, through legislation enacted by the National Assembly, and at local level with municipalities. Panamanian taxes are codified in the Fiscal Code,² which, along with certain ancillary laws, executive decrees and resolutions, provides the basis for most taxes imposed in the country.

A law enacting a new Tax Procedure Code was published in the Official Gazette on February 14, 2019.³ The new code, whose provisions generally come into force on January 1, 2023 (aside from certain specific provisions that enter into force at an earlier date), does not replace the Fiscal Code, but establishes a framework of principles and rules governing the relationship between the DGI and the taxpayer.

Panama has adopted a territorial system, and taxes only income earned or connected to domestic businesses and activities. Foreign-source income (along with expenses relating to the generation of that income) is excluded from the tax base. As a result, residency is not a significant factor in determining the tax liability of persons and corporations. Residency is relevant primarily to the method of tax collection, with resident corporations and individuals being able to waive withholding on certain types of income.

1.2. Currency

Panama is dollarized and all paper currency in Panama is US dollars. Panama's official currency is the Panamanian balboa, which is pegged at 1:1 to the US dollar. Panama also has its own coins.

For ease of reference, all currency amounts in this guide are stated in dollars.

1.3. Membership of International Organizations

Panama is a member of the World Trade Organization (WTO), the Organization of American States (OAS), the G-77, the Community of Latin American and Caribbean States (CELAC) and the Central American Integration System (SICA).

1.4. Official Websites

The following are official tax, finance and other relevant authority websites for Panama:

- Tax Authority (Dirección General de Ingresos (Spanish only) – <https://dgi.mef.gob.pa/>
- Ministry of Economy and Finance (Ministerio de Economía y Finanzas (Spanish only) – <https://www.mef.gob.pa/>
- Official Gazette – <https://www.gacetaoficial.gob.pa/>
- PROPANAMA (government investment information platform) – <https://propanama.gob.pa/en>

¹ Political Constitution of the Republic of Panama, 1972, as amended.

² Law No. 8 of January 27, 1956, as amended (hereafter referred to as the Fiscal Code).

³ Law No. 76 of February 13, 2019, approving the Tax Procedure Code of Panama, as amended by Law No. 208 of April 6, 2021, art. 6, and by Law No. 257 of November 26, 2021, art. 5.

1.5. Automatic Exchange of Information

Panama has ratified the OECD's Convention on Mutual Administrative Assistance in Tax Matters, which entered into force for Panama on July 1, 2017.⁴

Panama is a signatory to the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information, and has enacted legislation to implement the Common Reporting Standard (CRS).

Panama has enacted legislation to implement a FATCA Model 1 IGA with the United States.

Panama is a signatory to the Multilateral Competent Authority Agreement on the Automatic Exchange of Country-by-Country (CbC) Reports.

Panama is a member of the Inclusive Framework on BEPS, a group of countries that is developing standards on BEPS-related issues, and is reviewing and monitoring implementation of the OECD/G20 BEPS Action Plan.

2. Corporate Tax Computation and Administration

2.1. Residence, Taxable Status, Entity Characterization

2.1.1 Residence

A resident corporation is any entity that is incorporated under Panamanian law or a corporation established abroad that has material means of administration and management in Panama and is registered under the Public Registry of Panama. However, since Panama operates a territorial tax regime, residency has limited relevance (mainly in determining withholding requirements). Foreign corporations can register with the tax authorities to be treated as "resident" for purposes of withholding taxes.

The following factors typically determine whether an entity is a Panamanian tax resident:

- it carries out commercial activities or performs a support function for other entities from Panama and has offices in Panama;
- as a logical consequence of carrying out commercial activities in Panama, an entity must have employees in Panama executing its activities; and
- a private interest foundation regulated under Law 25 of 1995 need not meet the commercial activities requirement set out above, but it must have material means of management and administration in Panama.

2.1.2 Taxable Status

In general, business entities operating in Panama are subject to the corporate income tax. Micro, small and medium businesses, including sole proprietorships that are registered as such, are subject to a separate graduated income tax regime (see Section 3.1.3). Generally, there are no fiscally transparent commercial entities.

Foreign companies' branches and agencies are required to obtain a license to operate in Panama. Additionally, branches are taxed as corporations and, at the end of their fiscal year, a 10 percent branch tax is payable on profits remitted to a foreign head office as their after-tax profits are treated as having been distributed as dividends and are subject to withholding on dividends. This rule does not apply to professional firms organized as civil partnerships, however, because such firms may deduct distributions to their partners. Partners report the income in their return and pay tax at the same rate as other individuals.⁵

Companies operating under the MHQ and EMMA regimes (see Section 2.6.4) are exempt from the branch tax.

2.1.3 Legal Classification of Nonresident Entities

As Panamanian law allows for the creation of alternative business forms (such as limited liability companies and limited liability partnerships), and all such business entities, other than sole proprietorships, are subject to corporate tax, Panama treats foreign business entities as subject to corporate tax. As such the specific legal form is of less relevance for tax purposes.

⁴ Law No. 5 of February 21, 2017.

⁵ Fiscal Code, art. 699, para. 4.

For company law purposes, a foreign company is defined as a company legally constituted in a foreign jurisdiction.⁶

2.2. Corporate Tax Base

2.2.1 Resident Corporations

Resident and nonresident corporations are taxed only on income generated in Panama or through domestic activity. With limited exceptions (e.g., taxpayers with losses that do not have an actual deductible expense and nonprofit entities), the expenses related to the domestic-activity-generated income must be deductible by the taxpayer in Panama for the activity to be considered related to Panama-sourced income.

The income tax base is generally limited to net business income from domestic activities as dividends and capital gains are subject to separate taxation and primarily collected through a withholding regime.

2.2.2 Nonresident Corporations

Due to its territorial system of taxation, Panama does not contain a definition of the term "nonresident company." Both nonresident and resident corporations are taxed only on income generated in Panama or through domestic activity. A nonresident company is considered for tax purposes a company that is not established in Panama. Foreign companies without a permanent establishment in Panama, but deriving Panama-source income, are subject to a final withholding tax. Permanent establishments of nonresidents are treated as separate entities for income tax purposes and are subject to the general income tax on their Panama-source income.

As with resident corporations, the income tax base is generally limited to net business income from domestic activities as dividends are subject to separate taxation collected mainly through a withholding regime. For nonresident corporations, the withholding regime extends beyond capital gains and dividends. However, a foreign company maintaining a Panamanian permanent establishment (PE) is eligible to register with Panamanian authorities and to be treated as a resident corporation for purposes of withholding and tax filing.

With regard to PEs, given that Panamanian taxation is limited to domestically sourced income regardless of residency or the existence of a PE, the consequence of being considered to have established a PE is primarily in whether payments will be subject to withholding (as resident or registered foreign companies are not subject to withholding in certain cases).

2.2.3 Non-Corporate Business Entities

2.2.3.1 Recognition

Panamanian law allows for the creation of general partnerships, limited partnerships, foundations and trusts. An individual may also operate a business as a sole proprietorship.

General Partnerships

General partnerships are governed by Title VIII, Chapter III of the Commercial Code. In a general partnership there is no limit to the liability of the partners, with each partner being liable jointly and severally with the others for the debts of the partnership incurred whilst that partner is a member of the partnership.⁷

Limited Partnerships

Limited partnerships are governed by Title VIII, Chapter IV of the Commercial Code.

A limited partnership consists of one or more general partners and one or more limited partners. Only the general partners are authorized to transact business and sign for and bind the partnership, and only they are jointly and severally liable for the debts of the partnership. Provided that the limited partners act solely as providers of funds to the partnership, and do not take part in the management of the partnership,⁸ they are only liable to the partnership for the amount they have contributed.⁹

⁶ Commercial Code, art. 283.

⁷ Commercial Code, art. 327.

⁸ Commercial Code, art. 332.

⁹ Commercial Code, art. 331.

Foundations

Foundations are governed by the Private Foundation Law, 1995. A foundation is treated as having separate legal capacity.¹⁰

Once assets are transferred by the founder to the foundation, they cease to belong to the founder and do not become the property of any beneficiary until they are distributed. The foundation manages the assets, in accordance with the purposes specified in the Charter by the founder.

Trusts

Trusts in Panama are governed by Law No 1 of 1984, which generally applies to separate the legal and beneficial ownership of assets between trustees and beneficiaries.

2.2.3.2 Tax Status

For Panama income tax purposes, there is generally no concept of tax transparency.¹¹ All persons (including individuals, partnerships and other entities), are subject to income tax on the same basis as a corporation. Micro, small and medium businesses, including sole proprietorships that are registered as such, are subject to a separate graduated income tax regime (see Section 3.1.3).

Foundations are exempt from tax in Panama providing their assets:

- are located abroad;
- consist of money deposited in banks which does not have a Panamanian source; or
- consist of shares or securities issued by corporations which do not have Panamanian source income, even if the shares or securities are deposited in Panama.¹²

The tax laws of foreign jurisdictions may treat Panamanian partnerships as being transparent for tax purposes. However, this will depend on the foreign entity recognition rules under the tax laws of the foreign jurisdictions.

2.2.4 Permanent Establishments

2.2.4.1 Domestic Law Definition

Individuals or entities domiciled abroad are considered to be carrying out operations in Panama through a permanent establishment (PE) if, either directly or through a proxy, employee or representative, they have in Panama any premises, fixed place of business or center of activity where their activities are carried out, in whole or in part. Such individuals or entities are also considered to carry out operations through a Panamanian PE if they have, among other things, any of the following in Panama:

- a branch, agency, office, factory, store or similar establishment;
- construction, installation or assembly works, and related inspection and supervision activities, for a period or aggregate periods exceeding 183 days within any 12-month period;
- structures, installations, drilling platforms, ships and other substantial equipment for the exploration and exploitation of natural resources, and any related activities, for a period or aggregate periods exceeding 183 days within any 12-month period;
- mining, hydrocarbons, agricultural, forestry and livestock activities, or any other place of extraction of natural resources carried out in Panama;
- facilities operated on a permanent basis by an entrepreneur or a professional, or to purchase goods or acquire services; and
- real estate exploited under a lease or by any title.

In relation to the 183-day rule, the Fiscal Code provides that, if a related company carries out any relevant activities in Panama on behalf of the main company involved, the periods spent on those activities by the related

¹⁰ Private Foundation Law, 1995, art. 11.

¹² Private Foundation Law 1995, art. 11.

¹¹ Fiscal Code, art. 694.

company will be added to those of the main company. There is, however, an exception where activities are carried out concurrently during a period by related companies. In such a case, the concurrent activities can be counted once, as a single period.¹³

PEs and fixed bases located in Panama are subject to income tax on any income attributed to them. Any income obtained by a PE in Panama that is not attributable to the PE is subject to withholding tax.

For the creation of a PE through services performed in Panama (including through an agent or representative), see Section 2.2.4.3.

2.2.4.2 Treaty Definition

Panamanian tax treaties generally follow the OECD model treaty with respect to the definition of a permanent establishment and are interpreted by authorities in accordance with the OECD commentary and guidelines regarding the PE provisions of the model treaty.

2.2.4.3 Creation via Performance of Services

Under article 762-M of the Fiscal Code, a PE is deemed to be created if any type of service, including consulting services, is provided in Panama for a period or aggregate periods exceeding 183 days within any 12-month period, either directly or through employees or other personnel hired for that purpose.

A PE also arises where nondomiciled persons carry out professional or artistic activities, or have other workplaces in Panama where they carry out all or part of their work activity, regardless of whether they carry out such activities themselves, or through employees, agents, representatives or other personnel hired for that purpose.

An agent or representative, other than one acting independently, who acts on behalf of a nondomiciled person, and who holds and habitually exercises in Panama powers to conclude contracts in that person's name, is deemed to give rise to a PE in Panama with respect to those activities. If, however, a nondomiciled person carries out its activities in Panama through a broker, a general commission agent or any other independent agent, the nondomiciled person will not be deemed to have a PE in Panama solely by virtue of those activities, provided that such brokers, general commission agents or other independent agents act within the ordinary framework of their activities.

The fixed base in Panama of an individual who resides abroad, and through which independent personal services are provided, is also considered to be a PE. Similarly, any place where personal services of a scientific, literary, artistic, educational or pedagogical nature, among others, or independent professional services, are provided, constitutes a fixed base.

2.2.4.4 Creation via Customer Downloads or Website Access

Panama does provide express rules on this subject.

2.2.4.5 Creation via Cloud Services

Panama does provide express rules on this subject.

2.3. Taxable Year

2.3.1 Default Taxable Year

The default taxable year is the calendar year. However, companies may use a period that matches their accounting and fiscal year.

2.3.2 Reference Year for Computation of Tax

Taxpayers are subject to tax on income earned during the taxable year. For most companies, tax is collected in quarterly installments during the year, estimated using the prior year's tax liability. Final payment is due three months after the end of the fiscal year (March 31 for calendar year taxpayers). Thus, taxes for the 2022 tax year will be paid on 2022 income through estimated installments during 2022 that are based on the 2021 tax year's liability, with a return and final payment being made early in the 2023 tax year.

¹³ Fiscal Code, art. 762-M.

2.4. Computing Taxable Income

2.4.1 General

Taxable income is based on Panamanian-sourced income. Income is considered to be Panama-sourced if it arises from services or actions carried out in Panama, but also if it benefits individuals or companies located in Panama. For individuals and entities domiciled abroad, taxable income produced in Panama must be derived from the execution of services or actions related to the generation of Panamanian-source income or that affect its preservation, and the payment made for the services or actions must be registered as a deductible expense by the payer. Withholding rules will apply in regards to Panamanian income, including income paid or credited by Panamanian nonprofit entities, government entities and taxpayers with losses.

While dividends received and capital gains realized are taxable, they do not factor into the tax base for purposes of applying the general corporate tax rate—instead they are taxed, generally, at lower rates through a withholding regime.

From Panamanian sourced income, a taxpayer is permitted to deduct operating expenses and certain special allowances. However, as a result of the territorial system, deduction of operating expenses is limited to those expenses that are incurred for the production of Panamanian-sourced income. In addition, deductible costs and expenses may not exceed the percentage of total costs and expenses equal to the percentage of total income that is Panamanian sourced (and therefore subject to tax).

2.4.2 Exempt Income

Under the territorial system, income produced outside of Panama is typically not subject to income tax, but may be subject to dividend tax if distributed as dividend income. Income from operations or services performed outside of Panama is treated as exempt income.

In addition, certain categories of interest income are exempt, including interest on government securities, interest on bank savings and similar deposits, interest derived from securities sold on a stock exchange and issued by public companies registered with the National Securities Commission, and interest from loans made to entities in the agriculture or tourism industries.

2.4.3 Inventory Valuation and Inventory Flow

Inventory is generally valued at cost. The Fiscal Code and regulations allow taxpayers to utilize several methods of recording and accounting for inventory: FIFO, the specific identification method, average cost, and the retailer method. Once selected, an inventory accounting method may not be changed for five years.

2.4.4 Depreciation or Capital Allowances

Depreciation is generally taken on the straight-line basis over the useful life of an asset, however the tax laws and regulations also permit the use of the declining balance method and the sum-of-the-digits method. Taxpayers may select different methods for each asset—they are not required to use the same method for all assets or all assets of a certain class.

Allowable useful lives may vary based on industry, activity, usage conditions, maintenance quality, and potential obsolescence, among other factors. However, the useful life of personal/movable property may not be less than three years and that of real property may not be less than 30 years.

Expenses incurred in business start-up and formation are amortizable over a maximum of five years.

2.4.5 Reserves

Reserves for bad debts are deductible up to 1 percent of the total of credit sales of goods or services rendered in each fiscal year as an annual expense. However, the reserve may never exceed the 10 percent of the total accounts receivable balance at the end of the fiscal year.

2.4.6 Special Allowances

In addition to ordinary operating expenses, taxpayers are allowed a deduction for municipal taxes paid.

Interest deductions are limited to interest paid or accrued on debts that either produce income taxable in Panama or increase the value of domestic assets.

Real estate investment societies (similar to a US REIT) are allowed a special deduction of 90 percent of distributed profits when meeting certain conditions, which include distributing at least 90 percent of free cash generated and withholding 10 percent of any distribution as payment of tax creditable by shareholders.¹⁴

2.4.7 Special Provisions or Limits Applicable to Foreign Companies

Foreign companies are restricted in terms of the businesses in which they may operate. Foreign companies may not engage in retail business (such as supermarkets) or in certain professions that are limited to Panamanian citizens (such as law, medicine, engineering, etc.).

Where a foreign entity located abroad receives payment, the payment is not deductible by the Panamanian payer unless subjected to withholding tax. The effective tax rate on such payments is 12.5 percent of the gross payment (calculated by applying the 25 percent tax rate to a base of 50 percent of the payment amount).

2.5. Intercompany Dividends

Generally, intercompany dividends are subject to withholding at a rate of 10 percent. Where the dividend is paid on bearer shares, the withholding rate is 20 percent. Dividends paid out of foreign-source or export-derived income (including from free trade zones; see Section 2.6.1) are subject to a 5 percent withholding tax. In addition, dividends paid out of income received as dividends from another entity are exempt from tax so long as the payer of the dividend has paid a withholding tax on the received dividend or if it was exempt.

A 10 percent deemed dividend tax (20 percent in the case of bearer shares) is imposed on all loans or advances by a company to its shareholders, regardless of the income source.

Companies operating under the MHQ and EMMA regimes (see Section 2.6.4) are exempt from dividend tax.

See also Section 3.1.4 regarding the complementary tax which effectively operates as an advance payment of dividend tax.

2.6. Special Tax Regimes

2.6.1 Economic Zones

Panama has established certain free trade zones (FTZs) that provide for an exemption from the general income tax (with the exception of certain rental income), as well as other taxes and duties, such as sales taxes, import duties, export taxes and selective consumption taxes derived from royalties on exports and re-export activities. Instead, companies operating in the FTZs are subject to:¹⁵

- an annual notice of operation tax of 1 percent of capital, with a minimum tax of 100 dollars and a maximum tax of 50,000 dollars; and
- a dividend tax of 5 percent.

Panama Pacific Economic Zone (PP regime)

The PP regime was established to attract and promote investments into Panama, and to generate jobs in Panama, including through various tax incentives. Certain conditions apply, including limits on the proportion of expert and administrative foreign staff employed.¹⁶

The PP regime has been amended to comply with the OECD's BEPS Action 5 (Prevention of Harmful Tax Practices).¹⁷ As a result, the following activities are typically not eligible for preferential tax treatment under the regime:

- rendering services to individuals or legal entities located abroad;
- rendering high value-added services protected by intellectual or industrial property rights; and
- re-invoicing goods that do not enter Panamanian territory.

¹⁴ Law No. 8 of March 15, 2010.

¹⁵ Executive Decree No. 62 of April 11, 2017 (regulating Law No. 32 of 2011), art. 17.

¹⁶ Law No. 41 of July 20, 2004.

¹⁷ Law No. 66 of December 13, 2018.

2.6.2 International Finance or Holding Companies

Panama does not have a specialized tax regime applicable to holding or international finance companies.

2.6.3 Research and Development Companies and Activities

Panama does not provide for special incentives for R&D companies or activities.

However, with effect from December 28, 2018, a specific regime applies to the calculation of taxable income derived from qualified intangible assets where the recipient of the income is operating under an existing preferential tax regime. For these purposes, "qualified intangible assets" include patents, utility models, and industrial models or drawings protected by a registry and software protected by copyright, subject to a process of registration and approval. "Qualified expenditures" under the regime include expenses or costs incurred by a qualified taxpayer on R&D in Panama, provided they lead to the creation or improvement of a qualified intangible asset.¹⁸

2.6.4 Other Special Regimes

Multinational Headquartering Regime

A multinational headquartering (MHQ) regime, first established in 2007, was amended with effect from 2019 to comply with the OECD's BEPS Action 5 recommendations on Prevention of Harmful Tax Practices. The amended regime is subject to economic substance requirements.¹⁹

Before the 2019 amendments, a foreign company establishing global or regional headquarters within Panama was eligible for a full income tax exemption on all income derived from services provided to its foreign parent or affiliated entities. Since 2019 (subject to certain grandfathering rules) such income has been subject to an income tax rate of 5 percent.

Where a payment for services is made to an MHQ company by a Panamanian taxpayer that benefited from those services, the Panamanian taxpayer must withhold tax at the rate of 5 percent if (i) such services related to the generation or preservation of the taxpayer's Panama-source income and (ii) the taxpayer treated the payment as a deductible expense.

If services (including the use of IP rights, or a loan or other financing facility) are provided for the benefit of an MHQ company by a non-Panamanian entity, the MHQ company must withhold tax at the rate of 5 percent on 50 percent of the payment for those services (i.e., an effective rate of 2.5 percent), provided (i) the services relate to the generation or preservation of Panama-source income and (ii) the payment has been treated as deductible by the MHQ company. If the MHQ company is in a loss position, the withholding applies to all Panama-source income paid by it to a nonresident.

Licensed MHQ companies are exempt from the dividend tax (for which, see Section 2.5), complementary tax (for which, see Section 3.1.4) and branch tax (for which, see Section 2.1.2 and Section 9.4), regardless of the source of the income (local, foreign or exempt). They are also exempt from the annual notice of operation tax on capital (for which, see Section 2.6.1).

Tourism

Certain tax incentives are available to qualifying companies engaged in the tourism industry.²⁰

Call Centers

Income earned by natural or legal persons from the operation of call-center services under a concession granted by the National Authority of Public Services (*Autoridad Nacional de los Servicios Públicos – ANSP*) is exempt from income tax if the operator satisfies the following requirements for the fiscal period in question:

- it has at least five full-time employees;

¹⁸ Law No. 69 of December 26, 2018.

¹⁹ Law No. 41 of August 24, 2007, as amended by Law No. 45 of 2012, Law No. 57 of October 24, 2018 and Resolution No. 15 of 2018.

²⁰ Law No. 80 of November 8, 2012.

- at least 70 percent of its costs relate to the call-center activities; and
- it submits an annual report giving prescribed details (activities, costs, employees, financial statements) and any other information required by the ANSP.²¹

Special Regime for Multinational Companies Providing Manufacturing Services (EMMA)

The EMMA regime is available to multinational companies, whether foreign or Panamanian, that provide specified manufacturing services from Panama solely to other entities within their multinational business group.²²

The specified services are as follows:

- services related to the manufacturing of products, machinery and equipment;
- assembly services for products, machinery and equipment;
- maintenance and repair services for products, machinery and equipment;
- services related to the re-manufacturing of products, machinery and equipment, i.e., the restoration or modification of a product that has already been manufactured and used previously;
- services related to the conditioning of products, e.g., coding, batching and labelling;
- product development services, research or innovation of existing products or processes;
- analysis, laboratory, testing or other services in connection with the provision of services related to manufacturing;
- logistics services, such as storage, deployment and distribution centers for components and parts required for the provision of services related to manufacturing; and
- any other similar service, previously approved by the Cabinet Council in a reasoned resolution, provided it complies with the provisions of Law No. 159.²³

The EMMA regime provides various tax benefits, including:

- a reduced corporate income tax rate of 5 percent on taxable income derived from the qualifying services by companies subject to the EMMA regime (hereafter "EMMA companies");
- subject to at least 2 percent of net taxable income being paid as tax in Panama, a tax credit (which cannot be carried over to following fiscal periods) for any income tax or similar tax actually paid abroad by EMMA companies on income generated in Panama from the provision of services to nonresidents, as well as amounts withheld as income tax by Panamanian taxpayers;
- exemption for EMMA companies from dividend tax, complementary tax and branch tax, regardless of the source of the income (local, foreign or exempt);
- a reduced 2 percent tax rate on capital gains on the transfer of shares or securities issued by EMMA companies;
- a reduced tax rate of 1 percent on the transfer price of such shares or securities, withheld by the buyer as an advance payment of the seller's tax on such gains (the seller can elect this withholding to be the final tax on the gains); and
- exemption for EMMA companies from import duties on items used, or required, for the provision of services related to manufacturing.²⁴

²¹ Law No. 52 of October 17, 2018.

²² Law No. 159 of August 31, 2020, arts. 1-3, 6, 59.

²³ Law No. 159 of August 31, 2020, arts. 3, 4.

²⁴ Law No. 159 of August 31, 2020, arts. 20, 22, 25, 29.

Where a payment for services is made to an EMMA company by a Panamanian taxpayer that benefited from those services, the Panamanian taxpayer must withhold tax at the rate of 5 percent if (i) such services related to the generation or preservation of the taxpayer's Panama-source income and (ii) the taxpayer treated the payment as a deductible expense.²⁵

If services (including the use of IP rights, or a loan or other financing facility) are provided for the benefit of an EMMA company by a non-Panamanian entity, the EMMA company must withhold tax at the rate of 5 percent on 50 percent of the payment for those services (i.e., an effective rate of 2.5 percent), provided (i) the services relate to the generation or preservation of Panama-source income and (ii) the payment has been treated as deductible by the EMMA company. If the EMMA company is in a loss position, the withholding applies to all Panama-source income paid by it to a nonresident.²⁶

An extendable two-year temporary personnel visa is available to foreign individuals who provide services, at an operational or training level, to EMMA companies. The salaries and other remuneration (including salary in kind) of individuals holding such a visa are exempt from personal income tax, social security contributions and education insurance contributions, to the extent that the remuneration is paid, assumed and recognized as a personnel expense in the accounts of EMMA companies.²⁷ Those exemptions are also available to foreign personnel holding a permanent personnel visa, i.e., a five-year visa, extendable for further terms of five years for an unlimited number of times.²⁸ However, they are not available to foreign personnel who exercise an option to acquire permanent residence, a right that first becomes available five years after the approval of the initial visa.²⁹

The transfer pricing rules (see Section 7.1) apply to related-party transactions that are subject to the EMMA regime.³⁰

EMMA companies enjoy statutory guarantees of legal stability in respect of their investments.³¹

Companies wishing to avail themselves of the EMMA regime must apply to the prescribed authority for an EMMA license.³²

Special Regime for Limited Liability Entrepreneurship Companies

With effect from December 2, 2021, the limited liability entrepreneurship company (*sociedad de emprendimiento de responsabilidad limitada*, or SERL) regime aims to create innovative products, services and processes, or provide value creation or social benefits.³³ A SERL can be established by two to five natural persons of any nationality who are domiciled in Panama. These persons cannot be members of other SERLs, but they are permitted to be members of other types of business entities. Legal entities cannot be members of a SERL.³⁴

The required minimum share capital of a SERL is 500 dollars, and operations must commence within six months of incorporation.³⁵

Only micro and small businesses can qualify to be SERLs. For these purposes, a micro business is defined as having gross annual income of up to 150,000 dollars, and a small business is defined as having gross annual income of up to 1 million dollars. If the gross annual income of a small business exceeds 1 million dollars, it is required to be transformed into another form of business entity within six months from the end of the regular period for presenting the tax return for the respective fiscal year.³⁶

SERLs can benefit from the following tax incentives:³⁷

- corporate income tax exemption for the first two years of operation;
- exemption from registration fees; and

²⁵ Law No. 159 of August 31, 2020, art. 27.

²⁶ Law No. 159 of August 31, 2020, art. 27.

²⁷ Law No. 159 of August 31, 2020, art. 31.

²⁸ Law No. 159 of August 31, 2020, arts. 34, 35.

²⁹ Law No. 159 of August 31, 2020, art. 36.

³⁰ Law No. 159 of August 31, 2020, art. 21.

³¹ Law No. 159 of August 31, 2020, art. 55.

³² Law No. 159 of August 31, 2020, art. 12.

³³ Law No. 186 of December 2, 2020.

³⁴ Law No. 186 of December 2, 2020, art. 5.

³⁵ Law No. 186 of December 2, 2020, arts. 13, 47.

³⁶ Law No. 186 of December 2, 2020, art. 24.

³⁷ Law No. 186 of December 2, 2020, arts. 34-40.

- donations of up to 10,000 dollars per person can be made to the SERL, with the donation qualifying as a deductible expense on the part of the donor (who is not required to be a member of the SERL).

The Cabinet Council may also reduce import duties by up to 50 percent for products and raw materials acquired by the SERL to create innovative products, services, and processes.

Waste recycling and biodegradable materials

With effect from the 2022 fiscal year, various tax benefits are available, on application, to legal entities operating industrial recycling plants and to legal and natural persons in the plastics industry that have been required by law to replace their plastic products with biodegradable materials not containing plastic. The benefits run for five years from the date on which the applicant is notified that its application has been approved.³⁸

2.7. Double Taxation Protection

2.7.1 Mechanics

As Panama maintains a territorial tax system, income produced abroad is not subject to Panamanian income taxes.

As a result, the Fiscal Code does not provide for any foreign tax credit or other mechanism to unilaterally protect against double taxation.

2.7.2 Treaty or Statutory Priority

Where, in a particular case, a treaty rate is higher than the domestic rate, the domestic rate is applicable.

For treaty information, including the number of agreements signed or in force, original treaty texts, translations, consolidations and any modifications made by the Multilateral Instrument, if applicable, see the International Tax Treaties Collection.

2.7.3 Source of Interpretation

Panama follows the OECD model tax treaty commentary and guidelines in interpreting treaty provisions, although the commentary is not binding.

2.8. Returns and Filing Dates

2.8.1 Filing Deadline

Returns are due within three months of the end of the fiscal year (March 31 for calendar year taxpayers).

2.8.2 Filing Method

Corporations are required to file tax returns electronically.

2.8.3 Extensions

An extension of up to one month is available.

2.8.4 Penalties

For late filing of returns, article 753 of the Fiscal Code provides for the imposition of a fine ranging from 100 dollars to 1,000 dollars. However, a transitory paragraph added to article 710 of the Code provides, with effect from November 15, 2022, for a fine equivalent to 0.3 percent of the taxable income declared for the relevant period.³⁹

2.9. Payment Mechanics

2.9.1 Internal Withholding on Resident Companies

Certain payments to resident companies may be subject to withholding. In addition, taxes on dividends and capital gains are primarily collected through withholding for resident as well as nonresident companies.

³⁸ Law No. 223 of June 8, 2021.

³⁹ The transitory paragraph was added to Fiscal Code, art. 710, by Law No. 337 of November 14, 2022, arts. 29, 39.

2.9.2 Schedule for Tax Payments or Deposits

Estimated tax payments are made at the end of the sixth, ninth, and twelfth month of the fiscal year (June 30, September 30, and December 31 for calendar year taxpayers). Estimated payments are calculated as one-fourth of the tax liability for the previous year. The final payment of tax must be remitted when the return is due (March 31 of the following year for a calendar year taxpayer).

2.9.3 Electronic Payments

Taxes are payable at offices of the Tax Authority, at branches of the National Bank and certain banks affiliated to the Panamanian Tax Authorities. This is done to make it easier for taxpayers to pay their taxes. Panamanian law does not require that taxpayers maintain a local bank account.

Tax can be paid by the following means:

- cash;
- check;
- debit on current or savings accounts;
- debit or credit cards;
- any other instrument legally authorized for the payment of taxes;
- exceptionally, payment in kind, duly endorsed by the Comptroller General of the Republic of Panama (the head of the state agency responsible for the management of public funds).⁴⁰

2.9.4 Interest and Penalties

Taxpayers that fail to make estimated or final payments of tax will become subject to:

- a penalty of 10 percent of the amount of tax owed, plus
- default interest of 2 percentage points per month or part month above the market reference rate, as notified annually by the Superintendency of Banks and based on the rate set during the previous six months by commercial banks.⁴¹

2.10. Statute of Limitations

The statute of limitations on the collection of tax is seven years (five years effective January 1, 2023) from the day following that on which payment is required by law.⁴² On an audit, however, the limitation period for raising an assessment is three years from the date of filing the return.⁴³

3. Corporate Tax Rates

3.1. National Taxes

3.1.1 Corporate Tax Rates

Current rate: 25 percent to 30 percent.

All private corporations are subject to a flat rate of 25 percent. Entities in which the government owns at least 40 percent of the stock are subject to tax at a 30 percent rate, with those engaged in telecommunications subject to a 25 percent tax rate.

3.1.2 Alternative Tax Regime

Companies with taxable revenue of at least 1.5 million dollars are subject to an alternative minimum tax regime (*Calculo Alternativo del Impuesto sobre la Renta* or CAIR). Under the CAIR, minimum tax is calculated at the standard 25 percent tax rate applied to 4.67 percent of total taxable income (equaling 1.17 percent of gross income). Total taxable income is total revenue less any exempt revenue, including foreign source income. A

⁴⁰ Law No. 76 of February 13, 2019, arts. 68, 392.

⁴¹ Fiscal Code, art. 1072-A.

⁴² Law No. 76 of February 13, 2019, arts. 88, 392.

⁴³ Fiscal Code, art. 720.

taxpayer is obligated to pay the CAIR instead of ordinary corporate income tax where the ordinary tax on net taxable income is less than the amount calculated under the CAIR.

However, a taxpayer may be granted a waiver from the CAIR if payment of the CAIR would result in the company sustaining a loss for the year, or if the CAIR results in an effective tax rate greater than 25 percent. The Tax Authority has discretion to grant an exemption from the CAIR for the period requested, and three subsequent years.

Taxpayers must request the waiver from the CAIR within five business days (previously the same day) after submitting their corporate income tax return.

3.1.3 Special Reduced Rates or Regimes

Special reduced graduated income tax rates apply to micro, small and medium businesses (Spanish acronym, MIPYMEs). For these purposes, an MIPYME must meet the following conditions:

- it is duly registered with the appropriate authority;
- its gross annual income does not exceed 500,000 dollars; and
- it is not owned or controlled by any legal entity (i.e., ownership and control must be by natural persons).

The tax rates on net taxable income for a legal entity registered as an MIPYME are as follows:⁴⁴

- up to 11,000 dollars – 7.5 percent;
- 11,001 dollars to 36,000 dollars – 10 percent;
- 36,000.01 dollars to 90,000 dollars – 12.5 percent;
- 90,000.01 dollars to 150,000 dollars – 15 percent;
- 150,000.01 dollars to 350,000 dollars – 20 percent; and
- 350,000.01 dollars to 500,000 dollars – 22.5 percent.

For an individual operating as a sole proprietorship that is registered as an MIPYME, the tax rates on net taxable income are as follows:⁴⁵

- up to 11,000 dollars – 0 percent;
- 11,000.01 dollars to 36,000 dollars – 7.5 percent;
- 36,000.01 dollars to 90,000 dollars – 10 percent;
- 90,000.01 dollars to 150,000 dollars – 12.5 percent;
- 150,000.01 dollars to 350,000 dollars – 17.5 percent; and
- 350,000.01 dollars to 500,000 dollars – 22.5 percent.

See also Section 2.6.4 for the SERL incentive regime for small businesses.

Planning Point: The stated aims of the progressive tax regime include the formalization of the MIPYME regime generally for both legal entities and natural persons, including registration with the Micro, Small and Medium Enterprise Authority (Spanish acronym, AMPYME) and gaining access to other tangible benefits such as financing, guarantees, venture capital, and adequate tax management by the DGI. The formal requirements for taxpayers wishing to benefit from this regime, and the procedure for verifying income, are determined by the Executive Branch through the Ministry of the Economy and Finance.

⁴⁴ Fiscal Code, art. 699-A, as amended by Law No. 189 of December 17, 2020, art. 1.

⁴⁵ Fiscal Code, art. 700-A, as amended by Law No. 189 of December 17, 2020, art. 2.

3.1.4 Special Additional Taxes or Levies

Corporations that do not distribute at least 40 percent of their after-tax profits for a fiscal period as dividends are subject to a retained profits tax known as the complementary tax. This tax is charged at 10 percent of the difference between 40 percent of after-tax profits and the total of any dividends actually distributed during the year. In the case of dividends that are subject to the 5 percent dividend tax rate (for which, see Section 2.5 and Section 5.1), the tax applies if the corporation distributes less than 20 percent of the after-tax profits for the relevant fiscal period as dividends. In such a case, the tax is chargeable on the difference between 20 percent of after-tax profits and the total of any dividends actually distributed during the year.⁴⁶

If the corporation subsequently makes dividend or participation fee distributions from retained profits that have been subject to the complementary tax, it can credit the complementary tax paid against any dividend withholding tax due on those distributions.⁴⁷ In other words, the complementary tax effectively operates as an advance payment of dividend tax.

Companies operating under the MHQ or EMMA regimes (for which, see Section 2.6.4) are exempt from the complementary tax.

In addition, Panama levies a Banking Institution Tax (see Section 10.2).

3.2. State, Cantonal, Provincial or Other Local Taxes

3.2.1 Main Rates

Municipal taxes in Panama are levied at the sole discretion of the municipal authorities and are based on factors such as the business size and the industry or activity being engaged in.⁴⁸

3.2.2 Reduced Rates

Given the local autonomy in setting municipal rates, there is no general rule as to the availability of reduced rates that is applicable to all municipalities.

3.2.3 Income Tax Base

Panamanian municipalities levy taxes on gross income. However, the tax base remains limited to Panama-source income.

3.2.4 Income Tax Deductions

As municipalities levy on gross income, no deductions are permitted.

3.2.5 Incentives

Given the discretion vested in municipal authorities regarding local taxation, it is not clear what, if any, incentives are offered in various municipalities.

3.2.6 Non-Income Taxes in States

Local governments do not levy any non-income taxes in Panama.

3.3. Taxes Imposed as a Penalty

Panama does not levy any taxes that are in the nature of penalties. While a withholding tax is imposed on companies that do not distribute at least 40 percent of their after-tax profit (see Section 2.2.4), the tax is creditable against future dividend taxes at the time of distribution.

⁴⁶ Fiscal Code, art. 733(g), (i).

⁴⁷ Executive Decree No. 170 of October 27, 1993, art. 112, as amended by Executive Decree No. 98 of September 27, 2010, art. 62.

⁴⁸ Agreement No. 40 of April 19, 2011.

4. Corporate Tax Capital Gains, Losses, Group Treatment

4.1. Taxation of Corporate Capital Gains

As a general rule, capital gains are taxed separately from income derived from business activities.⁴⁹ Subject to certain withholding tax requirements described further below, a tax rate of 10 percent applies to capital gains realized from:

- sale of real estate not in the ordinary course of business (but see further below);
- disposal of shares, bonds, participation fees and other securities; and
- sale of movable property.

Special rules for real estate

For sales of real estate not in the ordinary course of business, the taxpayer must withhold tax as an advance payment equivalent to 3 percent of either the total value of the sale price or the cadastral value, whichever is higher. The taxpayer can opt for the tax withheld to be treated as the final tax payment. If, however, the amount of tax paid on withholding is higher than the amount that would be paid when applying the general tax rate of 10 percent on the realized capital gain, the taxpayer can claim a tax credit for the excess amount of tax paid.

Exceptionally, a final tax of 3 percent applies to capital gains from sales of agricultural and residential real estate in rural areas with a cadastral value of up to 10,000 dollars.

Capital gains realized from the sale of real estate in the ordinary course of a taxpayer's business (e.g., a real estate dealer or developer) are generally subject to the corporate income tax rate (see Section 3.1). However, in the case of the first sale of new homes and commercial premises, the following income tax rates apply to either the total value of the sale price or the cadastral value, whichever is higher:

- new homes with a value
 - of up to 35,000 dollars – 0.5 percent;
 - from 35,001 dollars to 80,000 dollars – 1.5 percent; and
 - exceeding 80,000 dollars – 2.5 percent; and
- commercial premises – 4.5 percent.

Special rules for shares, etc.

The buyer of shares, bonds, participation fees and other securities must withhold 5 percent of the total sale value as an advance tax payment on the capital gain. The seller can opt for the tax withheld to be treated as the final tax payment. If, however, the amount of tax paid on withholding is higher than the amount that would be paid when applying the general tax rate of 10 percent on the realized capital gain, the seller can claim a tax credit for the excess amount of tax paid.

For reduced rates applicable to the shares of EMMA regime companies, see Section 2.6.4.

4.2. Definition of Corporate Capital Gains

The Fiscal Code does not provide a definition of "capital gains". Instead, it provides for the separate taxation of "profits" derived from the sale or disposal of real estate; shares, bonds, participation fees and other securities; and movable property.⁵⁰

There is no distinction based on holding period.

⁴⁹ Fiscal Code, art. 701(a), (e).

⁵⁰ Fiscal Code, arts. 696(e), 701(a), (e).

4.3. Computation

Subject to the option to pay capital gains tax on the cadastral value of real estate or the full sale value of shares, etc. (see Section 4.1), the tax base for applying the 10 percent capital gains tax rate is the difference between (1) the actual sale value and (2) the sum of the original purchase cost and any necessary expenses incurred to carry out the sales transaction.

4.4. Corporate Combinations and Divisions

4.4.1 Mergers

In Panama, mergers and acquisitions are generally structured as either stock-for-stock transactions, stock-for-cash transactions or a combination of both. Acquisitions can also be structured as a straight purchase of shares or a purchase of assets.

When two companies merge under the corporate merger statute, neither company is taxed on gain from transferring its properties to the surviving company. Furthermore, in cases where shares are registered with the Superintendency of the Securities Market, shareholders are not taxed on gain from exchanging their shares for shares in the merged company or from the conversion of their shares to shares in the merged company, provided that no cash is paid as consideration (except, to avoid splitting shares, for a payment of up to 1 percent of the value of the shares received) and certain accounting requirements are followed. Neither the merged companies nor the shareholders will be treated as having made a taxable disposition of assets or shares. Both take carryover bases in the assets or shares they acquire as a result of the merger.

Stock-for-cash mergers are typically not tax-free transactions. This rule does not apply where shareholders of an extinguished entity receive de minimis payments of cash, goods or securities.

4.4.2 Transfers of Corporate Property

For the treatment of gains on mergers and divisions, see Section 4.4.1 and Section 4.4.4 respectively.

Any real estate transferred as part of the merger or acquisition will also incur real estate transfer tax (see Section 9.3.1).

4.4.3 Share Transfers

For the treatment of gains on mergers and divisions, see Section 4.4.1 and Section 4.4.4 respectively.

4.4.4 Divisions or Separations

In the case of a split-off or similar de-merger of companies, the transfer of assets to a new company pursuant to a split-off is not considered to be a disposal of the assets for tax purposes. As a result, no gain is recognized on the transfer and the new company inherits the tax attributes associated with the transferred assets.

In order for a split-off or de-merger to qualify for this tax-deferred treatment, the new company or companies created by the split-off must either be owned by the original company or have an exact identity of shareholders as the old company.

4.5. Position of Losses From Business Operations

4.5.1 Definition

Operating losses consist only of the amount by which operating expenses incurred in the production of Panama-source income exceed such Panama-source income. Capital losses are not included in operating losses, as noted above in Section 4.3. As foreign income and loss is not included in the tax base under Panama's territorial system, foreign losses cannot offset Panama-source income.

4.5.2 Treatment

Operating losses cannot be carried back, but can be carried forward. A company sustaining a loss may carry forward that loss and deduct up to 20 percent of the loss in each of the next five years. However, the deduction may not exceed 50 percent of net taxable income of any year. Any losses not used within a five-year period expire and may not be subsequently used.⁵¹

⁵¹ Fiscal Code, art. 698-A.

4.5.3 Losses After Change in Ownership

A change in ownership alone will not cause a corporation to lose accumulated losses. However, in the event of a merger, the surviving company may not use prior year losses of the merged company. Only losses incurred by the merged company in the year of the merger will be available to the surviving company.

4.6. Group Treatment

4.6.1 General Rule

There is no group or consolidated regime available in Panama.

4.6.2 Definition of Group

There is no group or consolidated regime available in Panama.

4.6.3 Special Aspects

There is no group or consolidated regime available in Panama.

5. Corporate Withholding Taxes on Nonresident Corporations

5.1. Dividends

Dividends paid to a nonresident are subject to the same tax and withholding regime as a domestic company. A company paying dividends is required to withhold 10 percent of the amount paid. When the dividend is paid on bearer shares the tax is 20 percent, and when paid from foreign-source or export-derived income it is 5 percent. Dividends paid out of income received as dividends from a payer that has withheld tax are exempt from any withholding tax. A 5 percent rate applies to dividends paid by companies operating in the Colon Free Zone, regardless of the dividends' source.

The exemption of certain dividends paid to a nonresident from dividend withholding tax will only apply if the nonresident has a formal opinion from an independent tax expert in the nonresident's jurisdiction showing that the nonresident recipient cannot claim a tax credit in the nonresident's jurisdiction.

See also Section 3.1.4 regarding the complementary tax which operates as an advance payment of dividend tax.

5.2. Interest

Interest paid to foreign entities is subject to withholding at an effective rate of 12.5 percent of the gross amount paid (i.e., the corporate rate of 25 percent applied to 50 percent of the payment). However, if the nonresident company registers with authorities in Panama, no withholding is required.

There are exemptions from withholding tax for certain interest payments to a nonresident, but they apply only if the nonresident has a formal opinion from an independent tax expert in the nonresident's jurisdiction showing that the nonresident recipient cannot claim a tax credit in the nonresident's jurisdiction.

5.3. Royalties

Royalties and commissions paid to a foreign entity are subject to an effective withholding tax rate of 12.5 percent of the gross payment (i.e., the corporate rate of 25 percent applied to 50 percent of the payment) in order to be deductible by the domestic payer. If a payer chooses not to deduct the payment, then no withholding is required.

There are exemptions from withholding tax for certain royalties paid to a nonresident, but they apply only if the nonresident has a formal opinion from an independent tax expert in the nonresident's jurisdiction showing that the nonresident recipient cannot claim a tax credit in the nonresident's jurisdiction.

There is an exemption for royalties paid by companies operating in the Colon Free Zone.

5.4. Services

Services income (fees and commissions) are treated the same as royalties in that they are subject to an effective withholding tax rate of 12.5 percent of the gross payment (i.e., the corporate rate of 25 percent applied to 50 percent of the payment) unless the payer chooses not to claim a deduction for the expense, in which case no withholding is required. This treatment applies to all payments for services, including general business and professional services.

There are exemptions from withholding tax for certain service fees paid to a nonresident, but they apply only if the nonresident has a formal opinion from an independent tax expert in the nonresident's jurisdiction showing that the nonresident recipient cannot claim a tax credit in the nonresident's jurisdiction.

5.5. Other Withholding Taxes

Capital gains derived by nonresidents on the sale of real property or securities are subject to withholding on the same terms as residents, as discussed in Section 4.1.

Where a foreign entity located abroad receives payment, the payment is not deductible by the Panamanian payer unless subjected to withholding tax, as discussed in Section 2.4.7.

5.6. Special Tax Havens Rates

Given the nature of the Panamanian tax system, there are no special rates provided for payments to any particular jurisdiction and the Panamanian authorities do not designate "tax havens."

6. Personal Taxes

6.1. Domicile and Residency Requirements

An individual is considered to be a tax resident if he remains or resides in Panama for more than 183 continuous or non-continuous days in a calendar year or in the immediately preceding year. He will also be considered tax resident if he establishes his permanent residence in Panama.

6.2. Income Tax Base

6.2.1 Tax Base for Residents

Because Panama is a territorial system, residents are taxed only on Panama-source income.

6.2.2 Tax Base for Nonresidents

Because Panama is a territorial system, nonresidents are also taxed only on Panama-source income.

6.2.3 Personal Income Subject to Income Tax

General – Income subject to tax includes all income from activities in Panama regardless of the place of receipt, and is taxed at progressive rates. Income of an individual may be classified as: employment income; professional income; business income; and investment income (i.e., profits, dividends, company participations, and any other form of profit distribution). Hence, deferred payments relating to services or activities in Panama are subject to Panamanian tax. For individuals, capital gains on real property are included in income and taxed at the graduated rates (although the collection of tax on gains is supplemented by withholdings), however, capital losses cannot offset employment income when calculating net taxable income.

Excluded income – Certain items of income are exempt, notably interest and gains on government-issued securities, interest earned on bank savings accounts and certificates of deposit, and gains on securities sold on a stock exchange and issued by an entity registered with the National Securities Commission. Dividends are also excluded from income as they are subject to a final withholding tax at the source.

Treatment of benefits – Income also includes most "fringe benefits" that an employer might provide. The value of housing and car allowances, school insurance payments, retirement benefits, and any other benefit-in-kind are included in the employee's income. An employee who uses his own vehicle to carry out activities generating taxable income may deduct all his vehicle's maintenance and operational expenses. However, the following benefits are not subject to tax as employee income: stock options granted by the employer; contributions made by the employer to the employee pension funds; tuition fees and scholarships paid by the employer to the employee or their family members.

Service income – Income from services performed by individuals within Panama is considered Panamanian-source for income tax purposes.

Foreign personnel of companies subject to the EMMA regime – for a tax exemption on the salaries of such personnel, see Section 2.6.4.

6.2.4 Deductions and Allowances

A taxpayer who files a return jointly with a spouse is entitled to a deduction of 800 dollars.

Interest on educational loans and medical expenses are also deductible.

Educational expenses (including fees, uniforms and transport) relating to school and university may be deducted by parents in relation to their dependents or by independent students. The deduction is capped at 3,600 dollars per student per year, with the exception of dependent disabled students who are able to attend regular classroom education, whose parents may deduct 100 percent of those expenses.⁵²

Capped deductions are available for mortgage interest (maximum of 15,000 dollars per year).

6.3. Main Rates and Bands

6.3.1 Individual Tax Rates

Individuals are subject to the following tax rates on net income:

- up to 11,000 dollars – 0 percent;
- from 11,001 dollars to 50,000 dollars – 15 percent; and
- over 50,000 dollars – 25 percent.

If a taxpayer receives a representation allowance (e.g., for expenses incurred to represent an employer when meeting customers and suppliers, such as entertainment), the allowance is subject to lower tax rates as follows:

- allowance amounts up to 25,000 dollars per year – 10 percent; and
- allowance amounts over 25,000 dollars per year – 15 percent.

Sole proprietorships that are registered as MIPYMEs are subject to a separate special graduated income tax rates regime (see Section 3.1.3).

6.3.2 Individual Returns, Filing Dates, and Payment

Individuals are required to file a tax return to report final annual tax liability by March 15 of the following year. However, an individual whose source of income is a single job paying a salary is not required to file a return. An extension of one month (to April 15) is available. Taxpayers may file jointly with a spouse, but are not required to do so. Electronic filing is required.

Under article 753 of the Fiscal Code, taxpayers who are required to file, but fail to do so or file late, are subject to a penalty that ranges from 100 dollars to 1,000 dollars. However, a transitory paragraph added to article 710 of the Code provides, with effect from November 15, 2022, for a fine equivalent to 0.1 percent of the taxable income from any source (except salary) declared for the relevant period.⁵³

Payment of tax is made in advance during the taxable (calendar) year. For those earning employment income, tax is withheld from salary and paid over to the authorities as a credit to the taxpayer's account. Taxpayers with more than one source of income or with non-employment income are required to make quarterly estimated payments based on the prior year's tax liability. Payments are due on June 30, September 30, and December 31 of the tax year. Final payment is due no later than March 31 of the following year. Taxpayers who fail to pay or are late in paying are subject to a penalty of 10 percent of the tax due and are subject to interest charges on the outstanding amount at a rate determined by the tax authorities.

For a tax payment discount available to taxpayers with gross income not exceeding 2.5 million dollars, see Section 2.9.2.

6.4. Dividends

6.4.1 Domestic Corporations

Individuals receiving dividends (whether in cash or in stock) from a domestic corporation are subject to the same tax and withholding rules as are corporate recipients of dividends. Such dividends are subject to a 10 percent tax,

⁵² Law No. 37 of June 5, 2018, arts. 1 (amending the Fiscal Code, art. 709), 2.

⁵³ The transitory paragraph was added to Fiscal Code, art. 710, by Law No. 337 of November 14, 2022, arts. 29, 39.

collected via withholding by the payer company. The withholding tax is 20 percent when the dividend is paid on bearer shares. Some dividends, however, are exempt (e.g., dividends received from another corporation that withholds the 10 percent tax, dividends paid from non-Panamanian source income, and dividends paid from export profits of CFZ companies).

6.4.2 Foreign Corporations

Dividends received from a foreign corporation are not considered Panama-source income. Under the territorial tax system of Panama, only Panama-source income is taxed domestically. As a result, foreign corporate dividends are excluded from income.

6.5. Interest

6.5.1 Domestic Borrowers

Interest received on government securities, bank savings accounts and certificates of deposit, and interest from securities purchased on a stock exchange and issued by a company registered with the National Securities Commission are exempt from tax. To the extent interest is not derived from an exempt source, it is not subject to withholding tax, but is includible in the taxpayer's return as income subject to ordinary tax.

6.5.2 Foreign Borrowers

As with dividends, interest received from a foreign borrower is not considered Panama-source income and therefore is not included in the income tax base as long as loan funds were used abroad.

6.6. Social Security/National Insurance Payments

6.6.1 Employer Tax or Contribution

Required employer contributions are as follows:

- social security – 12.25 percent; and
- educational insurance – 1.5 percent.

Employers must also pay workers' compensation insurance, which covers work-related personal injuries, occupational diseases, and death. Rates vary depending on the nature of business activities and other risk factors.

6.6.2 Employee Tax or Contribution

Required employee contributions are as follows:

- social security – 9.75 percent; and
- educational insurance – 1.25 percent (for nonresidents – 2.5 percent).

6.6.3 Employee Tax Collection Mechanism

Social security payments are mandatory and are collected monthly via withholding by the employer. Employees are not eligible to pay directly, but independent contractors and nonresidents are required to pay their portion of the tax directly.

6.7. Royalties and Rents

6.7.1 Domestic Licensors

Residents are taxed on the receipt of Panama-source rents and royalties, but are not subject to tax on such income derived from foreign uses of property or intangibles. Rents and royalties are included in an individual's gross income and taxes at the standard graduated rates. No withholding taxes are due on such payments to Panamanian residents.

6.7.2 Foreign Licensors

Foreign individuals will be taxable on rents and royalties relating to Panamanian property or the domestic use of intangibles. Royalties are subject to the 12.5 percent withholding tax, subject to the decision of the payer as to whether to claim a deduction. The withholding rate is considered a final tax.

7. Transfer Pricing Policies

7.1. Application

Panama has transfer pricing rules for transactions between a domestic entity and a foreign related party.

Related parties are deemed to be one or more persons participating directly or indirectly in the management, control, or capital of another person; or one person or group of persons (individual or legal entity) participating directly or indirectly in the management, control, or capital of such persons. In addition, related parties are:

- a permanent establishment and its home office;
- a permanent establishment and other permanent establishments of the same home office; and
- a permanent establishment and the other related parties of the home office.

Panama requires that related party transactions use an arm's-length price (ALP).

7.2. Permissible Pricing Methods

Panama allows taxpayers to utilize any method allowed under OECD guidelines regarding the setting of an arm's-length price. Under Panamanian law there are five methods for evaluating transactions between related parties:

- (1) the comparable uncontrolled price method;
- (2) the cost-plus method;
- (3) the resale price method;
- (4) the profit split method; and
- (5) the transactional net margin method.

Panamanian transfer pricing rules apply the most appropriate method principle. Priority is given to the transactional methods, but if those methods cannot be used the profit-based methods are permissible.

7.3. Penalties for Improper Pricing

There is no separate penalty regime for improper pricing found as a result of a DGI transfer pricing audit. For penalties on late paid and unpaid taxes generally, see Section 2.9.4.

7.4. Advance Rulings or Pricing Agreements

Advance rulings or pricing agreements are not available in Panama. The tax authorities will issue guidance, but that guidance is non-binding on both the taxpayer and the tax authority.

However, with effect from January 1, 2023, the new Tax Procedure Code (see Section 1.1) introduces a tax ruling procedure under which any person (legal or natural) may consult the Tax Administration about the application of tax legislation to a particular situation. Any resulting ruling is binding on the tax administration to the extent that it favors the interests of the taxpayer concerned.⁵⁴

7.5. Documentation

All taxpayers subject to transfer pricing rules are required to prepare documentation in Spanish. The taxpayer must prepare and file a disclosure report on all related-party transactions, their nature and amounts, and all information necessary to determine the price negotiated by the parties. The report is due no later than six months after the end of the taxpayer's fiscal year. Failure to meet these requirements can result in a penalty equivalent to 1 percent of the total amount of operations with related parties, up to a maximum penalty of 1 million dollars.

A multinational enterprise group will also be required to provide:

- an overview of the group's organization and legal structure, including the identification of the entities performing transactions with the taxpayer; and

⁵⁴ Law No. 76 of February 13, 2019, arts. 145-149, 392, as amended by Law No. 208 of April 6, 2021, art 6, and by Law No. 257 of November 26, 2021, art 5.

- a description of the group's transfer pricing policy.

If economically relevant to the facts and circumstances of transactions between related parties, the taxpayer may be requested to provide the following documentation:

- a description of the group's profit generators;
- a general description of the value chain of the group's five main products or services, including a description of the geographic markets in which the group operates;
- the group's financial statements;
- a list and brief description of intragroup service agreements relevant to transactions involving the taxpayer, including the transfer pricing policy for cost attribution;
- a list of the group's intangibles that relate to transactions involving the taxpayer, identifying the group entity that owns the intangible;
- a general description of the group's transfer pricing policy on intragroup financing and/or leverage, if members of the group are incident to transactions involving the taxpayer;
- a list of the group members' advance pricing agreements, if relating to transactions involving the taxpayer;
- a statement indicating whether the taxpayer has been part of, or affected by, a business restructure;
- a statement indicating whether the taxpayer has participated in a transaction relating to the transfer of intangibles; and
- a description of functions performed, assets used and risks assumed by the group's members, if affecting transactions involving the taxpayer.

Country-by-Country (CbC) Reporting

Panama has established a regulatory framework for CbC reporting in line with Action 13 of the OECD/G20 BEPS Project.

Annual CbC reports must be submitted by Panama-resident ultimate parent entities (UPEs) of multinational enterprise (MNE) groups whose consolidated revenue in a fiscal period exceeds 750 million euros (or its dollar/balboa equivalent at 2015 exchange rates).⁵⁵

The CbC reports must contain—

- with respect to each jurisdiction in which the MNE group operates, information relating to:
 - total revenue;
 - profits or losses before tax;
 - income tax paid and accrued;
 - stated capital;
 - number of employees; and
 - tangible assets other than cash or cash equivalents;
- a list of all the constituent entities (CEs) of the MNE group, indicating the nature of their main business activities, the jurisdictions of their tax residence and, where different, the jurisdictions of their incorporation; and
- any additional information or explanation that is necessary or which facilitates the understanding of the information contained in the CbC report.⁵⁶

⁵⁵ Executive Decree No. 46 of May 27, 2019, arts 2, 5 transitional paragraph.

⁵⁶ Executive Decree No. 46 of May 27, 2019, art. 4.

The CbC report must be submitted, within 12 months of the end of the fiscal year to which the report relates, in an XML schema, complying with regulations and guidelines to be provided by the Tax Authority.⁵⁷

A Panama-resident CE of an MNE Group, but which is not the group's UPE, must notify the tax authority of the identity and tax jurisdiction of the entity responsible for submitting the CbC report for the group. In addition, it must inform the authority of the group's fiscal period. The deadline, form and method of this notification are to be specified by the tax authority.⁵⁸

Failure to submit a CbC report within the deadline, will result in a penalty of 100,000 dollars, plus an additional penalty of 5,000 dollars per day until the CbC report is filed.

A penalty of 25,000 dollars applies if the information in the CbC report is incorrect. This can be increased to 500,000 dollars if the information in the CbC report is intentionally incorrect.⁵⁹

Panama is a signatory to the Multilateral Competent Authority Agreement on the Automatic Exchange of CbC Reports.

8. Anti-Avoidance Provisions

8.1. General Anti-Avoidance Provisions

With effect from January 1, 2023, the new Tax Procedure Code (see Section 1.1) introduces a general anti-avoidance rule (GAAR), empowering the tax authority to disregard legal forms when premeditated and designed actions are carried out with the sole purpose of avoiding the payment of taxes or obtaining any type of tax advantage. The burden of proof is on the Tax Authority. If it discharges that burden, the tax consequences of such transactions will be those corresponding to "the acts that were actually executed".⁶⁰

8.2. Thin Capitalization/Other Interest Deductibility Rules

Panama does not have any thin capitalization rules. The only limit on the deductibility of interest is that, in accordance with the territorial tax system, for interest to be deductible it must be paid on debt used to produce domestic income.

8.3. Controlled Foreign Company (CFC) Rules

Given the territorial tax system, Panama does not have a CFC regime.

9. Other Taxes

9.1. Payroll Taxes

Panama does not impose any payroll taxes beyond the social security taxes discussed in Section 6.6.

9.2. Capital Taxes (Capital Duties)

Operations Notice Tax (*Aviso de Operación*) is levied at a rate of 2 percent of capital up to a maximum of 60,000 dollars. If the company is operating in the Free Trade Zone, the rate is 1 percent of capital up to a maximum of 50,000 dollars.

9.3. Property Taxes

9.3.1 Transfer Taxes, Including Real Property Transactions

Real estate transfers are subject to a transfer tax of 2 percent of the purchase price or the cadastral value, whichever is higher. The tax is paid by the person transferring the property.⁶¹

⁵⁷ Executive Decree No. 46 of May 27, 2019, art. 5.

⁵⁸ Executive Decree No. 46 of May 27, 2019, art. 3.

⁵⁹ Fiscal Code, art. 756, as amended by Law 254 of November 11, 2021, art. 45.

⁶⁰ Law No. 76 of February 13, 2019, arts. 20, 392, as amended by Law No. 257 of November 26, 2021, art. 5.

⁶¹ Law No. 106 of December 30, 1974.

9.3.2 Real Property Taxes

Property is subject to an annual real estate tax, at the following rates according to the property's appraised value:⁶²

Primary domestic residences (family or single person)

- up to 120,000 dollars – 0 percent;
- from 120,001 dollars to 700,000 dollars – 0.5 percent; and
- over 700,000 dollars – 0.7 percent.

Secondary domestic residences or commercial/industrial properties

- up to 30,000 dollars – 0 percent;
- from 30,001 dollars to 250,000 dollars – 0.6 percent;
- from 250,001 dollars to 500,000 dollars – 0.8 percent; and
- over 500,000 dollars – 1 percent.

Further exemptions apply for newly constructed residential properties.⁶³

Agricultural land

Land used in agricultural activities is not subject to property tax, provided the land is used according to the Ministry of Agricultural Development guidelines and does not have an assessed value of more than 350,000 dollars.⁶⁴

Real estate tax is generally paid in three installments (April 30, August 31 and December 31). However, a 10 percent discount (increased to 15 percent for the 2022 fiscal year) on the amount of real estate tax payable is given to taxpayers who pay the entire sum by April 30 of the relevant year.⁶⁵

9.3.3 Taxes on Movable Property

Income tax payable on the sale of movable property is calculated on the profits obtained at a fixed rate of 10 percent.

9.3.4 Fixed Asset Taxes

Fixed assets are subject only to the 10 percent capital gains tax. The transfer of these assets is not subject to any withholding.

9.4. Miscellaneous Taxes

Branch Remittance Tax

A branch of a foreign company operating in Panama is subject to a tax of 10 percent of after-tax income, in addition to the corporate income tax.

Companies operating under the MHQ and EMMA regimes are exempt from the branch tax (see Section 2.6.4).

Licensing Tax

All commercial and industrial businesses requiring a notice of operation (which is virtually all business operating in Panama) are subject to an annual licensing tax calculated at 2 percent of net worth up to a cap of 60,000 dollars.

⁶² Law No. 66 of October 17, 2017, amending various provisions of the Fiscal Code.

⁶³ Law No. 28 of May 8, 2012; Law No. 66 of October 17, 2017, art. 4.

⁶⁴ Law No. 49 of September 11, 2018, art. 1, amending the Fiscal Code, art. 764(9).

⁶⁵ Fiscal Code, art. 786, as amended by Law No. 208 of April 6, 2021, art. 9.

Franchise Tax

All corporations must pay a franchise tax of 300 dollars per year, the deadline of which depends on the date of incorporation. Non-profits, cooperatives, and civil partnerships are not subject to the franchise tax.

Inheritance and Gift Tax

There is no inheritance or gift tax in Panama.

Excise Tax

Non-essential goods and services (e.g., soda, tobacco products, luxury items, etc.) are subject to excise tax calculated on the basis of insurance costs, freight plus import duty, or sales price. Rates vary depending on the good or service and range from 5 percent (on soda) to 100 percent (on tobacco products).

Stamp Duty

Certain commercial contracts are subject to a stamp duty of 0.10 dollars per 100 dollars of value. On May 28, 2014, the Supreme Court found the requirement of paying stamp taxes on memorials or written petitions addressed to or filed with any civil servant, public authority, or corporation as unconstitutional.

Value Added Tax (VAT)/Goods and Services Tax (GST)

For VAT/GST and similar taxes, see the VAT Navigator.

10. Special Industries

10.1. Oil, Gas and Mineral Extraction

Varying rates of royalty tax apply to extraction of sand, gravel, quarried stone, limestone, clay, and tuff stone. Also, contractors are subject to a 2 percent to 4 percent royalty tax on the value of minerals extracted in Panama.

Panama does not have any other tax regimes applicable to the oil and gas or mineral extraction industries.

10.2. Banking and Finance

Panama levies an additional annual tax on the assets of banks and banking institutions. Such institutions that hold an international license must pay 75,000 per year.

The annual tax due from holders of a general license depends on the value of the company's assets:

- assets under 100 million dollars – 75,000 dollars;
- assets 100 million dollars to 200 million dollars – 125,000 dollars;
- assets 200 million dollars to 300 million dollars – 175,000 dollars;
- assets 300 million dollars to 400 million dollars – 250,000 dollars;
- assets 400 million dollars to 500 million dollars – 375,000 dollars;
- assets 500 million dollars to 750 million dollars – 450,000 dollars;
- assets 750 million dollars to 1 billion dollars – 500,000 dollars;
- assets 1 billion dollars to 2 billion dollars – 700,000 dollars; and
- assets over 2 billion dollars – 1 million dollars.

About the Author



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Jose Rafael Reyes is a partner at Morgan & Morgan and heads the Taxation practice group at the firm.

Mr Reyes has over 10 years of experience handling complex legal and tax matters. He regularly advises clients from multiple industries in connection with international taxation, tax planning, transfer pricing, regulatory compliance, proceedings before local tax authorities, and representation before the Administrative Tax Court.

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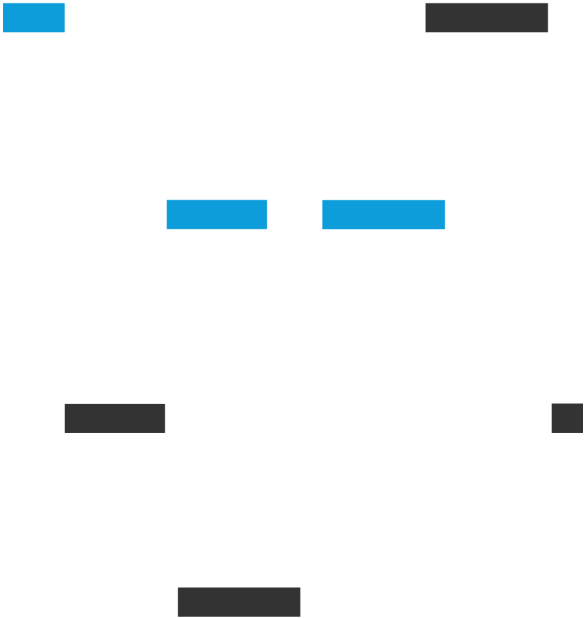
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