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The Latin American host with the most: relocating your corporate headquarters to Panama

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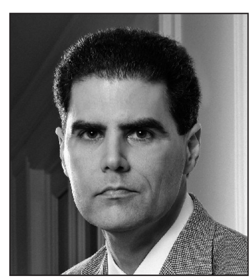
History repeats itself. For more than a hundred years, world and business visionaries have used Panama's strategic geographical position as a competitive advantage to obtain an edge against other nations and/or competitors. Initially, the Spanish used the Isthmus to consolidate and protect the wealth gathered while conquering the Americas. Centuries later, a pathway was built across Panama to connect the Atlantic and Pacific oceans and extend the reach of international trade. Following the construction of the Panama Canal, multinational companies followed and embraced the opportunity to develop the complementary infrastructure to accommodate the needs arising from the operation of this waterway.

The international recognition of Panama originated from being home to the Panama Canal, the world's most important waterway. The Canal is managed and administered by Panamanians and is undergoing a US$5.25bn expansion project to build a third set of locks and accommodate larger vessels.

Furthermore, Panama has taken advantage of its privileged location by also hosting the Colon Free Zone which is the largest re-export free zone in the Western Hemisphere, complemented with a modern port system that includes the busiest port in Latin American. In addition, Panama has a dynamic and well regulated banking and financial industry comprised of over 90 international and local banks, including HSBC, BBVA and Citibank, as well as wealth management and brokerage operations from Merrill Lynch, Credit Suisse and UBS.



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In the last 10 years, Panama has experienced sustained economic growth, with an average growth of 9.5% in the last three years. The economy is spearheaded by a robust service sector which today accounts for more than 70% of its GDP. It has been the recipient of the largest amount of foreign direct investment in Central America, reaching US$2.4bn in 2008. Despite the recent downturn in the global economy, Panama's economy is nonetheless expected to grow by 2.5% in 2009, according to the United Nations Economic Commission for Latin American and the Caribbean.

Panama has a territorial taxation system, meaning that only income earned from within its territory is subject to income tax. Furthermore, a wide range of activities are nonetheless treated as generating offshore income, hence, non-taxable.

In addition, the US dollar has been the legal tender for more than 100 years and as a result there are no exchange controls of any kind. There are no restrictions on foreign ownership or controls on the repatriation of capital and/or dividends. Panama enjoys business-friendly legislation and a strong rule of law providing foreign investors the same treatment as nationals, except very few limitations.

In sum, economic freedom has always been a priority. Government intervention in business is low, and most sectors of the economy are very competitive. Panama has enjoyed a longstanding political stability, holding democratic elections in the last 20 years, and a constitutional ban on military troops. In fact, power has transferred peacefully four times in this period from one party to another.

Investments in communications and infrastructure are one of the cornerstones of the country's current and future development. Panama boasts one of the more modern communication systems in the region with excellent internet connectivity. Moreover, the economy benefits from a bilingual and well-educated professional class and an extremely strong commitment to fostering educational development.

Newly elected President Ricardo Martinelli has announced an aggressive plan for the renovation and development of public works, including a new subway system for Panama City, road infrastructure projects and a proposal to interconnect the electric grids of Panama and Colombia. Previous administrations adopted legislation to position Panama as an attractive destination for multinational companies seeking to expand their regional operations in the Latin American marketplace.

Consequently, special legislation has been enacted to create incentives and attract foreign investment. As an example of such legislation, we can mention the Multinational Company Headquarters Law which provides a plethora of incentives to promote the re-domiciliation of multinational headquarters, the establishment of a new special economic zone in the Pacific entrance to the Canal, and tax benefits for the operation of call centres. As a result, numerous companies such as Dell, Sitel, Procter & Gamble, Maersk, Caterpillar Latin America, LG, Peugeot/Citroen, ST Aerospace, Cemex, Haliburton, Kumho Tires and Moffat & Nichols Engineers have since opted to re-locate their regional operations or call centres to Panama with a goal of capitalising on the new FDI-friendly legislation and making their regional operations more efficient and more importantly, more profitable.

Multinational Company Headquarters Law (Law No. 41 of 24 August 2007)

Law No. 41 of 24 August 2007 (MHQ Law), creates a special regime to facilitate the establishment and operations of the regional headquarters of multinational companies in Panama. Moreover, it creates a dedicated one-stop shop at the Ministry of Commerce and Industry, with representatives from various government institutions, to avoid bureaucratic red tape while processing applications, licences, immigration visas and other government permits.

There are special tax, immigration and labour incentives for multinational headquarters (MHQ) registered under the MHQ Law. Such incentives have provided the right business environment for companies such as Caterpillar Latin America, Maersk, Procter & Gamble, Western Union, AES, Endress+Hauser and many others, to relocate their regional operations to Panama.

The MHQ Law defines a multinational company's headquarters as the offices in Panama of a multinational corporation providing any of the following services to its headquarters, subsidiaries, affiliates or associates companies:

- management and/or administration of business operations, globally or for a specific geographical area, of any company of the economic or corporate group. Such services are strategic planning, business development, human resources management, training of personnel and/or logistics;
- logistics and storage of components or parts required for the manufacturing or assembly of products manufactured by the MHQ;
- technical assistance for companies of the economic or corporate group, or for clients that have acquired products or services from the MHQ;
- accounting for the economic or corporate group;
- elaboration of blueprints that are part of the designs for constructions related to the main business activities of the MHQ or its economic group;
- consulting, coordination and follow-up of marketing guidelines for goods and/or services produced by the economic or corporate group;
- electronic processing of any activity, including in the consolidation of operations of the economic or corporate group;
- financial management (treasury) for the economic or corporate group;
- support for operation and R&D products and/or services for the economic or corporate group; and/or
- any other service approved previously by the Licensing Commission of Multinational Companies.

An important prerequisite to obtain the incentives from the MHQ Law is that the total assets of the MHQ economic or corporate group must exceed US$200m.

Incentives provided by the MHQ Law

The MHQ Law offers several tax incentives for any MHQ itself, as well as for its foreign personnel working from Panama. At the corporate level, the MHQ will be exempt from income tax for all profits generated from services rendered to its subsidiaries and affiliates outside of Panama, and MHQs desiring to implement a global taxation strategy for fiscal efficiency may negotiate a tax scheme with the local authorities.

At the personnel level, all foreign mid-level and general management personnel will be exempt from income tax and from social security contributions if their salaries are paid from abroad. However, the MHQ shall provide private health insurance coverage to all its foreign personnel during their stay in Panama. Additionally, foreign personnel may import their household items duty free, up to a certain amount, when first arriving to Panama.

One hurdle traditionally faced by international companies considering relocating to Panama was the minimum labour quotas of national employees required under Panama's labour regulations and the cumbersome process to obtain immigration visas and work permits for foreign personnel. These problems have been addressed by establishing a special immigration programme for foreign personnel of MHQs and by exempting the application of local labour quotas. Furthermore, immigration visa applications are resolved in approximately two weeks and are granted for a renewable five-year period. Lastly, foreign personnel under such programme are exempt from the obligation to obtain work permits.

Panama-Pacific Special Economic Area (Law No. 41 of 20 July 2004)

Law No. 41 of 2004 (Howard Law), takes an important area covering 1,400 hectares (3,460 acres) within the old Canal Zone known as the Howard Air Force Base, and turns it into an attractive international commercial and logistical destination named the 'Panama-Pacific Special Economic Area' (Area). The Howard Law also creates an independent entity primarily to manage, promote and develop this special economic zone, as well as a dedicated one-stop shop to avoid bureaucratic red tape.

In the interest of attracting international investment, the government created a special regime with incentives in customs, taxes, labour and immigration within the Area, all of which welcome multinational companies to establish key regional offices in Panama for the import, assembly, repair and manufacture of products, as well as the provision of services, among other business activities, primarily destined for export.

Major companies such as Dell Computers have enjoyed the benefits of being in the Area for years, while others such as 3M and Caterpillar will begin operations soon. Also, in 2007 the master development of the Area was awarded for a period of 20 years, to a subsidiary of London & Regional Properties (LRP). LRP is set to invest more than UD$400m over eight years transforming the Area into a self-sufficient city with residences, schools, hotels, restaurants, parks and a golf course, among other amenities. The Area, being a former Air Force base, also has its own international airport which at first will handle cargo or private flights, and in the future may even handle commercial passenger flights.

The registration of any company in the Area brings with it the benefits of the Howard Law. Among them is the liberty to engage in permitted activities, duty-free import and export and other tax breaks, the right to employ foreign workers under a special regime, and automatic coverage under the Investor Protection Law (Law No. 54 of 1998).

With regards to taxes, the general principle in the Area is that all activities, business, services, operations or transactions within the Area, will be 100% free of national direct or indirect taxes, contributions, fees, duties and imposts. This includes, for example: import duties on merchandise, supplies, machinery, vehicles, parts, fuel, raw materials, etc., as long as these are destined to be used within the Area; sales tax on goods and services; business licence tax; stamp tax; export or re-export tax; revenue tax on foreign-sourced revenue; and international phone calls tax. However, the following taxes are not exempted provided the company provides services inherent to professions that are regulated by Panamanian law: revenue tax on locally-sourced income; dividend tax on retained earnings; complementary tax; remittance or transfer tax on payments made to foreign service providers; import duties and sales tax on goods and services.

In addition, the Howard Law provides for certain labour concessions such as the capacity to hire more foreign specialised personnel and, hence, avoid the national labour quota required by local legislation, flexible work schedules, overtime hours and vacations.

The Area is, without a doubt, a business and logistics centre that will attract international investors in the years to come.

International Call Centres Law (Law No. 54 of 25 October 2001)

Besides its privileged geographical position, Panama is the ideal location for companies in the information and communications technology (ICT) industry. The country offers a sophisticated telecommunications platform with five main submarine fibre-optic cables connecting North and South America with the Caribbean and the rest of the World. Consequently, Panama's digital connectivity guarantees the bandwidth, redundancy and security necessary to develop a vigorous telecommunications and information technology industry.

In addition to these key infrastructure factors, laws have been adopted to develop call centres, namely Law No. 54 of 2001. Over 87 national and international companies are operating under Law 54's umbrella including companies such as Dell, Sitel, Cable & Wireless Panama, Hewlett-Packard and National Asset Recovery System (NARS).

Call centres are defined as the service that enables both natural persons and legal persons operating from Panama to offer customers of Panamanian or foreign companies telephone assistance in: product-related and service-related technical or commercial information, sales, marketing, customer service, telemarketing, technical support or other specialised business activities. Parties interested in establishing a call centre in Panama must first obtain a government-issued concession by formally applying to the regulator.

Some of the incentives offered to commercial call centres by means of Law No. 54 are:

- exemption on income and value added tax for international call centres;
- exemption on all import duties for the equipment dedicated to call centre activity; and
- special labour provisions that allow companies to establish flexible work schedules, overtime hours and vacations.

As can be appreciated from the foregoing, Panama is more than a trans-shipment, banking and service centre to the World; it is a tailor-made corporate destination with a first-world cosmopolitan city, and a passenger hub that connects business and leisure travellers to all major cities in Latin America.

Visionaries force history to repeat itself and we at Arias, Fabrega & Fabrega are confident that Panama has enormous potential to become the premier Latin American centre for multinational headquarters. We are certain that our ability and expertise will provide an invaluable asset in helping multinational companies take advantage of the unprecedented opportunity to consolidate their regional operations from Panama.

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