Doing Business in Panama

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LEGAL SYSTEM

1. What is the legal system (civil law, common law or a mixture of both)?

Panama has a civil law system.

FOREIGN INVESTMENT

2. Are there any restrictions on foreign investment (including authorisations required by central or local government)?

There are no restrictions on foreign investment, except the following:

- Foreign governments cannot own real estate and foreign nationals cannot own real property within ten kilometres of the borders.
- Foreign nationals cannot engage in retail trade, with certain exceptions.

For reasons of national security, foreign participation is restricted in certain industries, such as:

- Aviation.
- Telecommunications.
- Mining.
- Explosives.

3. Are there any exchange control or currency regulations?

There are no exchange control or currency regulations.

4. What grants or incentives are available to investors? Are any of these aimed specifically at foreign investors?

The following incentives are available to investors:

- **Panama-Pacifico Special Economic Zone.** Panama-Pacifico operates in a former US air force base under special legislation, offering tax, customs, licensing, immigration and labour benefits, primarily to attract industries, commercial and service operations serving clients outside Panama.
- **Multinational headquarters.** Multinational companies that establish regional headquarters in Panama benefit from significant tax, labour and immigration incentives.
- **Call centres.** There is special legislation to promote the development of call centres in Panama.
- **Colon Free Zone (CFZ).** The CFZ provides income tax and other benefits to businesses engaged primarily in the warehousing and wholesale of merchandise for re-export.
- **Export Processing Zones (EPZs).** Manufacturing operations in any of the EPZs can obtain benefits, such as exemption from capital gains, dividend taxes and import duties.
- **Hydropower generation and clean energy.** Companies in this industry can benefit from exemptions from import duties and value added tax (VAT).
- **Industrial incentives.** In November 2009 the government created a Certificate of Industrial Development, which entitles holders to reimbursement of expenditure on certain qualifying activities.
- **Investment Stability Law**. This guarantees equal treatment and tax stability for up to ten years for foreign investors.

- **Free Trade Agreements (FTAs).** Panama has ratified FTAs with all of the Central American countries, Canada, Singapore, Taiwan, and the Caribbean common market. In 2008 it concluded negotiations for a bilateral Trade Promotion Agreement with the US.
- **Bilateral agreements.** Panama has signed bilateral investment agreements with several countries.

BUSINESS VEHICLES

5. What is the most common form of business vehicle used by foreign companies to conduct business in your jurisdiction? In relation to this vehicle, please provide details on:

- **Registration formalities (including timing).**
- **Minimum (and maximum) share capital.**
- **Whether shares can be issued for non-cash consideration, such as assets or services (and any formalities).**
- **Any restrictions on the rights that can attach to shares.**
- **Any restrictions on foreign shareholders.**
- **Management structure and any restrictions on foreign managers.**
- **Directors' liability.**
- **Parent company liability.**
- **Reporting requirements (including filing of accounts) and cost of compliance.**

The most common form of business vehicle used by foreign companies is a Panamanian subsidiary, or registering a branch.

- **Registration formalities.** Corporations are created by the registration of articles of incorporation at the Public Registry.
- **Share capital.** A corporation's authorised capital can be stated as:
  - a number of shares with par value;
  - a number of shares without par value; or
  - a combination of both.
- **Non-cash consideration.** Corporations can issue shares for money, services or assets.
- **Rights attaching to shares.** There are no restrictions on these. Rights, privileges and restrictions can be established in the articles of incorporation.
- **Foreign shareholders.** There are no restrictions based on nationality.
- **Management structure.** The board of directors is responsible for the management of corporations. Directors need not be shareholders, or Panama nationals or residents.
- **Directors' liability.** Directors are not liable for the corporation's obligations. However, directors are responsible for discharging their duties diligently, and can become liable for negligence in the discharge of their duties.
- **Parent company liability.** Shareholders, including parent companies, are not liable for the corporation's obligations, except for unpaid amounts on the subscription price.
- **Reporting requirements.** There are no legal reporting requirements and there is no requirement to file financial or other information. However, the following information must be registered:
  - amendments to the articles of incorporation;
  - changes of directors or officers;
  - the dissolution, merger or continuation of the company.

EMPLOYEES

6. What are the main laws regulating employment relationships?

Employment relationships are governed mainly by the Labour Code, which applies to all employment relationships if services are rendered in Panama, regardless of the choice of legal provisions in employment contracts or the parties' nationalities.

7. Is a written contract of employment required? Are any agreements and/or implied terms likely to govern the employment relationship?

A written employment contract is not required, but in its absence the burden of proof of the terms of the contract shifts to the employer. Certain provisions of labour law are public policy and the parties cannot contract out.

8. Are employees entitled to management representation and/or to be consulted in relation to corporate transactions (such as redundancies and disposals)?

Employees are not entitled to management representation.

9. How is the termination of individual employment contracts regulated?

The Labour Code regulates the termination of employment contracts, which includes:

- **Termination of contracts for an indefinite period.** Employees hired for an indefinite term can be dismissed:
  - without cause, if they were employed for less than two years, subject to notice and statutory severance payments;
  - only for just cause, if they were employed for more than two years, subject to statutory severance payments.
- **Termination of contracts for a definite period.** If an employment contract is for a definite period, or for a specific task, termination of the contract without cause before the conclusion of contract requires payment of an indemnification to the employee.
- **Other forms of termination.** Other employment contracts can be terminated by mutual consent.

10. Are redundancies/mass layoffs regulated? If so, please give details.

Except for in certain special economic zones, mass layoffs are only permitted in cases of economic hardship, with the approval of the Ministry of Labour. Examples of these cases include:

- The employer's insolvency.
- The unprofitability of the business.
- Suppression of work relevant to the employee's contract.
- Reduction of activity due to economic crisis, expiration of a concession, or other similar cause.

11. Do foreign employees require work permits and/or residency permits? If so, how long does it take to obtain them and how much do they cost?

Employment of foreign personnel is subject to quotas. Generally, 85% to 90% of the workforce must be Panamanian citizens.

Foreign employees require work permits and resident visas. Available visas include the following:

- **Temporary Visitor Visa as Ordinary Personnel.** This is issued to a foreign individual who has obtained a work permit as a foreign worker included in the 10% quota for foreign employees.
- **Temporary Visitor Visa as Executive, Expert or Technician.** This is issued to foreign individuals who have obtained a work permit as an expert, and is included in the 15% quota for expert foreign employees.
- **Special Temporary Visitor Visa.** This is issued to foreign executives who come to Panama to conduct transactions which become effective abroad, and whose salary is not paid from Panamanian sources. No quota applies to holders of this visa.

The total cost of these visas is about US$1,900 (as at 1 October 2010, US$1 was about EUR0.7), including the work permit, where required.

TAX

12. In relation to employees, what constitutes tax residency in your jurisdiction?

Foreign employees who stay for more than 183 days, whether consecutive or not, and earn Panama source income become taxpayers and are required to file annual tax returns. Those who stay for 183 days or fewer are not required to file tax returns, but are subject to income tax withholding on Panama source income.

13. What income tax or social security contributions must the following pay:

- **Tax resident employees?**
- **Non-tax resident employees?**
- **Employers, in relation to their employees?**

Tax resident employees

Tax resident employees must pay the following taxes:

- **Income tax.** Individuals earning between US$11,000 and US$50,000 annually are subject to income tax at 15%. Individuals earning US$50,000 or more are subject to income tax at 25%.
- **Social security contributions.** Individuals pay social security tax at 9%.
- **Education tax.** Individuals pay education tax at 1.25%.

Non-tax resident employees

Non-tax resident employees are subject to the tax requirements on their Panama source income.

Employers

Employers withhold income tax, social security contributions and education tax from employees' wages. In addition, employers must pay the following in relation to their employees:

- **Social security contributions.** Employers pay social security contributions at 12%.
- **Education tax.** Employers pay a 1.50% education tax.
- **Workers' compensation.** Employers pay workers' compensation at rates from 0.98% to 5.6%.
- **Severance fund contributions.** Employers must set up and make contributions to a severance fund, which includes seniority payments and funds set aside in the event that an employee is entitled to indemnification for unjust termination.

14. In relation to business vehicles, what constitutes tax residency in your jurisdiction?

Setting up a Panama corporation does not itself constitute tax residency. Tax residency is constituted by:

- Setting up a permanent establishment in Panama.
- Engaging in activities generating Panama source income.

In general, an entity creates a permanent establishment in Panama when it owns, directly or through an agent, employee, representative or other personnel, an office, fixed place of business, or centre where its activities are wholly or partially carried out, as well as where services or works are performed during more than 183 days in a 12-month period.

15. Please give details of the main taxes that potentially apply to a tax resident business vehicle (including rates).

Businesses are taxed on their jurisdiction source income. The main taxes that apply to a tax resident business vehicle include the following:

- **Income tax.** From 2011, most companies pay income tax at a 25% flat rate on net taxable income. Companies with taxable income exceeding US$1.5 million pay the 25% flat rate on net taxable income, with a floor of 1.1675% of gross taxable income.
- **Capital gains tax**. Gains on the disposition of equity interests of companies that have Panama source income are subject to a 10% capital gains tax on the portion of the gains allocated to Panama.
- **Commercial licence tax.** Companies with a net worth of more than US$10,000 that hold a business licence are subject to a 2% tax on capital and retained earnings, with a US$60,000 ceiling.
- **Annual franchise duty.** Companies must pay an annual franchise duty of US$300.
- **Other taxes.** Depending on their activities, business entities can be subject to other taxes, such as:
  - VAT;
  - stamp duty;
  - property and municipal taxes;
  - import duties.

16. How are the activities of non-tax resident business vehicles taxed?

The activities of non-tax resident business vehicles are subject to a 12.5% withholding tax, if the effects of those activities are felt within Panama.

17. Please explain how each of the following is taxed:

- **Dividends paid to foreign corporate shareholders.**
- **Dividends received from foreign companies.**
- **Interest paid to foreign corporate shareholders.**
- **Intellectual property (IP) royalties paid to foreign corporate shareholders.**

- **Dividends paid.** Business vehicles holding a business licence or generating taxable income must withhold:
  - 10% on dividends obtained from Panama source income with respect to nominative shares (20% if the payment is with respect to bearer shares);
  - 5% on dividends derived from non-Panama source income, export-related income and certain other exempted income, including income earned within the country's free trade zones.

- **Dividends received.** The business vehicle that makes the distributions must withhold the applicable dividend tax. These dividends are not subject to any further taxes in Panama.
- **Interest paid.** Interest paid to foreign creditors on loans whose proceeds are used in Panama is deemed to be Panama source income, and 50% of the interest earned is subject to income tax at the applicable rates, which is withheld by the borrower.
- **IP royalties paid.** Royalties paid abroad are subject to withholding tax at the applicable income tax rate over 50% of the amount paid.

18. Are there any thin capitalisation rules (restrictions on loans from foreign affiliates)? If so, please give details.

There are no thin capitalisation rules.

19. Must the profits of a foreign subsidiary be imputed to a parent company that is tax resident in your jurisdiction (controlled foreign company rules)?

The profits of a foreign subsidiary cannot be imputed to a tax-resident parent company.

20. Are there any transfer pricing rules? If so, please give details.

Transfer pricing rules apply to transactions between a Panamanian entity and a related entity resident of a country with which Panama has a tax treaty in force. Documentation must be prepared according to the OECD Transfer Pricing Guidelines and an informative return must be filed within six months following the end of the fiscal year.

21. How are imports and exports taxed?

Imports are subject to VAT at 7% and to import duties based on a tariff schedule. Certain imports are subject to excise tax. There are no export taxes.

22. Is there a wide network of double tax treaties? If so, please give details.

In 2010, Panama signed and ratified a treaty with Mexico. Treaties with Barbados, Luxembourg, The Netherlands, Portugal, Qatar, Singapore, South Korea and Spain have also been signed. Panama has also completed negotiations with Belgium, the Czech Republic, France, Ireland and Italy, though no tax treaties are yet in force.

COMPETITION

23. Are restrictive agreements and practices regulated by competition law in your jurisdiction? If so, please give brief details.

Generally, agreements or practices that hinder competition are prohibited. The following, among others, constitute absolute monopolistic practices and are illegal:

- Price fixing.
- Bid rigging.
- Geographic market allocation.
- Supply-side limitations.

The following, among others, are relative monopolistic practices, and can be illegal under certain circumstances:

- Territorial distribution restrictions.
- Tying agreements.
- Reciprocal dealings.

Business mergers and other business combinations are subject to merger control rules, although prior approval is not required.

INTELLECTUAL PROPERTY

24. Please outline the main intellectual property rights that are capable of protection in your jurisdiction. In each case, please state:

- **Nature of right.**
- **How protected.**
- **How enforced.**
- **Length of protection.**

Patents

- **Nature of right.** An invention is patentable if it is:
  - new;
  - original; and
  - capable of industrial application.

The patent owner has the exclusive right to exploit an invention for a specified period.

- **How protected.** Patents are protected by registration at the Industrial Property Office (IPO).
- **How enforced.** The patent owner can bring a civil or criminal action in court.
- **Length of protection.** The patent is protected for 20 years from the filing date.

Trade marks

- **Nature of right.** A trade mark is any sign or word, or combination of these, or any other graphical medium, whose characteristics identify a product or service. Non-traditional trade marks such as sounds and odours can also be protected. The registered trade mark owner has exclusive rights to use the trade mark, but the earliest user has a preferential right to registration.
- **How protected.** A trade mark is protected by registration with the IPO.
- **How enforced.** A trade mark owner can bring a civil or criminal action in court.
- **Length of protection.** A trade mark is protected for ten years from the filing date, renewable indefinitely for ten-year periods.

Registered designs

- **Nature of right.** Any new and unique two- or three-dimensional design which acquires a special appearance once turned into a product to serve as a pattern or model for manufacture or commercial purposes can be protected and registered. The design right gives the exclusive right to use the registered design.
- **How protected.** The design is protected by registration at the IPO.
- **How enforced.** The owner of a registered design can bring a civil or criminal action in court.
- **Length of protection.** The design is protected for ten years from the filing date, renewable for one additional five-year period.

Unregistered designs

Panamanian law does not address unregistered designs.

Copyright

- **Nature of right.** Any literary, scientific and artistic work resulting from an original intellectual creation can be protected by copyright. The copyright owner has the exclusive right to authorise use of the work.
- **How protected.** Copyright protection arises upon the work's creation. Registration is not required but is recommended to ensure enforceability.
- **How enforced.** The copyright holder can bring a civil or criminal action in court.
- **Length of protection.** Copyright remains for the life of the author plus 50 years, and is transferred at death. The lapse of economic rights causes the work to pass into the public domain.

Confidential information

- **Nature of right.** Confidential information that is considered a trade secret is any commercial or industrial information which provides a person or business entity with an economic or competitive advantage regarding third parties, and where the person or business entity has taken sufficient steps to ensure the information's confidentiality. Confidential information is most often protected by contractual rights, although some laws impose confidentiality duties on banks, trust companies, merchants, public servants and others.
- **How protected.** Confidential information is protected by law and contractual arrangements.
- **How enforced.** A breach of the confidentiality agreement entitles the aggrieved party to seek preliminary or permanent injunctions, or other relief, as well as monetary damages.
- **Length of protection.** Generally, there is no statutory length of protection, although statutes of limitation do apply.

MARKETING AGREEMENTS

25. Are marketing agreements regulated in your jurisdiction? If so, please give brief details in respect of the following arrangements:

- **Agency.**
- **Distribution.**
- **Franchising.**

There are no laws regulating agency, distribution or franchise agreements. These agreements are governed by general commercial laws.

E-COMMERCE

26. Are there any laws regulating e-commerce (such as electronic signatures and distance selling)? If so, please give brief details.

Laws on e-commerce in Panama regulate information and data protection, and the use of e-banking services, and provide that:

- Electronic signatures certified by qualified providers registered with the regulatory agency are valid.
- Electronic signatures and documents are admissible as evidence, subject to certain criteria.
- Businesses engaged in commercial transactions and providers of information over the internet must provide certain disclosures and opt-out provisions to end users and consumers.

DATA PROTECTION

27. Are there any data protection laws? If so, please give brief details.

The Constitution and several other laws contain data protection provisions which state that:

- Businesses must preserve the confidentiality of books and other documents stored in databases or elsewhere.
- Internet, telephone and mobile phone providers must preserve data collected and provided by consumers.
- Providers of electronic document storage must guarantee the protection of data stored by them.
- Banks are prohibited from disclosing client information without consent, unless they are required to do so under the banking, credit agency or anti-money laundering and terrorist financing laws.
- Credit card issuers must keep information they collect on users confidential, unless disclosure is required by law in the course of criminal investigations, and must ensure the security of that information.

PRODUCT LIABILITY

28. Are there any laws regulating product liability and product safety? If so, please give brief details.

Product liability rules are mainly found in the following:

- **Civil Code.** Generally, when a person causes injury to another person, the tortfeasor is liable and must compensate that person.
- **Consumer Protection Laws.** It is a manufacturer's duty to provide adequate labels, instructions and/or warnings regarding its product. The manufacturer is responsible for damages caused to the consumer only in cases of negligence or wilful misconduct.

A health authorisation certificate from the Health Ministry is required to import and market certain goods, for example drugs, medicated cosmetics and cleaning products.

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Qualified. Panama, 1994; New York, 1997

Areas of practice. Anti-trust; trade and competition; banking and finance; M&A and joint ventures; securities regulation; tax.

Recent transactions

- US$100 million loan by Citibank to TACA.
- US$225 million Citibank loan to the BAC/Credomatic Group.
- HSBC Bank (Panama) historic registration of a programme of Negotiable Banking Certificates in Mexico.
- US$1 billion bond offering by the Republic of Panama.
- US$750 million Goldman Sachs' cross-border structuring of notes issuance by Global Crossing Limited.