

LATIN LAWYER REFERENCE BANK FINANCING 2019

Panama

Estif Aparicio and Donald Canavaggio
Arias, Fábrega & Fábrega

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1 What are the most common forms of bank financing in your jurisdiction?

All types of bank financing are found in Panama: bilateral and syndicated, secured and unsecured, domestic and cross-border, for general corporate purposes and project finance.

2 Can non-bank lenders such as private credit fund managers offer credit in your jurisdiction?

Yes. There is no requirement that non-banking entities become banking entities in order to offer credit in Panama.

3 Are any governmental or central bank registrations or approvals required for a foreign arranger or lender (being an entity not incorporated in your jurisdiction or operating through a branch or office outside of your jurisdiction) to arrange on behalf of or to lend to a borrower in your jurisdiction?

Under the laws of Panama, there are no such registrations or approvals required for foreign lenders.

4 Are there any foreign exchange provisions restricting, or governmental or central bank registrations or approvals required for, a borrower in your jurisdiction to contract debt obligations in a foreign currency or to remit funds abroad?

Under the laws of Panama, there are no such foreign exchange restrictions to, or registrations or approvals required for, a borrower to contract debt obligations in a foreign currency or the remittance of funds abroad. Panama has no mandatory legal tender currency, although most transactions are effected in US dollars.

5 Are borrowers of foreign currency denominated debt required as a matter of law to maintain a minimum hedging ratio or a minimum forex liquidity ratio?

No. Under Panamanian law, there is no regulation of foreign currency-denominated debt. Moreover, under Panamanian law financial transaction can be entered into in any currency and not just the official currency. Nevertheless, if a contract fails to state the means in which the exchange rate is to be calculated in dollars, any change in the exchange rate shall be at the risk of the lender. While the balboa is the official currency of Panama, the US dollar is legal tender.

6 Are there any governmental or central bank registrations or approvals required for the prepayment of loans abroad?

Under the laws of Panama, there are no such registrations or approvals required for the prepayment of loans abroad.

7 Are any mandatory governmental or central bank deposits required to be made from loan proceeds?

Under the laws of Panama, there are no such deposits required to be made from loan proceeds.

8 Describe any governmental measures that may be taken to declare a moratorium on the loan obligations of private companies.

There is no specific legal framework for adopting moratorium measures.

9 Describe any environmental liabilities and any other areas of lender liability that may arise as a result of the activities of a borrower or the realisation of a security interest.

In general, a lender would not incur any environmental liability merely as a result of the granting of a credit facility to a particular borrower or the realisation of a security interest. Notwithstanding this, it is possible, in theory, that a lender who is foreclosing on a mortgage and who has acquired control over the mortgaged property could be exposed to environmental liability if such a lender fails to manage the environmental hazards of the property and as a result of such failure the land or other surrounding properties are polluted or contaminated.

10 Are interest payments or loan fees subject to a withholding tax?

Interest and fees earned by foreign domiciled lenders on loans and other credit facilities used to finance business operations in Panama or the proceeds of which are utilised in Panama are deemed to be Panamanian source income subject to income tax in Panama. As a result, 50 per cent of the interest or fee payments to foreign domiciled lenders are subject to income tax withholding at the general corporate income tax rate of 25 per cent. No income tax withholding is applicable to interest or fees earned by foreign domiciled lenders if the loans or other credit facilities are not used to finance business operations in Panama or the proceeds thereof are not utilised in Panama.

Interest and fees earned by lenders domiciled in Panama on loans and other credit facilities used to finance business operations in Panama or the proceed of which are utilised in Panama are deemed to be Panamanian source income subject to income tax in Panama. Such interest payments and loan fees paid to lenders domiciled in Panama are not subject to withholding income tax. Such lenders are responsible for paying its income tax due at the applicable rate.

11 Do there exist any thin capitalisation rules which limit the amount of debt a borrower may incur as a proportion of its equity or governmentally imposed credit rating maintenance requirements to mitigate overleverage risk?

There are no thin-capitalisation rules in Panama. Additionally, there is no regulation of government imposed credit rating maintenance requirements with respect to the debt incurred by a borrower. Nevertheless, pursuant to Panamas Securities Laws, certain publicly traded bonds and other securities may be required to report or maintain a credit rating (albeit not a specific minimum rating).

12 What other taxes or mandatory fees, for example, transaction, registration or documentary, apply to loan transactions?

Value added tax, known in Panama as ITBMS, applies to loan fees at the standard rate of 7 per cent when the lender is domiciled in Panama.

In addition, stamp taxes apply to the loan transaction documents, including agreements and contracts, when the loan is subject to income tax in Panama. Stamp taxes must be paid on each original copy of the loan or credit agreement and are calculated at a rate of US\$0.10 for each US\$100 of the face value of the principal obligation, as expressed in the loan or credit agreement. Stamp taxes do not apply to documents related to loan transactions that are not subject to income tax in Panama.

Notary public fees and public registry fees would apply as well, in particular if the facility is secured by one or more mortgages or by the transfer of assets to a trust (fideicomiso).

13 Are there different taxes applicable to loans repayable to lenders in your jurisdiction and loans repayable to lenders in a foreign jurisdiction?

The main difference between a domiciled lender and a lender in a foreign jurisdiction is the form of payment of the income tax, given that lenders in Panama are responsible for paying the income tax due and lenders in a foreign jurisdiction are subject to withholding of income tax by the borrower located in Panama.

Lenders domiciled in Panama are subject to income tax at the general corporate income tax rate of 25 per cent on the entity's net taxable income.

Income tax is reported and paid within three months after the end of each fiscal year.

The ITBMS rate applicable to loan fees (not interest) charged by banks domiciled in Panama is 7 per cent. Local entities pay ITBMS on a monthly basis based on a credit and debit system under which each entity pays the difference between the ITBMS it collected during the immediately preceding month as a result of performing taxable activities and the ITBMS that such entity was charged by third parties during the same period. ITBMS must be reported and paid within the first 15 calendar days of the month immediately following the month for which such ITBMS is to be paid.

On the other hand, the income tax obligations of entities domiciled in foreign jurisdictions ordinarily must be fulfilled through income tax withholdings on payments made by Panamanian entities to such foreign entities. The amount to be withheld would be the applicable corporate income tax rate (currently 25 per cent) over 50 per cent of the taxable amount remitted abroad as payment. As a result, the effective income tax withholding rate would be 12.5 per cent over the gross taxable amount. Lower withholding tax rates may apply if the lender is a tax resident of a state with which Panama have signed a treaty for the avoidance of double taxation.

The income tax withholding mechanism does not apply to foreign entities that have a branch in Panama, because each Panama branch of a foreign entity is deemed to be a Panama tax resident, is assigned a taxpayer identification number upon incorporation and has the obligation to report and pay income tax on its Panama source income.

14 Is your country party to any double taxation treaties that reduce taxes payable by borrowers in respect of loan payments abroad?

As of February 2018, the double taxation treaties with Mexico, Barbados, Qatar, Spain, Luxembourg, the Netherlands, Singapore, France, South Korea, Portugal, Ireland, the Czech Republic, the United Arab Emirates, the United Kingdom, Israel, Vietnam and Italy are in force.

15 Do any financing structures receive favourable tax treatment, such as prepayments of exports?

Under the laws of Panama, the following financings are exempt from taxes:

- financings structured as registered bonds placed with a stock exchange;
- financings by foreign banks to local banks;
- financings by multilateral agencies such as CAF, IDB, IFC, and others;
- financings by foreign governments or their instrumentalities, including export credit agencies;
- financings granted to the Republic of Panama or government entities;
- financings of social housing projects; and
- financings granted to private concessionaires for the construction of the concessioned project.

16 Describe any limitations on interest rates or the ability of lenders to charge default interest under loan agreements.

Under the laws of Panama, there are no limitations on the ability of lenders to charge default interest, except that the payment of such default interest must be agreed by the parties in the loan agreement or sought in judicial proceedings.

17 Are there any restrictions on the payment of interest in kind (PIK), generally involving the collateralisation of interest in the case of a loan?

Under Panamanian law, interests must be stated in terms of currency or money. The only requirement as to payment, is that the payment of such interest be made in the currency of the principal. As such, pursuant to the default rules, an interest payment cannot be satisfied through the incurrence of an additional obligation. Nevertheless, under the principal of freedom of contract, the parties may come to a different contractual arrangement.

18 What restrictions exist upon the ability of a borrower to provide an equity kicker to lenders, that is a conversion feature, warrant or some other right to acquire equity in the borrower?

There are no general restrictions on the acquisition in a borrower's equity. However, these conversion features must be reflected in the borrower's articles of incorporation. We note certain regulatory restrictions on changes in ownership and types of investment may limit or delay a lender's ability to acquire said equity stake. Specifically, certain regulated industries, such as banking and certain telecommunications, may require regulatory approval while others may have notice requirements.

In addition, any regulated banking institution is prohibited from acquiring shares or an interest in any company that is not related to the banking industry if the value of those interests exceeds 25 per cent of the banking institution's total capital fund.

19 Do any limitations exist on the ability of a lender to require a borrower to pay a make whole fee or premium in the event of prepayment of a loan, usually calculated on the expected return on the debt through maturity?

There is no limitation on the ability of a lender to require repayment of a make-whole fee or premium.

20 Describe any restrictions that may apply to the choice of law, for example, whether a choice of New York or English law will be recognised and enforced in your jurisdiction.

Under the laws of Panama, there are no restrictions on the application of the choice of foreign law, except that no provisions of foreign law will be applied by Panamanian courts if such provisions are contrary to the public policy of Panama.

21 Describe generally the requirements for the enforceability of a foreign judgment in your jurisdiction in respect of an outstanding loan.

Under the laws of Panama, any final judgement entered in a foreign court against a borrower for the payment of money in connection with an outstanding loan would be recognised, conclusive and enforceable in the courts of Panama without retrial or reconsideration of the merits of the case, subject to the issuance of a writ of exequatur by the Supreme Court of Panama. In order to issue a writ of exequatur, it is necessary that:

- the applicable foreign court grants reciprocity to the enforcement of judgment of the courts of Panama;
- that such foreign judgment is final (it should not be subject to appeal);
- the borrower is personally (not by mail) served in such an action brought by the foreign court;
- the judgment arises out of a personal action against the applicable borrower;
- the obligation in respect of which the judgment was rendered be lawful in Panama and not contradictory to the public policy of Panama;
- the judgment be properly authenticated by diplomatic or consular officers of Panama or pursuant to the 1961 Hague Convention Abolishing the Requirement of Legalisation of Foreign Public Documents; and
- a copy of the final judgment is translated into Spanish by a translator licensed in Panama.

22 Upon the closing of a loan, what procedural requirements (execution formalities, notarisation, registration, recordation or filing) should be observed to ensure that a loan agreement or related judgment is enforceable in your jurisdiction?

Other than the due execution and delivery of the loan agreement by each of the parties thereto, there are no procedural requirements to be observed under the laws of Panama for the enforceability of the loan agreement. However, if such execution and delivery occurs outside of Panama and the loan agreement is to be used as evidence in the courts of Panama, the signatures of the parties to the loan agreement will need to be authenticated by a Panamanian Consul or pursuant to the 1961 Hague Convention Abolishing the Requirement of Legalisation of Foreign Public Documents.

In addition, certain types of security documents that would secure the debt arising from the applicable loan agreement might need to undergo certain procedural requirements. For example, mortgages are required to be in the form of public deeds and registered with the Panamanian Public Registry, and trust agreements that are not in the form of public deeds are required to be notarised.

23 Does a loan agreement in English need to be translated or locally registered to be enforceable in your jurisdiction?

The enforceability of a loan agreement in Panama does not depend on the language in which such loan agreement is entered into or on any type of registration. However, if a loan agreement originally entered into in a language other than Spanish is to be used as evidence in the courts of Panama, such loan agreements will need to be translated into Spanish by a Panamanian licensed translator.

24 Must a foreign lender be registered in your jurisdiction to enforce any rights under the applicable loan documentation?

Under the laws of Panama, it is not necessary that a foreign bank be registered in Panama in order to enforce any rights under loan documentation.

25 Are foreign lenders treated any differently from local lenders in enforcing loan documentation in the courts of your jurisdiction?

Under the laws of Panama, there is no difference in the treatment given to foreign and local lenders in the enforcement of loan documentation in the courts of Panama.

26 Is consideration required for the enforceability of a contractual obligation or guarantee?

Under the laws of Panama, consideration is required for the formation of any contract and, therefore, also for such contract's enforceability.

27 To enforce a loan in your jurisdiction, need the loan be evidenced by a promissory note or other form of título ejecutivo?

It is not necessary that a loan, to be enforceable in Panama, be evidenced by a promissory note or a título ejecutivo. However, if the loan to be enforced is evidenced by a título ejecutivo, it is entitled to an executory judgment and the enforcement proceedings should take less time. Not all promissory notes constitute título ejecutivo and, therefore, not all promissory notes are useful to shorten the enforcement proceedings.

28 To enforce a guarantee (aval) in your jurisdiction, is it necessary that the guarantee be evidenced by a guarantee agreement or other form of título ejecutivo?

Please note that personal guarantees in Panama are not always in the form of avales. The most common form of personal guarantee in Panama is the fianza. The aval in Panama is a particular type of personal guarantee that is issued by the guarantor signing the applicable guaranteed documents and adding the phrase válido por aval (or an equivalent phrase). Avales are valid only for certain types of negotiable instruments, such as bills of exchange, checks and promissory notes. However, fianzas can be used to guarantee obligations under loan agreements. It is acceptable to have a fianza guarantee the obligations under a loan agreement and have an aval on the promissory note issued in connection with the same loan agreement, as long as, at the time of enforcement, the lender does not seek collecting on both obligations.

29 Are there any restrictions on loans to multiple borrowers or on a guarantee in respect of a loan to an affiliated entity?

Under the laws of Panama, there are no restrictions on simultaneous loans to multiple borrowers. Also, there are no restrictions imposed on guarantors with respect to their providing guarantees to affiliated entities.

30 Can a party grant a secured or unsecured guarantee in respect of a loan to an unaffiliated third party?

Panamanian law permits any person to provide a guarantee to any other person. However, if the guarantor is in the business of providing guarantees (for example, if the guarantor is an insurance company); such a guarantor will be required to comply with all laws and regulations governing such business.

In the absence of an express provision in a borrower's articles of incorporation, the issuance of a guarantee in connection with a third-party loan requires shareholder approval.

31 Is there a distinction between the granting of a security interest and the perfection of a security interest?

There is a distinction under the laws of Panama between the creation of a security interest and the perfection of such security interest. A security interest in Panama is created by agreement between the parties (which agreement, in some cases, may be required by law to comply with certain formalities). At the time of its creation, the security interest is enforceable between the parties thereto. Such security interest, however, is not enforceable against third parties, namely, third parties could share in the applicable collateral, if the perfection formalities have not been complied with.

Under the laws of Panama, different types of collateral may require different types of security interests. In part, this is because the floating charge does not exist in Panama, with the sole (and recent) exception of the possibility of a general pledge with respect to the pledgor's assets if located outside of Panama. As a result, depending on the types of collateral involved in the transaction, the parties may need to execute mortgages on real estate, mortgages on moveable property, pledges of capital stock, assignments of rights and other security documents. Each type of collateral has its own formality for perfection. For example, a pledge of capital stock is perfected by delivery of the share certificates with a stock power in blank, while an assignment of rights is perfected by giving notices to the persons or entities that are subject to the correlative obligations.

32 What is the most common form of granting and perfecting a security interest in movable assets?

As indicated in question 31, the type of security interest will depend on the type of asset. If the applicable movable asset consists of an investment account, a pledge of that account will be necessary, although a new and untested law permits chattel mortgages over rights such as bank accounts. If it consists of equipment, a mortgage of such equipment might be the best approach (unless the borrower is willing to part with the possession of such equipment, in which case a pledge thereof would also be feasible).

33 What is the most common form of granting and perfecting a security interest in real estate?

Under the laws of Panama, the only form of granting and perfecting a security interest in real estate is through a mortgage in the form of a public deed that is subsequently recorded with the Panamanian Public Registry.

34 What is the most common form of granting and perfecting a security interest in receivables and accounts?

With respect to receivables, the form of granting and perfecting a security interest therein is by assigning such receivables to the lender and notifying the payor thereunder that such receivables have been so assigned. With respect to accounts, the form of granting and perfecting a security interest therein is to enter into a pledge agreement between the account holder and the lender and by notifying the account bank that such account has been pledged. A new chattel mortgage law that, at the time of writing, remains untested, would permit a mortgage over receivables and/or bank accounts. However, it is not entirely clear how the mortgage over the bank account would be enforced.

35 Does your jurisdiction recognise the transfer of assets to a trust for the benefit of a lender as a means of granting a security interest in such assets?

Under the laws of Panama, it is possible to transfer assets to a trust (fideicomiso) for the benefit of a lender. Such a structure is used with some frequency in Panama as a means of obtaining collateral for a loan. However, strictly speaking, such a structure should not be deemed to create a security interest. Rather, it constitutes a transfer of legal title to an entity that is under the control of the lender, which entity will then use those assets for the benefit of the lender pursuant to the terms of the trust agreement.

36 Does your jurisdiction recognise the fiduciary transfer of assets (such as an alienação fiduciária) to a lender as a means of granting a security interest in such assets?

Please see question 35.

37 Are there any types of asset that cannot be pledged as collateral under the laws of your jurisdiction?

Although under the laws of Panama certain types of assets either cannot legally be pledged as collateral or can be pledged subject to certain restrictions, most of those types of assets or restrictions are not relevant to standard loan transactions. The most relevant assets that cannot be pledged as collateral are the assets of the Republic of Panama, for which reason any loan to the Republic of Panama needs to be unsecured.

38 Describe any restrictions on enforcement of security. For example, any statutory regime that may stay the enforcement of the security or provide that enforcement is limited to public sale through the courts.

It is well established under the laws of Panama that secured creditors of a debtor can foreclose on collateral. Except perhaps, when a regulated entity such as a bank is intervened or in the event of reorganisation of regular corporate, the ability of the secured party to foreclose on the collateral should not be delayed or affected even if such regulated entity is subject to insolvency proceedings. This fact is not affected by staying orders, even if the bankrupt entity is a regulated entity. In the case

of unregulated entities, the effectiveness of a reorganisation order could delay enforcement of the secured creditor for up to six months.

Under Panama Law, chattel and real property mortgages must be enforced through judicial proceedings (the new chattel mortgage law permits extrajudicial enforcement if the parties so agree in the chattel deed, but the applicable regulations have not been issued at the time of writing). Pledges could be enforced out of judicial proceedings if the pledge agreement so provides and a mechanism for the appraisal of the pledged assets is included in the pledge agreement.

39 Is all unsecured debt treated as *pari passu* in right of payment or may a loan include subordinated or mezzanine credits and, if so, how is the different ranking of credits achieved?

Unsecured debt in Panama is satisfied in accordance with the priority rules under the law. Pursuant to Panamanian Law, certain unsecured liabilities (such as municipal taxes) have priority over general unsecured liabilities. In addition, unsecured liabilities that were incurred at an earlier date have priority over unsecured liabilities that were incurred at a later date. Only to the extent that debt was incurred on the same date is such debt repaid on a pro rata basis.

Nevertheless, and subject to Panama's insolvency laws, a private contractual agreement among creditors to subordinate certain credit obligations to others will be upheld so long as the agreement does not otherwise violate law or public policy.

40 Describe any other relevant legal considerations in connection with loans to a borrower in your jurisdiction.

Lending by foreign banks in Panama is very flexible. Although the business of lending to the general public is regulated, lending to a specific borrower, without being engaged in the business of lending to the general public in Panama, is not regulated. As a result, it is very easy for foreign banks to make loans to Panamanian borrowers. Also, there is no limitation on the interest rate that may be charged by banks on their loans.



Estif Aparicio

Arias, Fábrega & Fábrega

Estif Aparicio is an accomplished partner at Arias, Fabrega & Fabrega. Mr Aparicio has worked on many of the most complex cross-border financial transactions that have taken place in Panama in recent years. He has extensive experience in the areas of securities regulation; banking and finance; mergers, acquisitions and joint ventures; antitrust, trade and competition; and taxation.

From 2004 to 2006, Mr Aparicio worked for the Panamanian government as chief trade negotiator of all bilateral and multilateral free trade agreements. In this role, Mr Aparicio coordinated Panama's participation in the Doha Round of the World Trade Organisation, successfully negotiating free trade agreements with the USA, Singapore and Chile.

Mr Aparicio also worked for Sullivan & Cromwell LLP in New York, participating in capital markets, M&A and project finance transactions.

Mr Aparicio has a law master's from the University of Houston Law Center and a bachelor of Laws from the University of Panama. He is a Fulbright scholar.

Bar admissions: Panama and New York.



Donald Canavaggio

Arias, Fábrega & Fábrega

Donald Patrick Canavaggio joined the firm in 2018, teaming up with the M&A group advising in complex M&A transactions. Mr Canavaggio has proven experience in advising foreign private issuers in the Latin American markets, such as Argentina, Chile, Costa Rica, Mexico and Peru. From 2013 to 2018, Mr Canavaggio worked as an associate for Milbank, Tweed, Hadley & McCloy LLP in New York, focusing on private and public capital markets and securitisation transactions, including high-yield offerings. Mr Canavaggio has a master's of arts in international studies from The Joseph H Lauder Institute for Management and International Studies dual degree programme, the Wharton School and the University of Pennsylvania School of Arts and Sciences, University of Pennsylvania; and a Juris Doctor from University of Pennsylvania Law School. Bar admissions: New York. Mr Canavaggio is fluent in Spanish, English and Portuguese.



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ARIFA Building, 10thFloor
Santa María Business District
PO Box 0816-01098
Panama
Tel: +507 205 7000

Estif Aparicio
estif.aparicio@arifa.com

Donald Canavaggio
dcanavaggio@arifa.com

www.arifa.com