The Legal 500 & The In-House Lawyer
Comparative Legal Guide
Panama: Tax (4th edition)

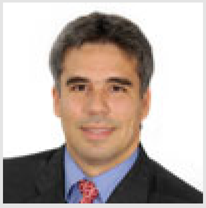
This country-specific Q&A provides an overview to tax laws and regulations that may occur in Panama.

It will cover witholding tax, transfer pricing, the OECD model, GAAR, tax disputes and an overview of the jurisdictional regulatory authorities.

This Q&A is part of the global guide to Tax. For a full list of jurisdictional Q&As visit http://www.inhouselawyer.co.uk/index.php/practice-areas/tax-4th-edition/

Country Author: Arias, Fábrega & Fábrega

The Legal 500



Estif Aparicio, Partner

eaparicio@arifa.com

The Legal 500

Jazmín Solís, Associate

jsolis@arifa.cpom

1. **How often is tax law amended and what are the processes for such amendments?**

Panama tax law are amended almost every five (5) years. Amended of the law is a governmental initiative. For changes in the Panama Tax Code a formal Law approve by the National Assembly is require. There are some other regulations that are amended by the emission of Cabinets Decrees and Executives Decree. Regarding regulations about tax administrative process there are modified by Resolutions issued by the Internal Revenue Office as is known the Panama Tax Administration.

2. What are the principal procedural obligations of a taxpayer, that is, the maintenance of records over what period and how regularly must it file a return or accounts?

Tax payer are oblige to comply with the presentation of tax forms applicable depending the business and operations perform within Panama. Some of the tax obligations are occasional, meaning that are applicable to certain transactions that are not part of the regular business of the taxpayer.

The most common obligations are:

- Filing an annual tax return only if the company performs operations within Panama subject to tax. The annual return is filed ninety (90) days after the ending of the fiscal period (general tax period goes from 1st January to December 31st). Payment of annual income tax must be complete on March 31st at the latest.
- VAT tax form must be file within the next fifteen (15) days after the month that is declare.
- Franchise tax must be paid on an annual base, before January 15 or July 15 depending the date of the company incorporation.

Accountings records are not file with the annual return neither the Financial Statements, nonetheless such information must be kept at hand in case it’s required by the Tax Authority. Accounting records must be maintain for a five (5) years period.

Regulated companies such as Insurance companies, banks, financial institutions, free trade zone companies, are oblige to present to the regulatory agent its audited Financial Statements.

3. Who are the key regulatory authorities? How easy is it to deal with them and how long does it take to resolve standard issues?

Panama tax authority is known as the Internal Revenue Office which is a directorate under the Ministry of Economy and Finance.

The Internal Revenue Office is divided into several departments, including: taxpayers’ assistance, legal advisory, international taxation, transfer pricing, collections, account balances, audit, invoicing, exemptions and refunds. However, all acts must be signed and issued by its

Director.

The caseload of the Tax Authority is heavy and the turnaround time is generally slow. Among the factors that contribute to the slow pace of the tax authority are its centralized organization, a lack of sufficient personnel to meet the demand and the lack of an efficient method to organize and manage the documents. Standard issues could takes as minimum (6) months to be resolve.

4. Are tax disputes capable of adjudication by a court, tribunal or body independent of the tax authority, and how long should a taxpayer expect such proceedings to take?

Resolutions issued by the tax authority can be appealed before the Tax Administrative Tribunal, which is the trial court for tax matters and the final step in the administrative process. This court is an independent body from the tax authority.

To file an appeal before the Tax Administrative Tribunal, the taxpayer has fifteen (15) days following the date that they are notified by the tax authority of the resolution deciding the recourse for review. The judge in charge of the appeal must determine the admissibility of the appeal, confirming that it was filed properly and in a timely manner by a party with legal standing and that the Tribunal has subject matter jurisdiction over the appeal. The admissibility of the appeal must be notified in person to the taxpayer.

Once the recourse for appeal is admitted, the tax authority has five (5) days to file counter evidence and the judge will decide on the admissibility of the evidence submitted by both parties. The judge may require the production of additional evidence by the parties in order to obtain further clarification on the subject matter of the appeal. The judge may also convene a hearing after all evidence has been submitted and evaluated, if it is deemed that further information is required to resolve the matter. Following the analysis of evidence and the hearing, if held, the parties have five (5) days to file written pleas. Finally, the Tribunal must issue its decision.

Based on the above the proceeding before the Tax Court may take as minimum one (1) year.

5. **Are there set dates for payment of tax, provisionally or in arrears, and what happens with amounts of tax in dispute with the regulatory authority?**

There are set dates for the payment of regular taxes. If the payment is done after such days there will be interest and surcharge to cover.

Only the tax debts that are under a payment agreement with the tax authority have set days of payment in order to comply with the articles or clauses of such agreement.

Surcharge of ten (10%) and monthly interest will rise regarding the amount under dispute. Interest will rise until the date the payment is done in case the resolution of the dispute is against the taxpayer.

6. **Is taxpayer data recognised as highly confidential and adequately safeguarded against disclosure to third parties, including other parts of the Government? Is it a signatory (or does it propose to become a signatory) to the Common Reporting Standard? And/or does it maintain (or intend to maintain) a public register of beneficial ownership?**

Tax data is not public information therefore is treated as confidential information. Only in specific cases such as criminal process, family process such information could be obtain but through the requirement of the judges.

Only the taxpayer and its authorized people are able to access to the tax data.

Panama has implemented the Common Reporting Standard (CRS) obligations. On July 31st, 2018 was the final date for filing CRS reports regarding 2017 information.

There is no public registry of beneficial ownership.

7. What are the tests for residence of the main business structures (including transparent entities)?

A company is resident if it is incorporated under Panamanian law or if its central management and control is exercised in Panama.

The following factors are necessary for the determination whether a legal entity is a resident in Panama: (1) meetings of the members of the board of directors, in which decisions that affect the directions, management and administration of the company are take and carry out in Panama, there should be a proof of evidence that the directors were in Panama at that moment of the meeting; (2) business activities, commercial or support activities to other companies are carried out from Panama, regardless of the source of income. In order to provide evidence to the tax authority that the company is carrying out activities within and from Panama, it must be necessary to present the following information:

a. That the company has an office or a place where the activities are perform (own or by a lease agreement)

b. That the company have employees registered in the Panama Social Security, or people in Panama that perform the company's operation in the country.

c. Evidence that in and from Panama some activities are perform even though this activities generates its effects abroad.

Companies with no operation within Panama and with no substance will not be allow to obtain the tax residency.

8. Have you found the policing of cross border transactions within an international group to be a target of the tax authorities' attention and in what ways?

Cross border transactions are targets by the tax authorities as usually involves multinational companies and taxpayers under the category of big contributors. Taxpayer under this category are more exposed to tax audits by the authorities.

In cross border transactions tax authority review if the capital gain tax rules had been applied in addition that stamp taxes had been covered.

9. Is there a CFC or Thin Cap regime? Is there a transfer pricing regime and is it possible to obtain an advance pricing agreement?

There are no CFC or Thin Cap rules in Panama.

Transfer Pricing regulations had been enacted since 2010. At the moment there are only applicable to transactions with related parties abroad and to those transactions that affects income, cost and expenses for the determination of the taxable base for income tax purposes.

In addition, there are no advance pricing agreement for transfer pricing matters. There is an initiative of establishing such agreements but had not been validated by the Panama Tax Authority.

10. Is there a general anti-avoidance rule (GAAR) and, if so, in your experience, how would you describe its application by the tax authority? Eg is the enforcement of the GAAR commonly litigated, is it raised by tax authorities in negotiations only etc?

There are no general anti-avoidance rule (GAAR) regulations in our tax code.

11. Have any of the OECD BEPS recommendations been implemented or are any planned to be implemented and if so, which ones?

Panama joined the Inclusive Framework of the Base Erosion and Profit Shifting (BEPS) Project of the Organization for Co-operation and Economic Development (OECD) on 31 October 2016.

The Inclusive Framework currently consists of 87 member jurisdictions, all of which will have a chance to intervene on equal terms in all of the CFA's meetings and its work teams on the BEPS project.

Panama as a member of the Inclusive Framework has committed to implementing the four minimum BEPS standards: (i) harmful tax practices (Action 5), (ii) treaty abuse (Action 6), (iii) country-by-country reporting (Action 13) and (iv) dispute resolutions (Action 14).

12. In your view, how has BEPS impacted on the government's tax policies?

Panama has acquired a short-term commitment to implement the minimum requirements under BEPS, this has led to various implementation changes such as, creation of tools for CRS reports, internal regulations for the exchange of information under CRS, modification in the transfer pricing form according to action 13 of BEPS.

In accordance with BEPS implementation, by the end of 2018 Panama has change some of its special tax regime, such as, Panama Pacific and Multinational Headquarters regime. Companies that were registered in these regimes were mainly exempt of income tax among other taxes, with changes in 2018, there are now obliged to pay income tax at a reduce tax rate and are subject to transfer pricing regulations.

Tax policies adopted for Panamanian Government is to comply with and accept the guidelines of the BEPS as part of the local legal system with ways to support the elimination of tax evasion.

13. Does the tax system broadly follow the recognised OECD Model? Does it have taxation of; a) business profits, b) employment income and pensions, c) VAT (or other indirect tax), d) savings income and royalties, e) income from land, f) capital gains, g) stamp and/or capital duties? If so, what are the current rates and are they flat or graduated?

Panama adopted mostly the OECD model for Double Taxation Treaties signed. In addition

Transfer Pricing Rules incorporate the OECD guides as part of our local regulation for Transfer Pricing matters.

a) Business Profits

A real estate tax is levied on Panamanian-situs real property at rates ranging from 0.60% to 1.00%. Real estates that are registered as family heritage or the principal home of an individual, will be exempt of paying this tax for the first US$120,000.00 of the register value of the property, in case the value is higher than US$120,000.00, then the excess will pay property tax ranging from 0.50% to 0.70%.

b) Employment income and pensions

Individuals are taxed at the following rates:

If the net taxable income is:	**Tax will be:**
Up to B/.11,000.00	0%
Over B/.11,000.00 up to B/.50,000.00	15% for income exceeding B/.11,000.000 up to B/.50,000.00
Over B/.50,000.00	Will pay B/.5,850.00 for the first B/.50,000.00 and a 25% on excess of B/.50,000.00

Employers are legally required to withhold from employees’ compensation their portion of social security contribution, income tax and educational tax. These amounts are paid on a monthly basis to the Social Security Administration, along with the corresponding employers’ contributions.

Employees pay 9.00% of their salaries for social security and 1.25% for educational tax. Employers contribute 12.00% of the salaries paid to the employees and 1.50% for educational tax.

c) VAT

The tax is levied at the flat rate of 7% (10% in the case of alcoholic beverages and hotel services; a further 15% rate is levied for tobacco related products) on the invoice value of the sale, lease (except as described above) or transfer of any good or services with the exception of intangibles. Foodstuffs, medicines and medical services, crude oil and its by-products, negotiable instruments, and other goods are specifically exempted from this tax.

The tax is paid at the moment the goods or services are invoiced or delivered / rendered, whatever happens first. As every other VAT it is withheld by the seller, lessor or transferor, who must remit the net amounts between what was paid by him (input VAT) and what has been collected by him (output VAT) on a monthly basis. Imported goods pay this tax at the moment of clearing customs.

d) Royalty Payments

Royalty payments are subject to a flat rate of 12.5% if done to non-residents in Panama. In case of residents will be subject to tax at the general flat rate of 25%.

There is no saving incomes as these kind of incomes are exempt of taxes in Panama.

e) Property Tax

A real estate tax is levied on Panamanian-situs real property at rates ranging from 1.75% to 2.1%. As from January 2019, real estate tax rates will be reduce to 0.60% to 1.00%.

f) Capital Gain Tax

Capital gains derived from the sale of securities and negotiable instruments are subject to a 10% tax. The purchaser must withhold 5% of the sales price as an advance payment of income tax and remit that amount to the tax authorities.

Gains from the sale or transfer of real property are considered capital gains. If the transaction giving rise to the gains is part of the taxpayer's ordinary business, the gains are subject to the specific corporate tax rates; if the transaction is not part of the taxpayer's ordinary business activities, the gains are taxed at a reduced rate of 10%. However, in the latter case, the seller must paid a 3% of the higher of the purchase price or the rateable value of the property as an advance payment of tax.

g) Stamp Duties

Any document evidencing the transfer of goods to Panama or rendering of services in Panama not subject to VAT are oblige to pay the stamp tax. In addition any contract through which a transaction that generates taxable income in Panama, will be subject to stamp tax also. As a rule of thumb, this tax amounts to 10 cents for each US$100 or fraction documented in the transaction. However, revenue transaction evidencing export and re-export of goods is not subject to stamp tax. Contracts or transactions that are consummated abroad will be exempt of stamp tax unless the document will be presented before a Panamanian Court, in which case the tax must be pay.

h) Commercial License Tax

The tax is a flat rate of 2% apply to the net worth of the business, with a minimum CAP of US$100 and up to a maximum CAP of US$60,000. Companies in special regimes will pay a flat rate of 0.5% apply to the net worth with a maximum CAP of US$50,000.

For the computation of net worth, the amounts due to foreign affiliates may not be considered in the liabilities of the business. Assets not used for activities requiring an Operation Notice are not included in this taxable base. Operation Notice taxes (formerly known as commercial and industrial license taxes) are deductible expenses for income tax purposes.

14. Is the charge to business tax levied on, broadly, the revenue profits of a business as computed according to the principles of commercial accountancy?

Taxable income includes all income derived from business activities in Panama less expenses incurred wholly and exclusively in the production of assessable income or the conservation of its source.

Panama has incorporated as part of its internal regulations the application of the NIIF as accounting standards norms. For tax purposes is mandatory to apply the accrued system to the registration of income, cost and expenses.

15. Are different vehicles for carrying on business, such as companies, partnerships, trusts, etc, recognised as taxable entities? What entities are transparent for tax purposes and

why are they used?

Vehicles for performing operations in Panama are the corporation, Limited Liability Company, limited liability partnership, general partnership, joint venture and branch of a foreign corporation.

Tax treatment for all the vehicles listed above is the same under Panama Tax Regulations. Nonetheless corporations are the most commonly used vehicle do to the fact that shareholders maintain as private information.

Depending on the jurisdiction where the holding is located, it might be possible that the Panamanian company incorporated is a limited liability company as is the transparent type of vehicle which shows the owners or shareholder information.

16. Is liability to business taxation based upon a concept of fiscal residence or registration? If so what are the tests?

Liability to business taxation is based upon if the income have been generated and obtain within the Republic of Panama, without the consideration of where the contract had been signed or the payment had been done.

Registration is mandatory for all companies incorporated in Panama, this do not trigger any filing or tax obligation.

17. Are there any special taxation regimes, such as enterprise zones or favourable tax regimes for financial services or co-ordination centres, etc?

Panama has various investment incentives regimes that provide lower tax rates or exemptions. The following are the special regimes in our jurisdiction.

- Panama Pacific Special Economic Area: The Panama-Pacific Special Economic Area has been designed to be the Business Center of the Americas. It is located 40 minutes from Tocumen International airport, 10 minutes from the port of containers at the Pacific, 1 hour form the Colon Free Zone and 20 minutes from Panama City.

Some of the benefits the Special Economic Are Panama-Pacific offers are: Fiscal, immigration and labor incentives; simplified procedures for installation and operation, training for employees and special customs regimen.

Offshore services have been eliminated from the full exempted activities in this regime. Now Panama Pacific companies are allowed to perform administrative services that are subject to income tax at the reduced rate of 5%. Regarding indirect tax, Panama Pacific companies are obliged to pay VAT for services rendered by Panamanian companies that are not registered in the Special Economic Area of Panama Pacific.

- Colon Free Trade Zone: Tax laws which apply to Panamanian source income do not apply to Free Zone operations. Income generated by re-exporting activities are exempted from the payment of income tax. Companies operating in the Colon Free Trade Zone, and from any other free trade area, are subject to a fixed dividend tax rate of 5%, applicable on the distribution of profits paid out from export and re-export transaction, as well as on the distribution of domestic income. Entities operating on this, or any other free zone, must have financial statements prepared in accordance with International Financial Accounting Standards and countersigned by a Panamanian Certified Public Accountant, for fiscal years starting after January 1st, 1997, and must file annual tax returns.

- Free Trade Zones: With the purposes of promoting investment and encouraging scientific, technologic, economic, and social development, Law 32 of April 5, 2011, implemented a new simplified regime for companies operating within established free trade zones. This law applies to both developers of the free trade zones, and companies within this areas, including manufacturers, service companies, technology companies, educational and research centers, logistic companies, and environmental services companies.

  Companies registered in the free trade zone regime are subject to: Dividend tax of 5% (they will only pay 2% of retained earnings tax if the business does not distributes dividends), annual tax based on 0.5% of the enterprise's capital, and a selective tax on the consumption of some goods and services. Funding provided by financial institutions will be also subject to a 1% surcharge, referred as FECI (Special Compensation Fund for Interest).

- Petroleum Free Zones: companies doing business in this special zone will be granted with the same fiscal treatment as the Colon Free Trade Zone entities.

- Call Centers Regime: CALL-CENTERS, duly registered with the *Autoridad Nacional de los Servicios Públicos ("ASEP"), will obtain* the same benefits conferred to Free Trade Zones under Ley 32 of April 5, 2011.

  Call-Centers performing business with clients not located in Panama and subject to their approval by the Public Utilities' Regulating Office and by Panama's Ministry of Commerce and Industry are exempted from income tax on income derived by attending clients not located in Panama.

  Additionally VAT (ITBMS) is exempted on goods disposed within the premises and on the services performed by the call-center to clients not located in the Republic of Panama Call Centers are also exempted from tariffs on the importation of goods needed for their operations.

- Multinational Headquarters Regime known in Spanish as Sede de Empresas Multinacionales ("SEM"): the regime provides full exemption on dividend and net worth tax. In addition, that SEM companies are not obliged to use fiscal printers for issuing their invoices. Export services provided to non-residents are exempt of VAT. Since 2019 SEM companies must now pay a reduced 5% income tax rate (the standard rate is 25%) on the net taxable income derived from the provision of the services. Taxes over income derived from services provided to Panamanian taxpayers will be paid via a 5% withholding made by the Panamanian taxpayer. SEM companies must apply transfer pricing rules to the services provided the other members of their economic group (residents and non-residents).

  SEM entities are allowed to provide back office services to companies that are part of the same economic group of the SEM, meaning that SEM entities are no permitted to offer services to third parties.

  Foreign employees working in Panama for an MHQ are exempt from income tax on their wages and other remuneration that is not paid by the MHQ.

The Panama Pacific Special Economic Area, Call Centers Regime and the SEM Regime are under evaluation by the Panama Government as part of the BEPS compromise is to review those special regimes that might be harmful for tax purposes. Before the end of 2018 year, this special regime must be amended in order to accomplish with BEPS and OECD rules.

18. **Are there any particular tax regimes applicable to intellectual property, such as patent box?**

There are no specific tax regimes for intellectual property.

19. **Is fiscal consolidation employed or a recognition of groups of corporates for tax purposes and are there any jurisdictional limitations on what can constitute a group for tax purposes? Is a group contribution system employed or how can losses be relieved across group companies otherwise?**

Group consolidations for tax purposes is not applicable in Panama.

20. **Are there any withholding taxes?**

Payments made to beneficiaries not resident in the Republic of Panama are subject to withholding tax, on 50% of the amount invoiced, at the applicable corporate income tax rate 25%. WHT will apply when the payment relates to services rendered in and abroad Panama, interest and income from intellectual property rights, royalties, know-how and alike.

No WHT will apply on service, royalty o know how payments, if the local entity considers that the expense incurred is not deductible for tax purposes, or if the foreign entity obtains a Panamanian taxpayer identification number and directly pays the tax.

Dividends – Dividends paid to a non-resident on nominal shares are subject to a 5% or 10% withholding tax, depending on the source of the dividends; the rate is 20% for bearer shares.

Interest – Interest paid to a non-resident is subject to a 12.5% (50% of the interest is subject to the general 25% corporate tax rate) withholding tax.

Royalties – Royalty payments made to a non-resident are subject to a 12.5% (50% of the general 25% rate) withholding tax if the payments benefit a Panamanian resident or if the expense has been deducted in Panama.

Service fees – Services paid to a non-resident are subject to a 12.5% withholding tax (50% of the general 25% rate).

Branch remittance tax – A branch of a foreign corporation must pay 10% of its after-tax income as a dividend tax in addition to the corporate income tax.

21. Are there any recognised environmental taxes payable by businesses?

There are no environmental taxes in the Panama Tax Code.

22. Is dividend income received from resident and/or non-resident companies exempt from tax? If not, how is it taxed?

All companies who have a Notice of Operations, an Operations Code to operate in the Colon Free Zone (CFZ) or which operate in a petroleum free zone or any other duty free or special zone, or generate taxable incomes in the Republic of Panama will be subject to the payment of these taxes, according to the following rules:

Companies who have a Notice of Operations, or generate taxable incomes in the Republic of Panama.

- **10%** - Profits from Panamanian source.
- **5%** - Profits from foreign source or from exports, and from exempt income from paragraphs **f** and **l** of article 708 of the Tax Code.

Companies registered in special tax regimes, such as Colon Free Zone, Panama Pacific Regime, Petroleum Free Zone, are oblige to pay dividend tax at the rate of 5% without the consideration of the source of the income to be distribute.

When an individual distributes dividends or participation quotas it should first use up the income from Panamanian source, or local or internal operations, before distributing dividends or participation quotas from income coming from foreign operations or exports and from local income exempt from the Income Tax, as foreseen in the Tax Code, accordingly.

Subsequent distribution of dividends is not subject to dividend tax as long as the tax has been paid at the source.

The distribution of dividends or participation quotas to those companies that do not require a Notice of Operations or do not generate taxable income in Panama is excluded from the concept of local income.

23. If you were advising an international group seeking to re-locate activities from the UK in anticipation of Brexit, what are the advantages and disadvantages offered?

Tax advantage in Panama are related with the territorial system. Therefore only income that is generate locally is subject to tax, any profits obtain from abroad are not subject to taxation under Panama Tax Regulations.

In addition to the above there are several tax regimes that provide tax benefits in addition to the provision of labor and custom duties incentives, such as the SEM regime that allow the Multinational Group to have a back office center within Panama exempt of taxes in addition that provide the benefits of having foreign individuals working for this special entity without the implications of labor limitations, meaning that the company is able to have more than 10% of foreign employees. In addition there are savings related to social security contributions do the exemption that is granted for foreign individuals working for the SEM Company.

Panama is also known as the HUB of the Americas providing the facilities for connections, communications in order to establish the LATAM center of business in our country.

Finally Panama is taking all the necessary steps to be a cooperative country as recommended and require by the OECD, GAFI among other international organizations.