

International Assignment Services

Taxation of International Assignees Country – Panama

*Human
Resource Services*

*International
Assignment
Taxation Folio*



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Additional Country Folios can be located at the following website: www.pwc.com/ias/folios

Introduction – International assignees working in the Republic of Panama

This booklet was prepared by PricewaterhouseCoopers to provide foreign nationals planning to work in the Republic of Panama with a general background of Panama tax law and other relevant issues. It reflects tax law and practice as of January 2011.

This booklet traces a Panamanian assignment through seven steps. These steps address the specifics of what to do before you arrive in the Republic of Panama, what to do when you are here, and what to do before you move out of the Republic of Panama. Familiarity with these issues will make your assignment easier and more enjoyable.

This booklet is not intended to be a comprehensive and exhaustive study of Panama's tax law, but should be used as a guide as you prepare for your assignment in the Republic of Panama. We should advise you against making any decisions without first seeking professional advice, as laws and interpretations in the Republic of Panama are still, to some extent, subject to relatively frequent changes without much prior notice. This booklet will give you the preliminary information you can use to define the issues that are relevant for your situation.

If we can be of assistance please contact us, a list of contacts can be found in Appendix C.

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Menu

Step 1 – Understanding basic principles

The scope of Panamanian taxation

1. Taxable income produced from any source within the territory of Panama, regardless of where it is received, is subject to income tax. Income tax is levied only upon net income derived from operations within Panama, by individuals and corporations, except those considered as nontaxable or exempt by law, in accordance to the corporate and personal income tax rates.

In this sense, income derived from activities performed abroad Panama is not considered taxable, although it may be subject to dividend tax.

The tax year

2. For purpose of the annual tax, fiscal period begins on January 1st and ends as of December 31st of each year, so filing must be completed on a calendar year basis.

Determination of residency

3. The term residency refers to a person physically located and generating income in Panama, for more than 183 days, being continued or rollover in the same fiscal year. Contrariwise, non residency refers to persons located in Panama and generating income, for less than 183 (continued or rollover in the same fiscal year).
4. Nonresidents are taxed on gross income produced from Panamanian sources at a rate of 15%, plus a 2.75% Educational Insurance Tax. Taxes arising from Panamanian salaries will be withheld by the payer, if all compensation is subject to withholding and all taxes are withheld by employer, the individual is not required to file an annual income tax return.
5. Residents are taxed on net taxable income (gross income – deductible allowances) earned from Panamanian sources, in accordance to the new rates for the calculation of income tax established by the Law No. 8 of March 15th of 2010.

For residents, the Educational Insurance Tax is assessed at the rate of 1.25% on salaries and wages paid by the employer.

6. Both nonresidents as well as residents will be subject to pay the Social Security Tax which is assessed at a rate of 8.0% wages and other compensation paid. Social Security contribution will be increase up to 9% in 2011 and 9.75% in 2013.

Method of calculating income tax

7. There are two different ways to calculate the income tax, one is when the person is an employee, in which the employer is responsible to withhold the corresponding taxes in attention to a progressive rates, and the other one is when the person is an independent contractor, a person with more than one job or an employee that has another kind of income, distinct from the employment, in which case the filing of an annual income tax return is required.

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8. Panamanian laws establishes in that case when the taxpayer has only one source of income related to his employment, he may file an annual income tax return. In the annual income tax return the taxpayer may deduct any expenses incurred within the fiscal year and that are directly related to the generation of income or its conservancy. The outcome after applicable deductions will constitute the annual tax base.
 9. It is important to mention that employment income will not be subject to deductions incurred in order to produce income or to preserve it, no losses arising from capital, rental or other sources will be allowed against employment income. The tax deductions may proceed only in case of freelance income.
 10. Progressive tax rates are then applicable to the annual income obtained in order to determine the taxes the employee must pay (See Appendix A for applicable rates).

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Step 2 – Understanding Panama's tax system

Taxable income

11. Taxable income under the Panamanian Income Taxes includes the following:
 - Income from dependent services (employment);
 - Income from independent services (independent contractor);
 - Income from dividends;
 - Income on the sale of real estate; and
 - Other income.

Employment income

12. This group of income includes income and related remuneration from employment. Taxable remuneration from employment includes all remuneration, whether monetary or non-monetary, and benefits in kind given to or provided for an employee or family member. The location of payment of salaries, bonuses etc., will not affect the tax treatment.

Income from independent services

13. Independent consultants and other self-employed individuals will nevertheless be taxed for the activities that generate income within the Republic of Panama, relating to income derived from services rendered in the Republic of Panama. Broadly, expenditure required to 'attain, secure, and maintain' the taxpayer's income, as well as the services rendered abroad to Panamanian tax residents that take the expense as deductible.

Deductible expenses are the costs and expenses incurred for the generation of Panamanian source income or its conservancy, anytime they are duly supported and the withholding at source has been made if applicable.

Income from dividends

14. Shareholders pay dividend tax at a rate of 10% through a definitive withholding by the corporation that distributes the dividend. Dividends on bearer shares are subject to a 20% dividend tax. Withholding tax on equity dividends is applied to residents and nonresidents on the same grounds.

The entity paying the income to the individual will withhold the corresponding taxes, and this will constitute the final tax liability on such income.

15. Dividends received from foreign sources or derived from entities located abroad (not performing activities within the Panamanian territory) are not subject to payment of taxes in Panama.

Income from the sale of real estate

16. The sale of real estate located in Panama is subject to income tax and transfer of property tax. Neither the losses nor the gains related to the sale of real estate is considered for determining income tax caused during the year derived from the other income obtained by the tax resident.

17. The property transfer tax is 2% on the tax base of whichever results higher from: the sale Price of property or the value of the property registered at the Public Registry plus a surcharge of 5% for each twelve (12) months period of ownership of the property.
18. Since the year 2009, the law 49 established that income tax will be withheld by the buyer at a rate of 3% on the gross income of the transaction for those who do not sell more than 10 properties within a tax year (not frequent seller). However, the seller has the right to prepare a special tax return to calculate the income at a 10% rate over the gains, or what is the same, over the outcome resulting from the cadastral value (value at the Property Registry), or the value according to accounting records (whichever less) and the sale price; if the difference between the withholding on the gross and the tax paid on the net amount results in a favorable amount to the taxpayer, he might request for the return of amounts paid in excess.
19. If the taxpayer sells more than ten (10) properties within a tax year (frequent seller), the capital gain on the transfer of properties will be subject to payment besides of the property transfer tax payment, to pay the corresponding tax at a rate of 3.75% over the cadastral value or the price of the transaction (whichever results higher).

Other income

20. The following are considered foreign source income as they are not produced within Panama, therefore is not taxable under the Panamanian Income Tax Law the following:
 - Gains on sales of shares and securities of Panamanian companies exclusively engaged in activities outside Panama;
 - Income for leasing contracts from properties located abroad;
 - Income from offshore or foreign trust, services rendered outside of Panama; and
 - Income not produced within the Panamanian territory.

There are also items exempt from income tax in Panama, such as:

- Interest and gains on sales of government securities;
- Gains on sales of stocks, bonds and other securities issued by entities registered with the National Securities Commission; and
- Interest on saving accounts and short or long term deposits maintained with banks.

Taxation of employment income

21. Panamanian Tax laws in respect to income are strictly territorial. Consequently, foreigners and nationals are taxed only on income produced within Panama by the same rules, regardless of where payment comes from, although there are differences between resident and nonresident taxpayers.
22. A nonresident foreigner staying in Panama for 183 days or less is subject to income tax, educational insurance and social security when working as an employee; the taxes will be calculated according to a combined income tax rate. This will apply for employees of national or foreign companies.
23. When the person is an independent contractor and stays for less than 183 days, the tax rate will be of 15% on the income tax.
24. The employee or the independent contractor will also be subject to the educational insurance tax which is for the non residents of 2.75% and for residents 1.25%.

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25. Only employees (nonresidents or residents), are subject to pay the Social Security which is assessed at a rate of 9.0% on wages and other compensation paid.

Territoriality principle

26. Nonresidents as well as residents will only be tax on the income generated within the Republic of Panama or derived from services rendered regardless of where the payment is received.

Benefits in kind

27. Taxable income includes employment income and benefits in kind, such as housing, taxes, school, car allowances, insurance, etc. According to the law it is mandatory to apply WHT over the fringe benefits paid regarding income tax as well as social security contributions.

Transportation and lodging

28. Transportation and lodging expenses will be deductible whether incurred locally or abroad if they are related to the activities performed by the company. The allowable expenses normally include travel and lodging for employees based in one point in Panama to another place in Panama or to a place abroad in pursuit of business. Deductibility for travel and lodging expenses in Panama of expatriates living in Panama is nondeductible.
29. Excessive or unrelated expenses can be objected by the tax authorities.

Tax deductions

30. Resident taxpayers will be subject to the normal tax rates on their net income arising from Panamanian sources. Panamanian legislation allows the following personal allowances and deductions to be deducted from resident taxpayer's taxable income:
- Married couples filing a jointly tax return are entitled to an annual deduction of US\$800;
 - Medical Expenses incurred on his behalf or for his dependents within the Republic of Panama. It will be necessary to prove through invoices or other documentation the expenses incurred, including the hospitalization and medical attention insurance premium;
 - Interests paid on mortgage loans for home improvements on residents located in Panama up to US\$ 15,000 per year;
 - Interest paid on loans for education;
 - Donations to local educational and charitable institutions if these institutions have been duly authorized by the tax administration to received such donations up to an amount of US\$50,000 per year;
 - Contributions to private retirement funds which are incorporated in accordance to Law No. 1 of 1984, up to the 10% of the annual gross income of the taxpayer or up to a maximum annual amount of USD15,000.00, whichever results less.

Company cars

31. In accordance with Panamanian law, the cost of providing a company car to an employee is considered as taxable income for the individual if the local entity deducts the expense related with depreciation, maintenance, insurances, etc. Law establishes that 70% of expenses will be considered as taxable income to the employee.

For social security contributions, the same rule regarding the 70% of taxability is applicable.

If employer don't deduct car's cost employee benefit is considered non taxable.

Housing benefit

32. This benefit is taxable if the employee is provided with an allowance for housing or a reimbursement of his/her housing costs.

Representative allowances

33. Employers often split the salary of their employees with a representation allowance. This payment is 100% deductible for the company. This amount is included in the employee's taxable income. However, it is subject to a special WHT rate of 10%, if payment of this retribution goes up to an annual amount of USD25,000. In case that the amounts paid as representative allowances exceeds USD25,000, USD2,500 will be payable for the first USD25,000, and exceeding amounts will be charged at a rate of 15%.
34. The split portion of the representation allowances might not exceed 100% of the salary split portion in accordance to the recent amendment of our Tax Law by means of Executive Decree 98 of 2010. It also establishes that the representation allowances shall be paid to high profile or trustworthy employees, although this concept is not very well defined.

The representation allowance is subject to social security contributions over 100% of the payment.

The employee that receives this type of compensation will have the choice to file an annual income tax return.

Christmas bonus

35. Under Panamanian Social Security law, some special Christmas bonuses are exempt from social security and educational insurance taxes if do not exceed a month of salary.

Payroll withholding tax

36. Income tax must be withheld by the employer on a monthly basis from employment income for the following individuals:
 - All employees of a Panamanian or foreign company generating income in Panama, including expatriates assigned to work at the company; and
 - All employees of a permanent establishment in Panama.
37. Since 2006, foreigners that hold a Special Temporary Visitor VISA or a Multiregional Headquarter Visa (SEM visa) will be exempted to pay income tax and Social Security Contributions if its payments come directly from its Head Quarter located abroad and company activities in Panama has an international character.
38. The tax will be withheld at source by the employer and should be paid to the appropriate tax authorities. The employer is obliged to operate a payroll and is responsible for tax registration and for correct payment of taxes.
39. If payroll withholding is not performed – for instance if the expatriate works at a deemed permanent establishment – then the employee is personally responsible for reporting that part of his employment

income which is subject to Panamanian tax, by means of an annual income tax return, and for making payments of taxes due.

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Step 3 – What to do before you arrive in the Republic of Panama

Entry and departure formalities

40. A valid passport is necessary for expatriates entering the Republic of Panama. The Panama Republic has signed agreements with some countries eliminating the need for entry visas for passport holders from these countries.
41. Expatriates who do require a visa to enter the Republic of Panama are obliged to provide it to the Panamanian Consulates located all over the world. They must give details of their time of arrival, place and length of their stay in Panama.
42. Expatriates who don't need a visa or have a tourist visa are allowed to stay for ninety days in the Panamanian territory, but if more time is required, they can ask for an extension that will be given for sixty more days. Foreigners are not allowed to work in Panama without a work permit and without the previous registration at the Social Security Office with few exemptions on certain types of migratory permits (SEM and Temporary Resident).

Work permit

43. All foreigners who intend to work in Panama must obtain a work permit. This requirement strictly applies even for short term assignments to Panama.
44. The work permit is not issued with a tourist visa, the foreigner should ask for another type of migratory service (technician or 10% employer visa). Employees must ask for the work permit after their arrival to Panama and these permits must be renewed annually.
45. In order to obtain a work permit, a formal request from your employer and confirmation of your employer's existence must be submitted to the labor office.
46. The formal request must be filed by you and your employer, who must submit some legal documents to the labor authorities.
47. In Panama at least 90% percent of the workers, in every commercial or industrial corporation must be Panamanian or certain specified foreigners, as foreigners married with Panamanians or foreigners with ten years of residency in Panama. Ninety percent of the total wages and salaries must be paid to Panamanians and specified foreigners. In the specific case of technicians is allowed up to a maximum of 15% of foreign personnel.

Employment contract

48. As a foreign national working in the Republic of Panama, you are required to have a specific employment contract, which must determine the terms and conditions set down by your employer for the duration of your stay in Panama.

It is important to mention that the work permit is only handled when submitting some documents to the Labor authorities, including the employment contract.

Importing personal possessions

- 49. You are allowed to import your personal possessions up to US\$1,250 (custom value); of this amount US\$500 is duty-free, and the remaining US\$750 is taxed with an import duty of 20% plus the value added tax, which is 7%.
- 50. 50 Foreigners coming into Panama with an international company executive migratory permit are duty free when importing their personal possessions. The executive can only ask for the exemption when having the corresponding permit as well as the temporary residence.
- 51. The foreigner must ask, in writing, for the exemption to the customs office, which will provide a form regarding the import of the goods; the form should be kept, as it will be required when re-exporting the possessions at the end of the assignment.

Importing your car

- 52. If you import your car for personal use you will have to pay import duty tax established by the law. There is no special treatment for foreigners.

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Step 4 – What to do when you arrive in the Republic of Panama

Residence permits

53. When arriving to Panama with or without a visa (depending on the country you are coming from), foreigners are allowed to obtain a residence permit in the country for one or two years (depending on the type of the permit) if they complete all requirements that the Migration authorities ask for.
54. Once the foreigner enters the country, he must register at the Foreigners Section of the National Migratory Service Office, where a unique identification number will be granted to the foreigner which will be used for migratory affairs as this identification number, will be as well its social security number and its tax payer number at the IRS Office.
55. After the expiration of the migratory permit, it has to be renewed for the same consecutive amount of time up to a maximum of six years, with a previous request on behalf of the foreigner, jointly with all the other requirements established by the law for each type of migratory permit. The National Migratory Services Office will issue then, if necessary, a Permanent Stay Resolution with the corresponding document that proves this.

Tax registration

56. If you are employed by a Panamanian employer it is possible that you might need to file an annual income tax return. The tax authorities require that you obtain a tax number (8-NT) in order to be included in the Ministry of Economy and Finance database. The procedure to obtain this 8-NT is the following: you must file out a Tax Payer Form and accompany it with your passport, immigration identification, social security slip, works and salary letter, certificate of marriage, water, telephone, or electricity bill.
57. The registration for tax purposes is important not only to satisfy the legal regulation but also due to the fact that upon tax registration, you will be allocated a registration number (8-NT). This number must be used in any communication with the Panamanian tax authorities. This number will also be used for the obtainment of a good standing certificate from the Tax Administration needed for the renewal of the migratory permit.

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Step 5 – What to do at the end of the year

Tax return submissions

58. If an employee receives income derived from one source income being employment and representative allowances, he might have the choice to file an annual income tax return or not.
59. A foreign individual will be required to submit a tax return if he stays in the Republic of Panama for more than 183 days in the tax year, if the employee receives as part of compensation benefits in kind or if they are employed by a foreign firm which has a permanent establishment in the Republic of Panama.
60. The tax returns must be filed by March 15th following the end of the tax year in which the income arises. Husbands and wives can file either jointly or independent returns.

Applying for an extension

61. The deadlines for filing your tax return may be extended to May 15th, if the taxpayers ask for the extension before March 15th.

Paying your tax liability

62. The position outlined below assume that the tax liability is not regarded as completely settled by payroll withholding.
63. Generally, taxes are payable in advance.
64. However, for the year in which you arrive, the full tax liability is due on the day of submission of your first tax return because there was no last known tax liability and therefore no tax advances were paid.
65. If taxes are caused, payment must be made by March 31st, at the latest, in order to avoid interests. These payments must be submitted to a specific Bank with a special slip indicating that payment of taxes was made. If taxpayers make a claim for an extension, the extension works only for filing and not for payment. Payment out of time will trigger interest (11% annual average rate).

Advance tax payments

66. After you as independent contractor submit your first tax return, you are required to pay tax advances in respect of the following year's tax liabilities. The amount of advances depends on the amount of your previous year's tax liability. The advances must be paid in three different installments after the original payment date of March 31st; which are June 30th, September 30th, and December 31st. Payments made after these dates will trigger interests. If you are an employee receiving salary and other employer payment, no tax in advance payment are required.
67. You should be aware that advances would be treated as advances of your liability for the year in which they are paid. If the tax return for the first year is filed in March of the second year, and the tax liability requires quarterly payments, then a payment must be done before March 31. Then on June 30th, September 30th and December 31st advances must be paid for the tax that will be caused because of the income received on the current year.

Fines & penalties

- 68. The tax authorities may levy a fine for late submission of your tax return. The fine is determined by the tax authorities, in practice, the authorities levy a penalty ranging from US\$100 to US\$500.
- 69. There are also interests for late payment of your tax liability. The penalty is around to 1% of your tax liability for each month of late payment. The 2011 interest rate is 0.84% per month.

Tax overpayment

- 70. A taxes overpayment can be offset by the tax administrator against other tax arrears, if any, and the balance can be credited against future tax liability. However, where there are no tax arrears, the taxpayer can apply for a refund of overpaid tax. In that event, the overpaid can be returned to the taxpayer.

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Step 6 – What to do when you leave the Republic of Panama

Informing the financial authority

71. Both, the Tax Administration as well as the Migration Authority need to be advised within 30 days after the termination of your assignment in Panama and that you have left the Republic of Panama permanently as an employee. This will release you from any obligation to pay further tax advances and fines.

Filing your tax return

72. You may submit your final tax return before your departure from the Republic of Panama. Otherwise your tax return should be prepared and submitted within the normal filing period. As you will not be present in the Republic of Panama, it is recommended that you appoint an official tax adviser with a general power of attorney to act on your behalf. Your final income tax return shall be submitted within the next thirty (30) days following the date of termination of your assignment in Panama.

Exporting your personal possessions

73. Exportation is free of duty in Panama. Therefore, taxes will not arise due to the exportation of personal possessions or vehicles.

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Step 7 – Other matters requiring consideration

Health and social security contributions

- 74. Health and social security contributions are demanded by every employee working within Panama. Social security contributions don't have a cap.
- 75. Health insurance is administered by the government and individuals are obliged to use public hospitals, which are specially designed for public health insurance, which covers health and medical care.
- 76. For both health and social security contributions, the employee is demanded to pay 9% of their salary and the employer must pay to the Social Security at a rate of 12% on the gross income of every employee. These Contributions will be increase as follows:

Year	Employee	Employer
2009	8%	12%
2010	8%	11.75%
2011-2012	9%	12%
2013	9.75%	12.25%

- 77. Social security contributions provide funding for separate funds including: health, sickness, maternity and pension or retirement.
- 78. The freelance taxpayers that by January of 2007 are still under 36 years of age are compelled to contribute to the social security pension/retirement program at a rate of 11% over 52% of gross annual income, anytime his annual income exceeds B/.9,600.00.

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Appendix A – Tax rates for individuals

Tax rates

If taxable income is	Taxes payable will be
Up to B/.11,000.00	0%
More than B/.11,000.00 up to B/.50,000.00	15% rate on amounts exceeding B/.11,000.00 up to B/.50,000.00.
More than B/.50,000.00	B/.5,850.00 for the first B/.50,000.00 and an applicable rate of 25% on amounts exceeding B/.50,000.00

Special tax rates for representation allowances

If taxable income is	Taxes payable will be
Up to B/.25,000.00	10%
More than B/.25,000.00	Will pay B/.2,500.00 for the first B/.25,000.00 and a rate of 15% over exceeding amounts.

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Appendix B – Individual tax calculation

Tax computation

Assumptions:

1. Tax Resident married
2. Exchange rate of the balboa at January 1, 2007: US\$1 = B/. 1.0361

Salary		80,000
Less—Deductions:		
• Interest on mortgage	(15,000)	
• Charitable contributions	(500)	
		(15,500)
Subtotal		64,500
Less—Personal exemptions:		
• Joint return	(800)	
		(800)
Taxable income		63,700
Tax thereon:		
• On first 50,000		5,850
• On remaining 13,700 at 25%		3,425
Tax payable		9,275

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Appendix C – Principal IAS contacts

For additional information on taxation in Panama, contact:

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