

Panama enacts economic substance rules for foreign-source passive income

October 1, 2026

In brief

What happened?

Panama enacted Law No. 526 of May 28, 2026, published in Official Gazette No. 30,534-B. The Law amends and adds articles to the Tax Code and creates an economic substance regime for certain foreign-source passive income earned by entities established or domiciled in Panama that belong to multinational groups. The Law was regulated by Executive Decree No. 32 of September 2, 2026, published in Official Gazette No. 30,603-B.

The regime applies as of the 2027 fiscal period, that is, for fiscal years beginning on or after January 1, 2027.

Why is it relevant?

The new rules represent a significant change in Panama's tax framework, directly affecting multinational entities that use Panama as a regional platform. Panama's territorial tax system remains in place; however, entities that earn foreign passive income through Panama now must show real activity and meet minimum economic substance requirements in Panama. Income earned by an entity that does not meet those requirements is subject to a single and definitive 15% tax on net taxable income.

Actions to consider

Companies should review their Panama structures to assess exposure to the new regime, identify

economic substance gaps, revisit service provider arrangements, and prepare the information that must be reported, before the rules take effect in 2027.

In detail

Background

Under the territoriality principle that governs the Panamanian tax system, passive income (including dividends, royalties, interest, capital gains, or real estate income) generated by offshore companies has not been subject to tax in Panama. The Law keeps that principle but makes the non-taxable treatment of foreign-source passive income conditional on the entity demonstrating adequate economic substance in Panama, in line with efforts to document that activities are actually carried out within the country.

Analysis

The Law introduces a structural change to the traditional principle of territoriality, aligning the Panamanian system with international standards on economic substance and combating structures without a real presence. The change impacts holding companies, investment entities, intangible companies, and regional structures established in Panama, including trusts and foundations.

The Law (1) establishes minimum economic substance requirements for entities in Panama belonging to multinational groups that receive passive income from foreign sources; (2) subjects that income to a single and definitive 15% tax on net taxable income when the entity is considered "non-qualified;" and (3) provides the Ministry of Economy and Finance (MEF), as the competent authority, with tools for auditing, controlling, and preventing abuse by these structures. For this purpose, a multinational group is a group of two or more entities related through ownership or control and tax resident in different jurisdictions, including the parent company, subsidiaries, and permanent establishments.

The regime applies to the following passive income from foreign sources: dividends, interest, royalties, capital gains, income from real estate capital, and other passive income from movable capital. Such income retains its non-taxable status only if the entity demonstrates adequate economic substance. Subject to certain requirements, the regime does not apply to entities operating vessels registered in Panamanian registries under special maritime legislation, financial entities regulated by the Superintendence of Banks or the Superintendence of the Securities Market, insurance and reinsurance companies (other than captive insurers within a multinational group), regulated securities intermediaries, and investment and pension fund managers. Entities under preferential tax regimes are not exempt from these obligations and must also report and provide evidence of substance.

A qualified entity is one within a multinational group that meets the economic substance requirements for each type of passive income in a given tax period. Conversely, a non-qualified entity is one that fails to report its foreign passive income in its income tax return, does not meet the economic substance requirements, provides no or only partial information to the MEF, or submits false or clearly inconsistent information on its activities, assets, risks, personnel, facilities, or operating expenses. Net taxable income is determined by deducting documented costs and expenses directly related to generating the foreign-source passive income, and surcharges, penalties, and interest also may apply. The Law further includes an anti-abuse provision allowing the MEF, through a reasoned resolution, to disregard structures whose main purpose is to obtain tax advantages without real economic substance.

To be considered qualified, the entity must meet the following criteria simultaneously:

- adequate, qualified, and paid personnel in Panama and facilities in Panama, linked to the management of income-generating assets;
- strategic decision-making and risk-taking in Panama;
- appropriate operating costs and expenses incurred locally and directly related to the passive income-generating activity; and
- demonstration of compliance for each tax period and for each type of passive income.

The Law and its regulations

The Law required the Executive Branch to issue implementing regulations within 90 days. That mandate was met with Executive Decree No. 32 of September 2, 2026, which develops the substance requirements and applies to entities of multinational groups incorporated or domiciled in Panama (including trusts and foundations) that receive passive income from abroad.

As a general rule, the entity must maintain in Panama at least one qualified and compensated individual dedicated, full-time or part-time, to its core activities, whether employed directly or engaged through a service provider. The entity also must have adequate physical premises in Panama, which may be owned, leased, or shared, provided the right to use them is properly documented.

The Decree also requires that:

- strategic decisions be taken in the country, with the board of directors or equivalent body holding at least two in-person meetings per year in Panama, keeping the related minutes in Panama, and not delegating these functions to third parties; and
- the entity incur, in addition to personnel and premises costs, other costs and expenses in Panama relating to the assets that generate its foreign-source income, reasonable in relation to the size and complexity of its operations and supported by contracts, invoices, or other records.

Other points covered by the Decree include:

- simplified substance requirements for entities primarily holding equity interests or real estate without a relevant business or investment activity, which may satisfy the personnel requirement with at least one compensated director, officer, or administrator resident in Panama;
- reporting of foreign-source passive income in the income tax return, together with details of the entity's activities, personnel, facilities, decisions, risks, and expenses;
- retention of the supporting documents in Panama, in physical or digital format, for five years;
- use of service providers to carry out core activities in Panama under a documented service agreement, to the extent the provider has adequate resources and the entity retains oversight and control, and with no simultaneous allocation of the same personnel hours to more than one entity;
- conditions for recognizing taxes paid abroad, which may be credited against the Panamanian tax up to the amount payable locally, with no carryforward, transfer, or refund of the credit;

- specific rules for income from intangibles registered in Panama, based on a qualifying-expenditure ratio; and
- the way the exclusions available to certain regulated entities are verified, including accreditations issued by the sectoral regulators. Supporting documentation must be filed in Spanish.

Both regulations have been published in the Official Gazette and become effective for fiscal years beginning on or after January 1, 2027.

Let's talk

For a deeper discussion of how these new rules might affect your business, please contact:

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