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# Global Tax Alert

News from Americas Tax Center

## Panama issues regulations on Panama-Pacifico regime

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On 27 December 2018, Panama published, in *Official Gazette No. 28684-B*, Resolution No. 010-18, which contains regulations outlining the requirements with which companies must comply if they want to qualify for benefits under the Panama-Pacifico (PP) regime as companies that provide office management services. The Resolution became effective on 28 December 2018.

### Background

#### Tax regime

On 12 December 2018, Panama published in *Official Gazette No. 28675-B*, Law 66 of 2018 (the Law), which amended the PP regime. Law 66 became effective on 14 December 2018.

The PP regime grants income tax benefits to companies that engage in certain activities. Law 66 limited eligibility for those benefits by removing the following activities from the list of activities eligible for preferential tax treatment under the PP regime: (1) rendering services to individuals or legal entities located abroad; (2) rendering high-added value services protected by intellectual or industrial property provisions; and (3) re-invoicing of goods that do not enter Panamanian territory.

The Law defined office administrative services as: (1) the direction, administration or support of operations; (2) strategic planning services and business development; and (3) technical assistance, technical support, logistics, and marketing. Companies rendering office administrative services to beneficiaries abroad must pay a 5% income tax on the related net taxable income. Panamanian recipients benefitting from these services must withhold 5% on the total service payment if: (1) the services related to the generation of local income or the conservation of its source (i.e., the maintenance of income considered as income produced in Panama); and (2) the payment is considered a deductible expense by the recipient.

The PP regime, as amended by the Law, also allows companies providing office administrative services to claim a tax credit for the amounts withheld by the Panamanian taxpayers, as well as for amounts effectively paid abroad for services rendered by nonresidents. However, the company will have to pay at least 2% of the net taxable income generated in Panama as a minimum income tax.

### **New requirements for certain activities**

The PP regime requires companies that engage in certain activities to meet the following requirements to claim income tax benefits: (1) incurring an adequate amount of operating expenses in Panama related to the activity; and (2) having an adequate number of full-time qualified employees engaged in the activity. The activities listed in the Law include: (1) radio, television, audio, video and data signal linking; (2) office administrative services; (3) call centers; (4) capturing, processing, storage, switching, transmitting and retransmitting data and digital information; (5) logistic and multimodal services; and (6) research and development of resources and digital applications for use in networks. For companies that conduct these activities and were registered under the PP regime before the enactment of the Law, the requirements apply as follows:

- ▶ From 1 July 2021, for companies that registered under the regime before 17 October 2017
- ▶ From tax year 2019, for companies that registered under the regime on or after 17 October 2017

Additionally, companies must submit an affidavit to the PP Agency. The affidavit must contain information on: (1) the activities carried out to generate the income received during the previous tax year; (2) the operating expenses incurred

in the execution of those activities; and (3) the number of employees that worked on those activities during the previous tax year.

### **Transitional provisions for services rendered abroad and office administrative services**

The Law established transition rules for companies that are currently registered in the PP regime as entities providing: (1) services to individuals or legal entities located abroad; or (2) office administrative services to users within the PP area or established outside Panama's territory.

Under the transition rules, companies that have been registered under the PP regime for more than 10 years and provide services to persons located abroad, as well as companies that provide office administration services to companies in the PP area or abroad, may submit a request to the PP Agency to be qualified as a company that provides office administrative services as provided in numeral 21 of Article 3 of Law 41 of 2004 and in accordance with literal k of Article 60 of Law 41.

For a company that does not qualify as a company that provides office administrative services, the following taxes apply: (1) income tax on the taxable net income earned from activities, businesses or operations conducted within the PP area; (2) dividends tax withheld from profits or dividends paid to shareholders or partners, and the complementary tax; and (3) tax withheld on commissions, royalties, and payments for technical assistance services.

Also, under the transition rules, companies that are registered under the PP regime for less than 10 years may submit a request to the PP Agency to: (1) eliminate the activities removed from the PP regime by Law 66 from their registries; or (2) qualify as a company that provides office administrative services as provided in numeral 21 of Article 3 of Law 41 of 2004 and in accordance with literal k of Article 60 of Law 41.

Companies that do not select either option, or whose request to qualify as a company that provides office administrative services is denied by the PP Agency, will still maintain their income tax exemptions for 10 years, beginning on the date they were registered in the PP Registry. The tax exemption will apply to the income generated from rendering services to the foreign market and the Panamanian market. However, the Law imposes value-added tax (VAT) on services provided

to beneficiaries in Panama. Furthermore, the companies must comply with the new requirements as follows to claim the income tax exemption:

- ▶ From 1 July 2021, for companies that registered under the PP regime before 17 October 2017
- ▶ From fiscal year 2019, for companies that registered under the PP regime on or after 17 October 2017

### Other provisions

Companies registered under the PP regime are subject to transfer pricing rules because of amendments introduced to the Fiscal Code through Law 69 of 2018. These amendments subject companies operating under any preferential tax regime (including the PP regime) to transfer pricing rules on their operations with related parties located in Panama, abroad or in any other preferential tax regime.

Additionally, the Law clarifies the VAT exemption that was already provided under the regime (i.e., on services rendered by companies registered under the regime to individuals or legal entities established abroad or within Panama and to companies registered under the PP regime).

### Resolution No. 010-18

Resolution No. 010-18 sets forth the rules for a company to qualify as a company that provides office administrative services. To be eligible as a company that provides office administrative services under the PP regime, an applicant must (1) be part of a business group with assets equal to or greater than US\$200 million; or (2) be a company that provides office management services to at least seven affiliates, subsidiaries or associated companies.

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