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Panama: Trends and Developments
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PANAMA

Trends and Developments

Contributed by:
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Icaza, González-Ruiz & Alemán is a Panamanian law firm with more than a century of experience advising high-net-worth individuals, family offices and private institutions. Its seven-lawyer private wealth team works with affiliate Icaza Trust Corporation, one of Panama's first licensed non-banking trust companies, on fiduciary, estate planning, corporate and cross-border structuring matters. The firm has offices in Panama, Singapore, Switzerland, Cyprus and Uruguay, while affiliated companies hold licenses to provide corporate services in Anguilla, The Bahamas, Belize, the British Virgin Islands, Nevis and the Seychelles. The practice covers trusts, private foundations, succession planning, family governance, philanthropy, tax, accounting and regulatory compliance. Recent work includes administering an average of approximately USD6.5 billion in assets over the past year, managing public trusts such as Fidemicro-Panamá, supporting syndicated loan structures and administering trusts connected to infrastructure projects, including the Panama Metro Lines.

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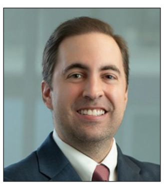

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Panama's Economic Substance Framework: The Final Regulatory Building Block

The final piece of the puzzle

Panama has occupied a central position in the global corporate services landscape for decades. Its territorial tax system, sophisticated legal infrastructure, favourable location at the crossroads of the Americas, and well-established corporate law tradition have made it a preferred platform for international holding structures, family wealth vehicles, and multinational group entities across Latin America and beyond. Under Panama's territorial tax system, Panamanian entities are subject to income tax exclusively on income derived from Panamanian sources; foreign-source income, including dividends, interest, capital gains, royalties, and other returns generated by assets held or activities conducted abroad, falls entirely outside the scope of Panamanian income tax. This principle, enshrined in the Fiscal Code, has historically made Panama a particularly efficient platform for structures designed to hold, manage, or transfer international assets, as foreign returns generated through a Panamanian entity do not give rise to Panamanian tax exposure.

Yet for all its strengths, Panama's competitive position has been complicated in recent years by the absence of a feature that had become standard across virtually every comparable jurisdiction: economic substance requirements. The British Virgin Islands (BVI), the Cayman Islands, the Bahamas, Bermuda, the Seychelles, Singapore, and Uruguay all introduced economic substance frameworks beginning in 2019. Panama did not follow, and that omission drew sustained criticism from international organisations, in particular the OECD, placing Panamanian structures under reputational and practical pressure in banking, regulatory and tax contexts. This will change with the enactment of Law 526 of 28 May 2026, which introduces economic substance requirements for Panamanian entities that form part of multinational groups and receive passive income from foreign sources. The law enters into force with effect from fiscal year 2027, and the Executive Branch has 90 calendar days from promulgation to issue the corresponding regulations that, as of the date of this article (August 2026), have not yet been published.

The enactment of Law 526 does not mark a departure from Panama's strengths as a corporate services jurisdiction, but rather their consolidation. This article examines the law's principal features, places them in the context of Panama's broader regulatory evolution over the past decade and critically identifies the open questions that the forthcoming regulations must resolve, including the treatment of pure equity holding structures and the permissible scope of outsourcing arrangements. The answers to these unresolved questions will define the practical impact of the new regime for a significant number of international structures.

The BEPS imperative: why economic substance legislation exists

Economic substance requirements are one of the central outputs of the OECD's Base Erosion and Profit Shifting (BEPS) project, which has reshaped international tax policy since its launch in 2013. BEPS Action 5, which targets harmful tax practices, requires jurisdictions offering preferential or no-tax regimes to ensure that entities benefiting from those regimes conduct genuine economic activity in the territory where they are incorporated or managed. The organising principle is straightforward: if a company claims a tax benefit on account of its presence in a particular jurisdiction, it should actually be present there in a meaningful sense, employing people, making real decisions, bearing genuine risks, and incurring real costs.

The motivation behind these rules goes beyond tax collection. Multinational groups that locate passive income streams in low-tax jurisdictions without corresponding operational activity have long been criticised for eroding the effective tax base in higher-tax countries where their genuine business activity is conducted. Economic substance legislation addresses this concern directly, by requiring a demonstrable and verifiable link between the income attributed to a jurisdiction and the economic activity that actually takes place there.

For jurisdictions in the international corporate services industry, compliance with BEPS Action 5 has become a condition of regulatory respectability and, increasingly, of market access. The EU's list of noncooperative jurisdictions for tax purposes, together with the banking, regulatory, and reputational consequences of inclusion on that list, has provided powerful additional incentive for jurisdictions to adopt and enforce adequate substance requirements. Panama, having navigated a challenging international reputational environment in recent years, has compelling reasons to align fully with these standards. Law 526 is the result of that commitment.

Panama's regulatory journey: a decade of progressive alignment

Law 526 does not emerge in isolation. It is the latest and arguably the most significant step in a decade-long process through which Panama has systematically modernised its corporate regulatory framework to bring it into line with the standards prevailing in comparable jurisdictions. Understanding this context is essential to appreciating both the significance of the new law and the trajectory it represents.

Law 52 of 2016 established mandatory accounting records requirements for two categories of Panamanian legal entities particularly relevant to international structuring: those that do not carry out operations with effects within Panama, and those exclusively dedicated to holding assets, whether within or outside Panamanian territory. As strengthened by Law 254 of 2021, entities within scope must maintain accounting records and supporting documentation for a minimum of five years; those exclusively holding assets must maintain records reflecting the value of assets held, the income received therefrom, and the related liabilities, and must deliver their accounting records or copies thereof to their registered agent annually by 30 April. Law 51 of 2016, also amended by Law 254 of 2021, established Panama's regulatory framework for the automatic exchange of financial account information in line with the OECD Common Reporting Standard (CRS), enabling the systematic exchange of tax information between Panama and its partner jurisdictions.

Panama also enacted a beneficial ownership registration regime, requiring all companies and private foundations to maintain up-to-date information on their ultimate beneficial owners and to make that information accessible to competent authorities through a secure system administered by registered agents. This regime aligns Panama with the Financial Action Task Force (FATF) recommendations on beneficial ownership transparency that have become a baseline expectation across the international financial services industry. Beneficial ownership registers have similarly become a standard due diligence requirement of banking counterparties and foreign regulators dealing with Panamanian entities.

Together, these measures have brought Panama into substantive alignment with the corporate governance and transparency standards of jurisdictions such as the BVI, the Cayman Islands, Singapore, Uruguay, the Seychelles, Jersey and Guernsey, all of which have enacted comparable frameworks for accounting records, beneficial ownership, and economic substance. Law 526 adds economic substance to this framework, completing the alignment and addressing the one regulatory gap that the OECD and the EU had most consistently identified as a point of concern.

Law 526: a targeted regime, not a general rule

One of the most important features of Law 526 is what it does not do. It is not a general economic substance requirement applicable to all Panamanian entities. Its scope is specifically limited to entities that simultaneously satisfy three conditions: they must be incorporated or domiciled in Panama; they must form part of a multinational group; and they must receive passive income from foreign sources.

A multinational group, for purposes of Law 526, is defined as a group of two or more entities linked by ownership or control, whose members are tax resident in different jurisdictions, including the parent entity, its subsidiaries, and any permanent establishments. Critically, a Panamanian entity does not form part of a multinational group merely because it holds foreign assets, maintains offshore bank accounts, or receives dividends from a foreign investment. The determining factor is the existence of a cross-jurisdictional control or ownership link between entities that are tax resident in two or more different jurisdictions.

The vast majority of Panamanian private interest foundations, closely held holding companies, and family wealth vehicles used for personal or family estate planning purposes without structural links to entities tax resident in other jurisdictions, will not fall within the scope of Law 526. For these structures, the law introduces no new substantive obligations, and the foundational principle of Panama's territorial tax system remains fully intact.

For entities that do fall within scope, the passive foreign-source income categories covered include dividends, interest, royalties, capital gains, real estate income, and other foreign-source capital income. These entities must demonstrate economic substance in Panama through adequately qualified and remunerated human resources, adequate physical premises, strategic decision-making conducted from within Panama, genuine risk-bearing in Panama, and operating costs incurred in Panama proportionate to the level of activity. Law 526 also expressly permits the outsourcing of certain activities to service providers in Panama, subject to conditions that the regulations will further define.

Pending questions: what the regulations must resolve

Law 526 establishes the broad framework, but its practical application will depend critically on the content of the regulatory decree that the Executive Branch must issue within 90 days of promulgation. Three issues stand out as particularly consequential, and practitioners advising clients with Panamanian structures should monitor the regulatory process closely.

The definition of tax residency in Panama

Under existing Panamanian law, an entity is considered a fiscal resident of Panama if it is a Panamanian income taxpayer, which generally implies the receipt of Panamanian-source income, or if, in accordance with Article 762-N of the Fiscal Code, it has material means of management and administration in Panama that allow it to apply for a tax residency certificate before the *Dirección General de Ingresos* (DGI).

If the forthcoming regulations seek to apply a broader or different interpretation of fiscal residency for purposes of the economic substance regime, a fundamental legal question arises: can that outcome be achieved by regulatory decree, or would it require a direct amendment to Article 762-N of the Fiscal Code, which currently governs the determination of fiscal residency under Panamanian law? The answer has material structural implications for international groups with Panamanian holding entities, and the regulations must address it with precision.

Pure equity holding companies: the case for a proportionate standard

Perhaps the most commercially significant question under Law 526 concerns the economic substance standard applicable to entities whose sole or primary activity is the holding of participations in other companies, commonly referred to in international practice as "pure equity holding companies" or "pure equity holding entities"(PEHEs). These structures are widely used in international estate planning, family office arrangements, and multinational group hierarchies involving Panama, and their treatment under Law 526 will have broad practical implications.

Comparable jurisdictions have consistently recognised that the substance requirements applicable to a pure equity holding entity should be proportionate to the limited operational character of that activity. The British Virgin Islands introduced its economic substance framework under the Economic Substance (Companies and Limited Partnerships) Act 2018. Under Section 8 (2) of that Act, a pure equity holding entity is defined as an entity that carries on no relevant activity other than holding equity participations in other entities and earning dividends and capital gains. Such entities are subject to a materially reduced economic substance test. For entities with purely passive holdings, compliance is achieved by maintaining adequate arrangements through a registered agent in the BVI and meeting applicable statutory filing obligations. No full-time employees, dedicated office premises, or detailed reporting on local operational expenditure is required at the reduced test level.

Uruguay adopts a comparable approach. Under Uruguayan corporate income tax rules, the employee and premises requirements that form part of the general economic substance framework do not apply to entities whose core business consists of holding interests in other entities. The policy rationale is sound: a passive holding vehicle does not need a dedicated workforce or physical offices to perform its core function, and imposing those requirements on such structures would be both disproportionate and commercially unrealistic.

Panama's regulations should address the treatment of pure equity holding entities explicitly and introduce a proportionate standard consistent with international practice. A calibrated reduced standard, focused on compliance with applicable corporate obligations and the maintenance of a duly appointed registered agent in Panama, would be both legally defensible and commercially appropriate. Without this guidance, advisers and their clients will be left to navigate significant uncertainty in designing holding structures that are compliant without being operationally artificial.

Outsourcing: defining the permissible scope

Law 526 permits certain core activities to be outsourced to service providers in Panama, provided that those activities are carried out within the national territory under the direct supervision and control of the contracting entity. The regulations, however, will need to define the parameters of permissible outsourcing with sufficient specificity to give entities and practitioners clear guidance.

In Singapore, outsourcing of economic activities is recognised under the economic substance framework applicable to foreign-sourced disposal gains under Section 10L of the Income Tax Act 1947. Outsourcing is accepted as a valid means of meeting the substance requirement provided that: the outsourced entity conducts genuine economic activities in Singapore; the outsourcing entity exercises direct and effective control over those activities; and the outsourced entity has adequate dedicated resources, not merely shared or incidental staff, committed to the arrangement. Singapore also permits a single service agreement to cover the economic activities of multiple entities within a multinational group, which provides useful structural flexibility.

Uruguay requires detailed documentation of outsourcing arrangements, including specification of the human resources engaged, the hours applied to the relevant activities, and the physical facilities in which those activities are performed. Panama's regulations should provide comparable clarity on the documentary basis for outsourced arrangements, the conditions under which shared service arrangements within a group may satisfy the substance test, and the distinction between genuine outsourcing and the mere formal delegation of functions without operational substance.

Consequences of non-compliance

Panamanian entities within the scope of Law 526 that fail to demonstrate adequate economic substance will be classified as "non-qualifying entities." The principal tax consequence is that their passive foreign-source income will be subject to a flat income tax rate of 15% on net taxable income for the relevant fiscal period, a charge that could represent a significant and unexpected liability for structures that have historically operated under the full exemption afforded by Panama's territorial tax system.

Non-compliance may also give rise to penalties, surcharges, and interest under the Panamanian Fiscal Code. In addition, Law 526 includes a general anti-avoidance provision empowering the Ministry of Economy and Finance to disregard structures or arrangements whose principal purpose is to obtain tax advantages that are incompatible with the law's objectives. This provision introduces a substance-over-form principle that operates alongside the specific economic substance tests, giving the tax authorities broad discretion to look through arrangements that are formally structured but economically hollow.

Entities within the scope of Law 526 that are required to comply with economic substance requirements will also be required to file an annual income tax return, regardless of whether their income consists exclusively of passive foreign-source income. This annual filing obligation is a new formal requirement for many Panamanian holding entities that have historically had no interaction with the Panamanian tax administration, and it should be factored into the operational planning of affected structures well before the 2027 fiscal year commences.

Preparing for 2027: a Practical roadmap

With Law 526 entering into force for fiscal year 2027 and the regulatory decree expected within weeks of publication of this article (August 2026), the window for preparation is shorter than it may appear. Practitioners and their clients with international structures involving Panamanian entities should begin a structured review now, rather than waiting for the regulations to be finalised.

The first priority is a threshold assessment: whether each Panamanian entity in a given structure falls within the law's scope, specifically, whether it forms part of a multinational group and whether it receives passive income from foreign sources within the relevant categories. A careful factual analysis is required before any conclusions are drawn in either direction.

For entities that do fall within scope, the next step is a functional analysis, an assessment of where, by whom, and on what basis key decisions are made in relation to the relevant foreign-source income-generating activities, and whether the current level of activity in Panama is sufficient to support a credible economic substance demonstration. This analysis should be calibrated against the anticipated regulatory guidance on the treatment of pure equity holding entities and outsourcing arrangements.

Panama is entering a new regulatory chapter, and it does so from a position of considerable institutional strength. For international investors, multinational groups, and families who have long valued Panama as a platform for wealth management and corporate structuring, this chapter opens with the assurance that Panama's framework now fully meets the standards that international partners, banking institutions, and tax authorities have come to expect of a serious, well-regulated corporate services jurisdiction. Navigating the new regime requires careful analysis and expert guidance, but the destination is one that strengthens the long-term legitimacy and durability of structures built around Panama.

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