an intent to submit a bill to curb oligopolies and restrictive trade practices and to provide consumer protection.

5.02 Monopolies and market dominance. No legislation as yet exists on this subject. Though Article 257 of the Constitution prohibits private monopolies, in practice there are several.

5.03 Mergers are not restricted. However, Executive Decree 18 of March 14, 1994, redefined the terms "consolidation" and "merger" as discussed in the 1927 Corporations Law and stipulated that certain tax benefits may accrue only to company reorganisations that follow the rules stated in the new decree. The reorganisation process must be reported to and is subject to review by the tax authorities.

The reorganisation must proceed in accordance with the provided rules for accounts payable and related reserves, related parties' accounts receivable, inventory and obsolete inventory reserve, depreciation, capital accounts, income, cost and expense accounts; transference of assets; inventory valuation methods; accounting systems and records. The benefits are as follows:

- Deeds, agreements and other operations necessary to complete the merger or consolidation would not be subject to income tax, value-added tax, tax on property transfer, dividend tax or complementary tax.
- Shareholders of extinguished companies will be exempt from income, dividend and complementary taxes, as long as they receive only shares of the new company in exchange for their old shares.

5.04 Freedom to sell. A manufacturer may legally sell or refuse to sell to anyone. In 1989 the Supreme Court reaffirmed this right by striking down Decree 344 of 1969, which bound manufacturers to contractual distribution arrangements. The new court established after the 1989 US invasion has upheld this position.

Although virtually no restrictions apply to exclusive distributorships that are set up by the manufacturer, the majority of companies operate through non-exclusive distributors.

A manufacturer may sell at varying prices to different dealers and may sue an unauthorised dealer that has procured its merchandise from a foreign source.

5.05 Resale-price maintenance. Manufacturers may not enforce minimum resale prices, but many do suggest prices.

5.06 Price controls. The Endara government freed prices on several major items during 1991–92. As part of an October 1992 agreement with the local Texaco oil refinery, the government decontrolled petroleum derivatives (except for cooking gas sold in small amounts). Prices of a few basic foodstuffs, industrial products, medicines and public transport remain subject to control by the Office of Price Regulation (OPR). As Panama moves closer to GATT membership, these controls can be expected to be eliminated.

Rent control, enforced by the Ministry of Housing, applies to property extant before 1985 and (in the case of residential units) renting for less than $250 per month. Rent increases may be obtained for such property by special application, documenting erosion of the return on investment. Controls may be ended via conversion of a building into a condominium, but this requires the consent of a majority of occupants.

6.00 Exchanging and remitting funds

6.01 Exchange controls. Panama imposes no exchange controls. There are no official guarantees against inconvertibility.

6.02 Capital inflow and repatriation. Repatriation of capital is unrestricted.

6.03 Profit remittances. Transfer of profits and dividends is unrestricted.

6.04 Loan inflows and repayment. There are no controls on borrowing of funds from abroad. Transfer of interest and repayment of principal are both unrestricted.

6.05 Transfer of royalties and fees is unrestricted.

6.06 Restrictions on trade-related payments. There are no restrictions on leading or lagging of trade-related payments, or on foreign exchange obtained from exports.

7.00 Corporate taxes

7.01 Overview. Corporate tax rates in Panama are low, and tax morality is fairly high by Latin American standards. Panama does not tax income from non-Panamanian sources—a policy that has made it a favoured place to base holding and sales operations. Generous tax incentives are also available, mainly for export-oriented concerns (3.00).

7.02 Corporate tax rates. Income is classified in three categories for tax purposes: (1) Panamanian-sourced income, ie that derived from sales or services anywhere in the country; (2) export income, derived from the export of goods manufactured in Panama or that pass over Panamanian soil; and (3)

Corporate taxation in Panama

Below is a simplified example of how Panamanian taxes apply to three companies, each with $1m in net worth and parent company loans, and $200,000 in taxable income. Firm A is located in Panama proper and has only Panamanian-sourced income; Firm B is in the Free Zone, with 50% of its income deriving from imports and 50% from sales to Panama proper; and Firm C is also in the Free Zone but derives all its income from exports. The example assumes that the parent companies are in countries that grant no tax credit for taxes paid in Panama.

	Firm A	Firm B	Firm C
Taxable income	$200,000	$200,000	200,000
Income from operations in Panama	200,000	100,000	0
Tax on Panamanian income (30%)	60,000	30,000	0
Net Panamanian income after tax	140,000	70,000	0
Imputed dividend tax (10% of 40% of net)*	5,600	2,800	0
Export income	0	100,000	200,000
Tax on export income	0	6,000	17,000
Annual basis licence tax (1% of $1m)	10,000	10,000	10,000
Total taxes	75,600	48,800	27,000
Tax burden as % of taxable income	37.8%	24.4%	13.5%

*Assuming dividend does not exceed 40% of net.

non-Panamanian income, from the management of non-Panamanian operations, from dividends and similar income paid by non-Panamanian entities and from the sale of goods not entering Panama.

A company (or a branch of a foreign firm) located in Panama proper is liable for tax on both its Panamanian-sourced and export income (unless it is exempt through an incentives contract—see 3.03), but not on non-Panamanian income.

Under Law 31 of December 30, 1991, a single corporate income tax rate of 30% applies to net income up to $500,000, and another of 34% to amounts exceeding $500,000. The law also ended tax deductions for certain expenditures (7.03).

For examples of how the corporate tax system applies in practice, see the box above.

7.03 Taxable income defined. Taxable income is generally defined as income less the expenses necessary to produce it or to preserve productive capacity (eg expenses for repairs to a plant or for advertising).

The Panamanian income tax is meant to apply only to income derived from sources within the territory of the Republic, and the law specifically states that the following activities do not produce income that is taxable in Panama: (1) invoicing from an office in Panama the sales of goods that do not enter the country; (2) handling offshore transactions from an office in Panama; and (3) distributing dividends from income derived abroad, including income from (1) and (2).

Interest and royalty payments are deductible, as are research and development costs. Organisational expenses may be excluded from taxable income in the year incurred or amortised over five years, at the discretion of the tax-payer.

Bonuses to employees in excess of the lesser of one month's salary or $750 are not deductible, unless included in pension fund contracts. Profit-sharing payments are deductible.

Law 31 of 1991 ended the deductibility of expenses incurred as the result of transactions between the tax-payer and its directors, shareholders and relatives of same.

Manufacturing firms qualifying for certain incentives may carry losses forward to any of the five years immediately after the year in which the loss occurs. Otherwise, there is no provision for loss carry-forward or carry-back, unless the extent of the loss cannot be assessed in the same tax year. In such cases the loss is taken in the year in which it can be assessed.

Overpayment of taxes is now reimbursable, or may be used to offset future liabilities.

7.04 Depreciation. Decree 170 of October 27, 1993, did away with previous depreciation rates on particular types of assets. Depreciation is now calculated on the basis of the useful economic life of the depreciating good, which may not be less than three years for movable property or 30 years for immovable property, according to one of the following formulae:

- Straight-line method, applying a fixed percentage to the original cost.
- Declining-balance method, applying a fixed percentage to the declining balance of cost.
- Sum-of-digits method.

Tax-payers may use other methods as well, but depreciation of revalued assets is not permitted. Once a company chooses a system, it may switch only with the approval of the tax authorities.

Patents, trademarks and other intangible assets are now eligible for amortisation.

7.05 Schedule for paying taxes. Each year in March a company must file an estimate of the current year's tax bill with the final tax return for the previous year.

Estimated income taxes, based on the previous year's tax, are payable either in one instalment on June 30 or in three equal instalments on June 30, September 30 and December 31.

With permission from the tax authorities, firms not using calendar years for fiscal purposes may meet the payment requirements six months, nine months and 12 months after the close of their prior fiscal year. Late payments are subject to a 10% surcharge plus interest amounting to two percentage points over a reference bank rate established by the National Banking Commission.

7.06 Capital taxes. None.

7.07 Treatment of capital gains. Capital gains derived from the sale of real property are taxed as regular income.

Upon the transfer of real assets, the seller is liable for an advance payment on the capital gains tax proper. This takes the form of a 2% transfer tax on the original cost of the asset as adjusted or on the sale price of the property, whichever is larger. The adjustment in the property's value depends on the number of years that have elapsed since the year the property was acquired and the time it was sold. The number of years is multiplied by 5% and the resulting coefficient is then multiplied by the original value of the property; that result is added to the original. The new figure is compared with the sale price.

As an alternative to the capital gains tax, the seller may opt to pay 5% income tax on the sum of the cadastral value of the property at the time of its original acquisition, the value of improvements effected, plus 10% of the sum of these two values for each year between the time the property was acquired and when it was sold, or the dates of the improvements and the date of sale.

No income tax is imposed on capital gains from sales of stock registered with the National Securities Commission if at least 25% of the assets of the company whose stock was sold are located in Panama. Gains from other stock sales may be included in income and taxed at the ordinary rates.

7.08 Taxes on dividends. A 10% withholding tax is levied on dividends from operations in Panama proper in the case of nominal shares. In the case of bearer-type stocks, the tax rate is 20%.

If dividends distributed equal less than 40% of after-tax income, the tax is nevertheless levied on 40% of net income. The same is true for the Panamanian-sourced income of Colón Free Zone firms.

Under Law 25 of 1992, dividends declared by free zone firms from export earnings are exempt from the withholding tax.

7.09 Taxes on interest. In general, interest and royalties are deductible expenses under the general principle and are taxable income to the recipient.

When payments are made to non-resident individuals or corporate entities, income taxes must be withheld by the payer at the appropriate income tax rate.

There are no taxes applying to interest obtained by banks from foreign operations, to interest generated by time deposits or savings accounts held by companies or individuals in local or foreign banks, or to interest from Panamanian government securities. A 5% tax, which is withheld at source, applies to interest on securities issued by companies registered with the National Securities Commission.

7.10 Taxes on royalties and fees. As with interest, payments of royalties and fees are subject to taxation at the appropriate corporate or personal income tax rate. In both cases the payer withholds the tax on payments made abroad.

Royalty and fee expenses are deductible from the licensee's pre-tax income to the extent that they are necessary for the production of income or the conservation of productive capacity.

The portion of the licenser's receipts represented by the cost of providing the licence may be deducted from licensing income before taxes. When the total cost cannot be established, Panamanian law assumes that there is a deductible cost of 10%.

Royalties paid by firms in the Colón Free Zone to parties outside Panama are not subject to withholding tax.

7.11 Double-tax treaties. None.

7.12 Intercompany charges. The deductibility of expenses that originate between certain entities is restricted in the case when the two parties do not make use of the same accounting system. The expenses are those between a corporation and its subsidiaries and affiliates; between a corporation's directors, officers, executives and shareholders; and between the relatives of the above within the fourth degree, and in-laws within the second degree.

7.13 Regional management companies. Income derived from services rendered to firms or offices outside Panama is not taxed. However, headquarters companies are subject to the business licence tax (7.15).

Personal taxation in Panama

Personal tax rates are as follows:

Taxable income ($)	Tax on lower amount ($)	Tax on remainder (%)
0–3,000	—	0
3,001–3,250	0	52
3,251–4,000	130	4
4,001–6,000	160	6.5
6,001–10,000	290	11
10,001–15,000	730	16.5
15,001–20,000	1,555	19
20,001–30,000	2,505	22
30,001–40,000	4,705	27
40,001–50,000	7,405	30
50,001–200,000	10,405	33
Over 200,000	60,000	30

The following illustrates the 1994 tax burden on an individual with a dependent spouse and two dependent children who earns a salary of $40,000 or $80,000 and has no other taxable income:

Salary	$40,000	$80,000
Deductions:		
Personal	800	800
Spouse	250	250
First child	250	250
Second child	250	250
Net taxable income	38,450	78,450
Total taxes	6,987	19,794
Tax burden as % of income*	17.5%	24.7%

*Individuals are also subject to social charges of 8.25% and an education tax of 1.25% on salary, withheld by the employer. The tax burden may be lower if deductions for medical expenses or interest on housing loans are taken (9.03).

7.14 Turnover, sales and excise taxes. All sales except those of food, pharmaceuticals, textbooks and fuel are subject to a value-added tax (VAT) of 5%. Small export levies and import duties apply to a few products. A 10% VAT applies to liquor and cigarettes.

7.15 Other taxes. Other taxes levied on firms in Panama include the following:

• An annual corporate fee (*tasa única*) of $150 is assessed on all corporations inscribed in the Public Register. The tax is due within three months of the anniversary of incorporation. Late payments incur a $30 penalty.

• An annual business licence tax (*patente*) is levied on firms located in Panama proper. The tax amounts to 1% of declared capital, with a maximum charge of $20,000.

• Stamp taxes are payable at $4 per sheet of paper for certain documents. All contracts—including sales contracts (except those subject to VAT), bank cheques and bills of exchange—bear stamp taxes at varying rates, depending on the type or value of the transaction.

• The property tax is graduated according to assessed value, with zero tax on the first $10,000 and a progressive tax of 1.4–2.1% thereafter (the top rate is reached at valuations above $75,000). In addition, a transfer tax applies to certain sales of real property (7.07).

• A tax of 7.5% on the fob value of most imports is payable in addition to regular import duties (11.02).

• An education tax is assessed on payroll at the rate of 1.5% for employers and 1.25% for employees.

• A 5% surcharge applies to all air and marine traffic fares, to provide funds for the Tourist Bureau.

• A $0.02 surcharge is levied on all letters and telegrams.

8.00 Personal taxes

8.01 Overview. Panama's personal tax burden is moderate. The rates were last modified in 1991, when low-income recipients were exempted from income tax payment. Taxable income for individuals is determined under the same general rules that apply to corporations.

8.02 Residence. Residents and non-residents are subject to essentially the same tax.

8.03 Determination of taxable income. Tax applies only to Panamanian-sourced income and extends to people working in the country temporarily.

Taxable income comprises wages and salaries; profits from business; pensions and bonuses; income from copyrights, royalties, trademarks and patents; and gains from the sale of stocks, bonds and other securities (unless the issuing company is listed with the National Securities Commission and has at least 25% of its total assets invested in Panama, in which case the gain is not taxed).

Items not taxed include interest received from government securities and from savings accounts and time deposits maintained with banks established in Panama. Persons earning less than $3,000 in taxable income pay no tax.

Dividends are subject to a 10% withholding tax, which is considered final. (No dividend tax is withheld on distributions by Colón Free Zone firms engaged in re-export sales.) Properties received as gifts are taxed on a graduated schedule from 4% to 33.75%, depending on the degree of family relationship and the value of the assets involved. All medical expenses incurred in Panama may be written off. Interest paid on home mortgages or on loans for home improvements or education (up to $15,000 per year), donations to approved charities and the 1.25% education tax on earnings are also deductible.

8.04 Personal tax rates. Individual tax rates and two examples of the personal tax burden in Panama appear in the box on p 22.

8.05 Capital taxes. None.

9.00 Capital sources

9.01 Overview. Official institutions exert minimal control over credit, whose availability is ample. The National Banking Commission (a department of the Planning Ministry) sets reserve requirements for banks. Banks may operate under one of three types of licences: general, which allows them to accept local and foreign deposits; international, which allows them to accept only foreign deposits; and representative, which is used for servicing customers. No central bank exists, but the National Bank of Panama performs some of the functions of one, serving as the repository of public funds but issuing only coins.

There are no restrictions on bringing or moving money to or from Panama.

9.02 Short-term capital. As of the end of 1993 there were 107 banks operating in Panama, of which 60 held general licences, 29 international licences and the rest representative licences.

Two banks, the Banco Nacional and the Caja de Ahorros, are owned by the Panamanian government, and Panamanian capital controls another 19 private banks. Many foreign banks do a mix of international and domestic lending, with Chase Manhattan and Citibank leaders in lending within Panama.

According to figures compiled by the accounting firm KPMG Peat Marwick, the ten leading general-licence banks and their total assets as of December 1993 were as follows: Banco Latinamericano de Exportaciones (Bladex), $3.12 billion; Banco Nacional de Panamá, $2.52 billion; Deutsche Sudamerikanische Bank, $1.5 billion; Banco do Brasil, $1.32 billion; Banco General, $868m; Bank of Tokyo, $817m; Dai-Ichi Kangyo Bank, $765m; Chase Manhattan, $703m; Banque Sudameris, $644m; and Primer Banco de Ahorros (Pribanco), $575m. Despite a drop in offshore activities, total deposits in the banking sector rose by $2.2 billion in 1993, to $21 billion, and total assets by $3 billion, to $26 billion.

Corporations normally maintain credit lines with two or more banks holding general licences, renewing once each year. These may be Panamanian banks or branches of US, European or Japanese banks that engage in international and domestic operations. Banks aim at compensating balances of about 10% of credit facilities, but this depends upon the client's credit standing.

Loans are usually granted for six months, though longer terms are available. Domestic borrowing rates are based on a spread over LIBOR, varying according to the quality of the client and the volume of collateral business it generates for the bank. Maximum rates are usually three to four percentage points above the US prime rate—a spread that is tending to narrow.

9.03 Medium and long-term capital. Banco Nacional and foreign development institutions such as the Inter-American Development Bank are the main sources of longer-term funds. To a lesser degree, private banks also lend to the agricultural and industrial sectors, but their long-term funds go mainly into mortgages.

Bladex, established in 1979 and located in Panama, serves as a regional export bank, offering a wide range of services to exporters. The bank's primary aim is to promote non-traditional production by providing short- and medium-term finance for the actual export of goods (not their manufacture). Bladex's assets amounted to $3.12 billion as of December 1993, compared with $2.35 billion at the end of 1992.

The Panama Stock Exchange (PO Box 87-0878, Panama; Tel: 69-1966; Fax: 69-2457), created under Decree 44 of 1988, began operations in 1990. The exchange is regulated by the National Securities Commission, a department of the Ministry of Commerce and Industry. It offers trading in bonds, IOUs, and other national and international government and private company issues.

The stock exchange is primarily national and operates like exchanges throughout Latin America. Member firms must maintain one or several bank accounts in the country, with balances sufficient to meet the value of purchases made on the exchange. Listing requirements are less restrictive than those of the New York Stock Exchange. Very little trading is in equity.

As of September 1994 the exchange listed the securities of a total of 71 domestic and three foreign companies (including six state-owned firms). Total trading volume came to $201.4m in 1993, compared with $102.8m in 1992. Most of the transactions were in bonds and commercial paper. Among the factors fuelling the current rapid growth in trading volume is the tax exemption for interest income from bond issues.

10.00 Human resources

10.01 Overview. Finding unskilled and semi-skilled personnel in Panama is not difficult. However, companies report that competent upper-echelon executives and skilled labourers with manufacturing experience are hard to come by. Several international firms have had success in hiring third-country expatriates resident in Panama to fill top management positions. Workers are recruited directly or through the Labour Ministry's Employment Service. Panamanian workers reportedly respond well to in-house training and frequently have the advantage of being bilingual.

Though unemployment has come down over the past several years, the official jobless rate in the main urban areas remains close to 13%.

10.02 Labour law. Labour relations are regulated under Panama's 1972 Labour Code, which has been described as one of the most "pro-labour" codes in the world and is considered by local business groups to be a significant drawback to doing business in the country. The code establishes a detailed minimum wage, mandates special bonuses, requires high severance pay for unjustified dismissals of employees who have been working for over two years with the same company, orders that bonus payments be computed as salary for the purpose of paying severance pay and benefits (which may make firings costly), prevents employers and workers from independently setting productivity arrangements and makes it very difficult to fire union-affiliated workers. Another problem is inadequate interpretation or implementation of some of the clauses of the code. However, recent laws have exempted small and export-oriented companies (including tenants of export-processing zones—see 3.01) from important code provisions.

Workers are usually hired through a contract, the duration of which varies by occupation. For manufacturing companies, the Labour Code allows a trial period of three months, during which the employer may terminate the contract without incurring any liability beyond the worker's salary up to the day of termination.

The Perez Balladares government has made "flexibility" in the labour market a chief goal. It has announced it will seek changes in the Labour Code permitting greater flexibility in firing workers and rotating them on the job, as well as reductions in the cost of indemnity payments and productivity bonuses.

10.03 Industrial labour. Union membership is concentrated in the public sector and the banana industry. Overall union membership, currently less than 10% of the workforce, has fallen since 1989 because of the support by union leaders for the ousted Noriega government, the anti-labour stance of the Endara government, and high unemployment.

High unemployment has also dampened labour militancy. Nevertheless, in 1994 strikes over salary levels have occurred in the public sector among teachers, garbage workers and telecommunications workers, and in the private sector among sugar-cane labourers and at the Clayco tile factory. Stoppages also occurred in the banana fields in Bocas del Toro, when workers protested the lack of adequate protection against pesticides and other chemicals.

Employers must pay workers for the duration of a legal walkout. In the event of a dispute, attempts at conciliation must be made before a strike may be legally declared. The conciliation procedure is handled by a specially trained corps of Labour Ministry officials. If conciliation fails, the parties have the option of submitting to binding arbitration. If a strike is declared, its legality is decided upon by a special labour court.

10.04 Wages and fringe benefits. Panama's system of legal minimum wages varies according to location, with an urban minimum wage of $0.94 per hour and a rural minimum of $0.64–0.69 per hour. The rates were increased by 20% in 1992, for the first time in ten years.

Average wages have decreased significantly over the past five years, mainly as a result of high unemployment and the impact of political and economic turbulence. According to data from Panama's general comptroller, the average monthly wage in the main urban areas amounted to about $400 as of the end of 1992 (latest available data), down from $450 in 1988. Sectoral averages were as follows: manufacturing, $440; retail/commerce, $360; and services, $480. See the box on p 25 for a summary of the average wages for key positions.

Mandatory fringe benefits represent an estimated 35–40% of base pay.

Workers are entitled to one month's paid vacation for every 11 months of continuous service. Up to two months of vacation time may be accumulated by agreement between the worker and the employer. In addition, employers must pay all workers a 13th-month bonus consisting of one month's salary. The bonus must be distributed in three equal instalments during the year.

The Social Security Institute (CSS), an autonomous state agency, pays health, dental, maternity, disability and old-age benefits, widows' and orphans' pensions, and compensation for occupational accidents. Employers must pay 11.25% of each employee's base pay to the CSS; employees' contributions are 8.25% (withheld by the employer). The CSS also collects the 1.25% education tax, paid by employers and employees alike.

In addition, employers pay 0.567–5.6% of total payroll to cover workers' compensation, according to the degree of risk in an industry. Benefits include medical care and hospitalisation for an

Compensation in Panama*

Position	Average monthly salary ($)
Labourer	220–570
Mechanic	430–940
Foreman	845–1,345
Clerk	345–695
Secretary	540–1,340
Accountant	1,320–1,650
Engineer	1,320–1,650
Manager	1,320–1,650

As of mid-1992 (latest available data).
Source: Contraloria, survey of multinationals in Panama.

unlimited period of time, greater pay benefits during the period of disability, a death benefit as funeral payment and a pension to survivors at half the rate due the insured individual under either old-age or disability benefits.

Employees are entitled to 18 sick days a year; these may be accumulated for two years. Maternity leave, which must be granted for six weeks prior to childbirth and eight weeks immediately thereafter, is covered by the government through social security or, if the employee is not covered, by the employer. Restrictions are placed on dismissals of pregnant women.

10.05 Working hours. The maximum normal work-week is 48 hours for daytime work, 42 for night-work and 45 for mixed day and night-work. Law 1 of March 1986 requires overtime compensation at the rates of 125% of basic pay for daytime work and 150% for night-work in large, non-agricultural and non-exporting firms, and at the rate of 125% of basic pay regardless of time of day in small firms, agricultural concerns and export enterprises. The latter types of firms may also impose mandatory overtime in certain cases.

10.06 Part-time and temporary help. High unemployment makes it easy to find part-time and temporary help. No special regulations apply to them.

10.07 Termination of employment. The Labour Code stipulates three justifications for dismissal: (1) lack of discipline; (2) inability to perform duties; and (3) economic reasons (eg a loss or fall-off in business).

Notice of the reason for and effective date of termination of employment must be provided in writing. Dismissals for property damage, immoral conduct, divulging company secrets and similar acts may be effected without compensation. Absence from work for three consecutive work-days without excuse or on six Mondays in any one year is also grounds for dismissal. Employees with more than two years' service who are fired without justification are entitled to indemnification, which varies according to the length of service (see below).

Notice requirements for dismissals vary with the employee's tenure, ranging from just 24 hours for employees with less than three months' service to a maximum of six months for those with 25 years or more of service. Farms, small businesses and Colón Free Zone operations can dismiss workers with a maximum of 30 days' notice. The worker may choose to work out the period or demand immediate payment of the full compensation involved.

Workers dismissed for economic or similar reasons must be paid indemnification of one to 36 weeks' pay, depending on the length of service. These payments are based on average earnings for 30 days or six months before dismissal, whichever is most favourable to the worker. Under Law 71 of 1981, workers must be rehired or paid additional severance benefits (at the option of the employer) if the labour courts find the dismissal has no legal justification. Workers terminated without just cause who are not reinstated must be replaced.

10.08 Employment of foreigners. Foreign senior executives with representative functions may account for no more than 10% of the workforce of the local company for which they work. (Foreign nationals who have resided in Panama for at least ten years or who are married to Panamanians are considered local citizens.) Moreover, such foreign nationals may receive a maximum of 10% of the total wages paid by the company. All foreign nationals working in Panama must have a work permit issued by the Ministry of Labour. Permits are valid for one year, with a possible extension to five years.

When foreign experts and technicians are needed, they are permitted to make up no more than 15% of the total workforce in a company and to receive no more than 15% of total wages and salaries. The Labour Ministry can authorise the employment of specialists or technicians over the 15% limit but only for a maximum of five years, after which the company must replace each foreigner with a Panamanian national.

11.00 Foreign trade

11.01 Overview. Although it is not a member of the Central American Integration System, Panama has a bilateral trade treaty with each member country.

Imports grew to $2.137 billion in 1993 (cif value, excluding imports into the Colón Free

Zone), a 7.6% increase over their 1992 level, and are projected to rise to $2.34 billion in 1994 and $2.46 billion in 1995. Imports consist mainly of machinery, oil and chemicals, and food products. They come mostly from the USA, Japan, Germany and Mexico.

According to the 1994 US Embassy Commercial Guide, the best prospects for US exports to Panama are in wheat and other agricultural products; computers and peripherals; auto parts; agricultural, food-processing, medical and telecommunications equipment; and apparel.

Panama's exports of goods (excluding exports from the Colón Free Zone) totalled $507m in 1993, up about 7% from their 1992 level. They are forecast to increase to $538m in 1994 and $565m in 1995. Exports consist primarily of bananas, shrimp, clothing, sugar and other goods, and are purchased mainly by the USA, Germany and Costa Rica.

The Colón Free Zone itself exported $5.15 billion worth of finished goods in 1993 (up 5.5% from the 1992 level). Most of these items (especially textiles, footwear and electronic goods imported from Asia and Europe) will be re-exported to the Caribbean and the rest of Latin America. The on-going liberalisation of imports in these countries has contributed greatly to increased commercial activity in the free zone (3.05).

Panama has traditionally offset its merchandise trade deficit with a strong surplus in its service account. Net exports of services amounted to about $1 billion in 1993, and a similar total is expected for 1994. Most of these are exports of transit services, such as those offered by the Panama Canal and the oil pipeline, plus financial and commercial services.

Panama does not discriminate against the exports of any country.

11.02 Tariffs and import taxes. Import duties on goods that do not compete with locally produced items have traditionally been light, since Panama considers itself a trade crossroads and allows many luxury re-export and tourist products to enter at negligible rates. Duties on most manufactured items are 10–30% *ad valorem*.

Protective tariffs on imports that compete with local products have been reduced in recent years. Cabinet Decree 16 of April 16, 1992, abolished specific tariffs, so that protection is now expressed *ad valorem*, with rates not to exceed 40% for industrial products and 50% for agro-industrial products. However, processed tomato products, cigarettes and beer continue to face tariffs above these limits. In addition, protection of some domestically produced agricultural goods ranges up to 90% *ad valorem*. For instance, Cabinet Decree 41 of September 9, 1992, set a 90% tariff level for rice, accompanied by minimum acceptable reference prices for different kinds of rice. Decree 16 also instituted a system of minimum import prices (reference prices) for certain industrial goods, allegedly to prevent either dumping or undervaluation of imports. There are complaints that this system allows for surreptitious hikes in real levels of protection.

Imports into Panama proper—including those from the Colón Free Zone—are subject to the 5% value-added tax, calculated on the sum of the cif value and all other import taxes and charges. A tax of 3% of cif value applies to imports of machinery, raw materials, spare parts, semimanufactured products and packaging.

11.03 Import restrictions. Although in theory import quotas have been replaced by tariff protection, in practice imports of some agricultural items (such as sugar, milk, cheese, flour and oil) and "sensitive" industrial products remain subject to quotas—at least for the time being. Importation of these items requires a licence from a special quota commission made up of the ministers of agriculture and the Treasury along with the general comptroller.

The Agricultural Marketing Institute (IMA) maintains a list of 48 agricultural products under import quotas, including corn, beef, dairy products, soy beans and wheat. Other non-tariff barriers include import permits required by the Ministry of Agriculture for things like animal products, animal by-products and seeds. In addition, a 1993 decree restricts poultry imports on the basis of phyto-sanitary requirements and lack of trade reciprocity.

Panama's petition for membership in the GATT will require a lowering of these tariff levels and the abandonment of non-tariff barriers. To meet its mid-1995 target date for GATT membership, the government will have to negotiate a schedule for trade liberalisation by that date. A tariff-adjustment period of ten to fifteen years is likely.

11.04 Taxes on exports. An export tax, usually 1% of declared value, applies to a few articles, such as gold, silver and platinum, and scrap metal. Bananas face a variable rate depending on volume.

11.05 Free ports, zones. The Colón Free Zone, on the Atlantic side of the Panama Canal, is the second-largest free trade zone in the world. Established in 1948, the zone is segregated by law from the customs territory of the Republic of Panama and is allowed absolute freedom for the movement of goods, with no duties on imports or exports. Activity in the zone continues to grow.

There are three methods of locating in the Colón Free Zone. First, a company may build or purchase its own building, with a renewable 20-year lease on the land (the zone's Technical Department must approve building plans, and at least 60% of merchandise must be exported). Second, space may be leased in zone-owned buildings. Public warehousing operated by the zone administration is available, along with related services such as mixing or simple assembly. Third, firms may engage management-services firms (there are more than a dozen in the zone) to operate warehousing and all related distribution and administrative services. This option enables companies to initiate operations in the zone without any investment in space, facilities or personnel. Companies are permitted to negotiate the rates for such services on the basis of percentage of value, cost-plus or fixed fees.

Warehouse construction costs in the free zone are $200–250 per square metre. High demand has made rental of entire public warehouses difficult, but officially monthly rates are $2.40 per square metre in the Colón area and $1.75 per square metre in France Field. Spaces within public warehouses, also limited, incur a flat annual fee of $200 plus 0.5% of the value of the cargo per month. The alternative is to purchase a self-contained section of a private building (at $275–325 per square metre) or rent same ($3–3.60 per square metre per month). There are separate charges for handling and lorry transport. Preparation of incoming and outgoing documents ranges from $20–35 for a single shipment, which includes the bill of lading, consular invoice and commercial invoice.

11.06 Export restrictions. Exports subject to taxes require an export authorisation from the Ministry of the Treasury. Through Ministry of Agriculture Resolution ALP-0260-ADM of August 13, 1992, the government freed agricultural and livestock exports from any restriction. (Previously, some products could not be exported until the needs of the national market were covered.)

11.07 Export insurance and credit. The government has considered setting up export-insurance facilities, but a concrete policy has yet to be developed. No special export-credit facilities exist and local banks do not offer them. Bladex (9.03), a regional export bank located in Panama, provides credit for regional exporters.

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ILT Panama

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1.0 The operating environment

1.1 Political conditions. Panama's planning minister hailed the country's debt accord reached with commercial banks in May 1995, saying it would shave up to 45% off the country's principal payments and 33% off past-due interest.

Planning Minister Guillermo Chapman said the deal was agreed in principal with international banks and would be closed at the end of 1995 or early next year. Once the contract is signed, Panama will make a $100m initial payment.

The agreement covers $2 billion in principal and $1.5 billion in past-due interest accumulated since 1987. The debt will be converted into 18- to 30-year bonds, including par, discount and past-due interest bonds. As part of the agreement, the country's creditors will swap old loans for new bonds. They will have the option of picking among a variety of floating- and fixed-rate securities, some of which are partially backed by US securities. These so-called Brady bonds will be denominated in US dollars.

Brady bonds are named for former US Treasury Secretary Nicholas Brady, who proposed debt restructuring for developing countries after the debt crisis of the 1980s; a typical Brady restructuring reduces a country's debt by one-third to one-half. The Panama deal makes it the 14th country to swap its bank debt with Brady bonds. (The other countries that have issued Brady bonds are Mexico, Venezuela, Nigeria, Costa Rica, Uruguay, Argentina, Jordan, Brazil, the Dominican Republic, the Philippines, Bulgaria, Poland and Ecuador.) Panama last agreed to a restructuring of its loans in October 1985, but has not made payments on them since March 1988.

The Panamanian team came to the agreement with a committee representing a group of banks who make up the country's seven major creditors—Citibank, Bank of Tokyo, Bank of Nova Scotia, Bank National de Paris, Lloyds Bank and Swiss Bank Corp.

As part of the government's attempt to prevent money laundering, the establishment of new controls at the largest commercial emporium in Panama, the Colon Free Zone, has been proposed. The laundering of drug money in Panama is one of the authorities' main concerns, and President Ernesto Perez Balladares himself has recognized the government's inability to confront drug trafficking and drug-related activities.

A high-level presidential commission on money laundering is also considering new regulations that will include controls on banking secrecy in Panama without affecting legitimate investments. The commission also plans to create a special unit to fight criminal activity as part of the recommendations that will be presented to the executive branch.

1.2 Market conditions. Panama's service economy ranks fourth in size in the region. President Ernesto Perez Balladares' programme of economic liberalisation, fiscal reform and promotion of foreign investment is succeeding. He already has realised a top policy goal: rapprochement with the USA. The administration's commitment to eradicate poverty, on the other hand, will be tested by budgetary constraints.

Last year's 5% GDP expansion was driven by activity in the Colon Free Zone, along with recovery in the financial and transport sectors, and better-than-expected agricultural performance. Growth will dip to 4.5% in 1995, as the construction boom slows and local producers suffer from economic openness.

Imports increased faster than exports in 1994, leading to a deficit of around $1.1 billion. Similar results are expected this year. Panama is aggressively pursuing membership in the World Trade Organisation (1.6), the Asian Pacific Economic Conference and NAFTA.

The government is keen on attracting private investment into the old Canal Zone, tourism, and gold and copper mining. Opportunities for foreign participation will emerge from planned privatisation in electricity, water, telecom and ports (1.4). Imports of consumer-oriented agricultural products are much in demand, as are computers, medical supplies and household goods.

1.4 State role in the economy. A deal that floated the national airline, TACA, on the Panama Stock Exchange, raises hopes that Panama's fledgling capital markets will begin to move away from their traditional reliance on money markets. The listing was made possible thanks to a $30m Eurobond issue from Lafise (US), an investment bank.

It is hoped that other Central American exchanges will follow suit. The Salvadorean government, for example, has set up some fairly stringent hurdles. Its Superintendency of the Financial System, which regulates the capital markets, has become very demanding in its disclosure and other requirements for firms wishing to be listed.

Approval to register the TACA bonds throughout Central America has not been forthcoming, but the possibility excites many investors.

"With respect to government," Panamanian Ambassador to the USA Ricardo Arias said in April 1995, "we are privatising basically all of our public services."

Telephone services will be privatised this year, and legislation is in place to open up electric utilities. Mr Arias also said Panama was privatising several public ports and constructing a private port.

In fact, on June 12, 1995, Grupo Ericsson de Mexico SA, a unit of Sweden-based LM Ericsson, announced that it had a $35m contract with Panama's National Telecommunications Institute (Intel) to design, plan and implement the expansion of the public phone network in Panama. The company will install 77,000 digital lines throughout Panama, carrying Ericsson's AXE technology, the world's most widely used digital-switching system in more than 110 countries, according to company officials. All of the equipment is scheduled to be operational by June 1996.

Parts of the state electricity monopoly, the Instituto de Recursos Hydraulico y Electrificacion (IRHE), will be sold by the end of this year, and the government has also announced the rapid privatisation of several areas of the Instituto de Acueductos y Alcantarillados Nacional (IDAAN, the water board).

Meanwhile, there is growing interest from foreign investors in developing export platforms for industrial products in the Canal ports. The government has set up a Comision Maritima Nacional (COMAR) to co-ordinate the initiatives.

Taiwanese investors have recently agreed to support an export-processing zone near the Panama Canal, along the lines of the Subic Bay development in the Philippines. The president promised a package of tax incentives for the zone, and the government of Taiwan offered $10m to help finance the development (11.5).

Ambassador Arias also said he expected that Panama would incur serious financial losses when it assumes responsibility for management of the Panama Canal from the USA on December 31, 1999. He estimated that Panama would lose income representing 3–4% of its national gross income, in addition to the loss of about 10,000 jobs.

To compensate, Panama will try to attract more investment by opening its market and making labour more efficient, he said. Arias said Panama, which has traditionally remained competitive by imposing high tariffs, will relax trade barriers. "We are trying to open that, and lower our tariffs."

The US government is scheduled to release the canal into Panamanian government hands on December 31, 1999. Panama has made no decisions about what to do with the canal, valued at between $20 billion and $40 billion, and the subject undoubtedly will be studied and debated for years at both the national and multilateral levels.

The current pro-free-market government of Ernesto Perez Balladares will preside over the decision-making process, and a grand scheme could be well under way even before the canal is Panama's. But since Perez Balladares' term ends September 1, 1999, he may not be around to shepherd the canal through potential privatisation.

Senior Panama Canal Commission (PCC) officials are trying to dispel growing fears in the US Congress that both the canal's attractiveness to ship operators and its competitiveness could diminish after December 31, 1999, when the US must turn over to Panama complete control of the vital waterway.

Concerns about possible privatisation were aired at a US House of Representatives Special Oversight Panel on the Merchant Marine hearing to consider PCC re-authorisation for the financial year from October 1, 1995.

Congressman Gene Taylor, the panel's ranking minority member, demanded assurances that the'canal would not "be used as a 'cash cow' for whatever [Panamanian] government was in power, so that money would not be available for canal maintenance". He said there were concerns "in the US publicly, and in Panama privately" that this would happen.

Current PCC administrator Gilberto Guardia conceded that "this has been a concern of canal users" and "it is also a concern in Panama itself". But he added, "This is one of the areas in which PCC is participating with many groups in Panama regarding the sensitivity of keeping the canal competitive. There is an awareness being developed of the need for keeping this canal efficient and competitive."

He noted that PCC was investing some $125m a year to maintain, modernise and improve canal facilities.

Mr Taylor also cited speculation in the US that PCC would privatise after control passes to Panama.

Mr Guardia said this would "probably not happen". He said "there definitely is not an environment in Panama" that would allow privatisation of the canal, even though government is attempting to privatise many other activities.

Mr Guardia said that further traffic and toll revenue growth was expected this year thanks to continued growth of the US economy, economic recovery in western Europe, signs of a revival in the Japanese economy, and expected expansion of Asian and Latin American trade with Europe and the USA. The current forecast is for 12,675 ocean-going transits (34.7 a day) for 1995, and a 2.1% rise in toll revenues to $428m.

1.5 Foreign investment. In May 1995 Belgian Kredietbank NV bought a small stake in Panama-based Banco Latinoamericano de Exportaciones SA (Bladex) in a move to expand its position in international trade financing. The bank declined to give information on the level of shareholding or other terms of the deal.

Bladex specialises in short-term financing of Latin American exports, mainly by advances to local commercial banks. Its other major shareholders include Latin American central banks and some commercial banks.

A joint Mexican-Panamanian construction firm, Proyectos y Construcciones Panama SA (PYCSA), has won a concession to build and operate two toll roads worth $328m. The cabinet of President Ernesto Perez Balladares approved the concession in late December 1994, in a vote at the Public Works Ministry.

PYCSA is a Panama-based company with majority Mexican investment, officials said. It reportedly outbid another Mexican company, Ingenieros Civiles Asociados SA, for the contract. PYCSA will build a 53-kilometre (31.8-mile) highway linking Panama City to the Atlantic port city of Colon and 17 kilometres (10.2 miles) of a highway skirting Panama City, according to the Public Works Ministry.

According to the contract, PYCSA must finish the highways in less than two years, and will operate them for 30 years. The company will charge a $3.50 one-way toll for the Panama-Colon highway, according to the terms of the deal.

The event marks the first time Panama has awarded a private concession to build and operate a highway. As part of a change in attitude towards privatisation, President Perez Balladares has said he wants to grant concessions to private firms to build and operate ports, highways and parts of the state-run electricity system.

Public Works Minister Luis Blanco has called the new highway project an historic event, since it is the first time the government has been able to carry out a public works project without resorting to debt. In March 1995, however, the ministry announced that the location of the highway would have to be modified because of environmental concerns (2.6).

1.6 International agreements. In early May 1995 Panama concluded a round of negotiations on the rules of the international market as set by the World Trade Organisation (WTO), formerly the General Agreement on Tariffs and Trade (GATT).

In a news conference held by Agricultural Development Minister Carlos Sousa Lennox, the minister argued that the latest rounds of negotiations in Washington and Geneva made it possible to maintain the nation's current level of agricultural production on an open market, though exceptions to the open-market principle were made for maize, rice, poultry and pork. Poultry will pay a tariff 320% over the ordinary duty, and this tariff will gradually drop to 260% in 10 years. A spokesman for the National Association of Panama's Poultry Farmers (Anavip) commented that the agreement will help maintain the country's poultry industry, which is a big consumer of other local inputs such as grain.

As for maize, it was established that the amounts over the normal duty will be subject to a tariff of 99% in the first three years, which will drop to 40% in seven years. Rice will pay a tariff of 150% during the first three years and will drop gradually to the current tariff, 90%, in seven years. The initial tariff on pork will be 90% and will drop gradually to 70% in 10 years.

2.0 Organising an investment

2.6 Environmental law. After awarding a contract to the Mexican-Panamanian construction firm PYCSA (1.5), the Public Works Ministry modified the route where the Panama City-Colon Highway will run, especially regarding its location along the country's northern corridor. While there was no specific environmental code that was being breached, the move reflects increased government sensitivity to ecological issues. Public Works Minister Luis Blanco made the official announcement, saying the decision was made to heed the recommendations by environmental groups. Blanco has affirmed that PYCSA will carry out the agreement signed with the government despite these modifications.

9.0 Capital sources

9.1 Capital sources overview. The National Bank of Panama's (BNP) assets increased 5.7% during 1994, according to the state-run bank. The BNP said in a statement released in the first quarter of 1995 that its assets reached $2.66 billion at the end of 1994, claiming that the increase was due to "fixed-income deposits at local and foreign banks."

Liquid assets stood at $1.42 billion, while deposits were at $2.17 billion. Net profits for the year were $30m, a 42% rise over 1993. The BNP acts as an informal central bank, but does not print money or defend currency because Panama uses the US dollar as legal tender.

10.0 Human resources

10.3 Industrial labour. A number of ship pilots demonstrated in front of the Panama Canal Commission administration building in Balboa in April 1995, claiming that the long hours they work presents a safety threat. The Pilots' Association claims many of its members are now required to work as much as 14 to 18 hours without a break, which is a risk to individual safety and to the Canal, as well as to vessels using the Canal and to the environment. According to the Association, the present strength of the pilot force is sufficient to sustain about 37 transits per day and that at a very minimum, 20 new pilots are required. The Association also claims that a recent study prepared by consultants on behalf of the Panama Canal Commission shows that pilots in Panama are paid about 28% less than pilots working under similar conditions in the USA.

In other labour developments, some 40 Panamanian unions held a one-day nationwide strike in late May 1995 to protest against proposed government labour reforms, although most Panamanians ignored a call for a general work stoppage.

Union leaders said the 24-hour strike was a success and a warning to the government that it should scrap reforms to Panama's labour code that would cut worker benefits.

11.0 Foreign trade

11.1 Foreign trade overview. Panama's banana exports hit record highs during 1994 despite a European quota on Latin American banana imports, authorities said.

According to Panama's National Banana Council, banana exports totalled 41.2m crates during the year, up from 38.3m crates in 1993 and slightly more than the previous record level of 40.7m in 1990.

Earnings from banana exports also hit a record $206m, up 2.4% from the previous high in 1993. The increase was mostly attributed to improved working conditions. Labour stoppages and flooding had plagued production in 1993.

Europe maintains an import quota on Latin American bananas of 2.58m tonnes for 1995. The Banana Council believes that this has caused lower prices in the non-European banana market and squeezed earnings from banana exports, Panama's main export earner.

While Europe still accounts for the bulk of Panama's banana exports, the US market takes up much of the slack: Banana exports to the USA accounted for 20% of the 1994 total, up from 6% in 1993.

11.5 Free ports, zones. Taiwan's Minister of Economic Affairs P.K. Chiang announced on May 30, 1995, that the government plans to build an industrial zone in Panama. Saying that the industrial zone will serve as a base for Taiwanese investors in the region, he indicated that negotiations with the Panamanian government on the project are expected to begin very soon.

The area to be developed is a 300-hectare property that formerly had been an American Army base. The economics minister also indicated that if the investment project is carried out successfully, Panama will serve as a manufacturing centre for Taiwan in the Americas.

Trade through Panama's Colon Free Trade Zone increased 13.61% during the first quarter of 1995, compared with the same period last year, Panama's trade authorities said.

A report by the Colon Free Trade Zone Administration noted that some $2.66 billion worth of goods passed through the duty-free zone during the first three months of the year compared to $2.34 billion during the same period in 1994. Exports through Colon grew by 9%, to $1.25 billion, while imports jumped 18.6% to $1.41 billion, the report said.

The Colon trade zone did some $10.73 billion in trade in 1994, and has grown more than 10% in each of the last five years. Based on the Atlantic entrance to the Panama Canal, the zone is the second-largest free-trade centre in the world next to Hong Kong.

Trade zone officials, however, are worried that a government proposal to place a 1.5% duty tax on imports into the free-trade zone will hurt business and erode the zone's competitiveness against other Latin American free-trade centres.