Economic Substance in Panama: Executive Decree No. 32

Executive Decree No. 32 of September 2, 2026 ("Executive Decree No. 32") develops and clarifies the economic substance rules incorporated into the Tax Code by Law 526 of May 28, 2026. The regime applies to certain foreign-source passive income—including dividends, interest, royalties, capital gains and income from real property, among others—received by entities incorporated or domiciled in Panama that form part of a multinational group. For these purposes, an entity means any legal vehicle, including companies, trusts and foundations. The regime is aligned with international economic substance standards and requires entities receiving this type of income to maintain a genuine presence and conduct substantive activities in Panama. Both the Law and its implementing regulations apply to fiscal periods beginning on or after January 1, 2027.

The principal clarifications introduced by Executive Decree No. 32 are as follows:

1. Human Resources: Article 5 of Executive Decree No. 32 establishes that the human resources devoted to managing assets that generate foreign-source income may not consist of fewer than one person, whether employed or engaged under any arrangement, including through outsourcing.

2. Corporate Governance: Article 6 of Executive Decree No. 32 requires the board of directors or equivalent governing body responsible for strategic decisions to hold at least two in-person meetings in Panama during the corresponding fiscal period, duly supported by documentary evidence, in the case of entities required to comply fully with the economic substance requirements. In addition, strategic decision-making and the assumption of risks may not be delegated, outsourced or subcontracted under any arrangement.

3. Documentation: Article 9 of Executive Decree No. 32 sets out eleven categories of information that must accompany the income tax return, including the payroll of personnel assigned to core activities, details of premises and operating expenses and, where applicable, a description of the intangible assets involved. Such information must be supported by documentation maintained in Panama for five years, in Spanish.

Executive Decree No. 32 also clarifies two areas of uncertainty that had raised concerns for groups with asset-holding structures (i.e. pure holding companies). For entities whose principal activity is holding equity interests or real property that are acquired and disposed of on a non-routine basis, Article 8 of Executive Decree No. 32 develops the simplified regime already contemplated by the Law: it sets out that it is sufficient to demonstrate adequate personnel and premises, without the need for local strategic decision-making or specific operating expenses. Notwithstanding the foregoing, if the entity actively participates in the day-to-day operational decisions of the companies in which it invests, provides financing to unrelated third parties, or engages in regulated financial intermediation, it ceases to qualify as a pure holding entity and becomes subject to all requirements applicable under the substance regime. This is a substance-over-form test. Accordingly, each holding entity should assess its actual operations against the applicable standards.

With respect to outsourcing, Article 11 of Executive Decree No. 32 confirms that economic substance may be demonstrated through service providers located in Panama, provided that certain conditions are met. In particular, the relevant activities must be performed exclusively within Panamanian territory, the service provider must have adequate resources of its own and, where it serves more than one client belonging to the same group, it may not simultaneously count the same personnel working hours toward demonstrating economic substance for more than one entity.

Finally, for income derived from intangible assets registered in Panama—patents, utility models, industrial designs and copyright-protected software, expressly excluding trademarks and image rights—Executive Decree No. 32 establishes a specific calculation formula. Only the portion of income proportional to research and development expenditure actually incurred in Panama, increased by 30%, is excluded from the 15% tax applicable to non-qualifying entities.

Groups must therefore have the required economic substance in place by the start of their 2027 fiscal period and should assess their current situation against the requirements established by Executive Decree No. 32. The first declaration reporting compliance must be filed by March 31, 2028. Alcogal's team is available to assist multinational groups with a presence in Panama in assessing their exposure under Law 526 and Executive Decree No. 32 and in preparing the necessary documentation before the 2027 fiscal period begins. If you would like to discuss the impact of the above on your structure, please do not hesitate to contact us.

This article is intended for general informational purposes only; it does not constitute legal advice with respect to any particular matter.

Frequently Asked Questions About Panama's Economic Substance Regime

1. What is Panama's economic substance regime?

Panama's economic substance regime requires certain entities within multinational groups that receive foreign-source passive income to demonstrate a genuine presence and substantive activity in the country. It was incorporated into the Tax Code by Law 526 of 2026 and regulated by Executive Decree No. 32 of 2026.

2. Which entities must comply with Panama's economic substance regime?

The regime applies to entities incorporated or domiciled in Panama that form part of a multinational group and receive certain types of foreign-source passive income. This income includes, among other categories, dividends, interest, royalties, capital gains and income from real property.

3. What are the principal economic substance requirements in Panama?

The principal requirements include maintaining adequate personnel and premises in Panama and retaining supporting documentation. Entities subject to the full regime must also hold at least two in-person meetings of their board of directors or equivalent governing body in Panama each year. In addition, strategic decision-making and the assumption of risks may not be delegated or outsourced.

4. May the activities required to demonstrate economic substance in Panama be outsourced?

Yes. An entity may demonstrate part of its economic substance through service providers located in Panama, provided that the activities are performed exclusively within the country and the provider has adequate resources of its own. Strategic decision-making and the assumption of risks may not be outsourced.

5. When does Panama's economic substance regime take effect?

Law 526 and Executive Decree No. 32 apply to fiscal periods beginning on or after January 1, 2027. During the transition period, multinational groups may classify their foreign-source passive income, evaluate their current level of economic substance and prepare the required documentation.