



Panama: Political and Economic Conditions and U.S. Relations

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Summary

With five successive elected civilian governments, the Central American nation of Panama has made notable political and economic progress since the 1989 U.S. military intervention that ousted the regime of General Manuel Noriega from power. Current President Ricardo Martinelli of the center-right Democratic Change (CD) party was elected in May 2009, defeating the ruling center-left Democratic Revolutionary Party (PRD) in a landslide. Martinelli was inaugurated to a five-year term on July 1, 2009. Martinelli's Alliance for Change coalition also captured a majority of seats in Panama's National Assembly. Panama's service-based economy has been booming in recent years, largely because of the ongoing Panama Canal expansion project (slated for completion in 2014), but economic growth slowed in 2009 because of the global financial crisis and U.S. economic recession. Nevertheless, the economy rebounded in 2010, with a growth rate approaching 7%, and strong growth is continuing in 2011.

President Martinelli retains high approval ratings, but he has been criticized by some civil society groups for taking a heavy-handed approach toward governing and for not being more consultative. The country experienced labor unrest in July 2010 after the government approved legislation that would have weakened labor laws in several respects, but the government ultimately agreed to repeal the provisions. In February 2011, the government amended the country's mining code to facilitate foreign investment. Indigenous groups protested the law even though President Martinelli vowed that his administration would not approve any mining concessions in indigenous areas. Ultimately, in early March 2011, President Martinelli called for the repeal of the law.

The United States has close relations with Panama, stemming in large part from the extensive linkages developed when the Canal was under U.S. control and Panama hosted major U.S. military installations. The current relationship is characterized by extensive counternarcotics cooperation; support to promote Panama's economic, political, and social development; and a proposed bilateral free trade agreement (FTA). U.S. bilateral assistance amounted to \$7.3 million in FY2010 while the FY2011 request is for \$10.6 million and the FY2012 request for \$2.6 million. This funding does not include assistance in FY2008 and FY2009 under the Mérida Initiative to assist Central American countries in their efforts to combat drug trafficking, gangs, and organized crime; beginning in FY2010, Panama has been receiving assistance under the successor Central America Regional Security Initiative.

The United States and Panama signed a bilateral FTA in June 2007, and Panama's National Assembly approved the agreement in July 2007. Neither the 110th nor the 111th Congress considered the agreement, but the 112th Congress could consider the agreement this session. Issues that have raised congressional concern relate to worker rights and to Panama's tax transparency. In the 112th Congress, several measures have been introduced that would express support for the FTA with Panama: S.Res. 20 (Johanns) and S. 98 (Portman), both introduced January 25, 2011; and H.Res. 86 (Frelinghuysen), introduced February 11, 2011. For additional information, see CRS Report RL32540, *The Proposed U.S.-Panama Free Trade Agreement*, CRS Report R40622, *Agriculture in Pending U.S. Free Trade Agreements with Colombia, Panama, and South Korea*, CRS Report RL34112, *Gangs in Central America*, and CRS Report R41731, *Central America Regional Security Initiative: Background and Policy Issues for Congress*.

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Recent Developments

On April 28, 2011, President Obama is scheduled to meet with President Ricardo Martinelli in Washington, D.C. to discuss next steps regarding the proposed free trade agreement as well as the Central America Security Partnership announced by President Obama in March.

On April 18, 2011, a Tax Information Exchange Agreement (TIEA) between Panama and the United States entered into force. United States Trade Representative Ron Kirk maintained that completion of action on labor and tax transparency issues cleared the way for technical discussions with Members of Congress on the draft implementing bill for the Panama FTA. (See “Tax Haven Status” and “Remaining FTA Issues” below.)

On April 8, 2011, the Department of State issued its 2010 human rights report. The Panamanian government generally respects human rights, although the State Department report noted continued problems in several areas. (The Panama section of the report is available at: <http://www.state.gov/g/drl/rls/hrrpt/2010/wha/154514.htm>. Also see “Human Rights Issues,” below.)

On April 5, 2011, President Martinelli signed into law two pieces of labor legislation. One eliminated the prohibition against the right to strike in companies less than two years old and restrictions on collective bargaining in export processing zones. The second repealed restrictions on collective bargaining rights in the special economic zone of Barú. (See “Remaining FTA Issues,” below.)

On March 30, 2011, the Office of the United States Trade Representative issued the National Trade Estimate Report on Foreign Trade Barrier. (See full text of the report, available at http://www.ustr.gov/webfm_send/2751, with the Panama section on pp. 290-295 of the pdf.)

On March 30, 2011, the House Committee on Ways and Means, Subcommittee on Trade, held a hearing on the Panama free trade agreement, featuring Deputy United States Trade Representative Miriam Sapiro and outside witnesses. (See “Remaining FTA Issues,” below. Also see the testimony at: <http://waysandmeans.house.gov/Calendar/EventSingle.aspx?EventID=230458>.)

On March 17, 2011, the House Committee on Foreign Affairs Subcommittee on the Western Hemisphere, held a hearing on the Colombia and Panama free trade agreements.

On March 3, 2011, the Department of State issued its 2011 International Narcotics Control Strategy Report, which maintained that the Martinelli government “continued Panama’s history of close cooperation with the United States on counternarcotics operations.” (See “Drug Trafficking and Money Laundering,” below. Also see the full text of Volume 1 of the report, available at: <http://www.state.gov/p/inl/rls/nrcrpt/2011/vol1/156362.htm#panama>, and Volume 2, available at: <http://www.state.gov/p/inl/rls/nrcrpt/2011/vol2/156376.htm#panama>.)

Figure 1. Map of Panama



Source: Map Resources. Adapted by CRS.

Political and Economic Conditions

Panama has made notable political and economic progress since the December 1989 U.S. military intervention that ousted the military regime of General Manuel Antonio Noriega from power. The intervention was the culmination of two and a half years of strong U.S. pressure against the de facto political rule of Noriega, commander of the Panama Defense Forces. Since that time, the country has had five successive civilian governments, with the current government of President Ricardo Martinelli of the center-right Democratic Change (CD) party elected in May 2009 to a five-year term. Inaugurated on July 1, 2009, Martinelli is a businessman and former government minister. His electoral alliance, known as the Alliance for Change, also won a majority of seats in the unicameral National Assembly. Panama's largely service-based economy has been booming in recent years, spurred on by the Panama Canal expansion project that begun in 2007 that is expected to be completed in 2014.

From the Endara to the Torrijos Administration

Endara Government (1989-1994)

Before the U.S. intervention, Panama had held national elections in May 1989, and in the presence of a large number of international observers, the anti-Noriega coalition, headed by Guillermo Endara, prevailed by a three-to-one margin. The Noriega regime annulled the election, however, and held on to power. By the fall, the military regime was losing political power and relied increasingly on irregular paramilitary units, making the country unsafe for U.S. forces and U.S. citizens. On December 20, 1989, President George H. W. Bush ordered the U.S. military into Panama "to safeguard the lives of Americans, to defend democracy in Panama, to combat drug trafficking, and to protect the integrity of the Panama Canal Treaty." Noriega was arrested on January 3, 1990, and brought to the United States to stand trial on drug trafficking charges. (Also see "Status of Manuel Noriega," below.)

As a result of the intervention, the opposition coalition headed by Guillermo Endara that had won the May 1989 election was sworn into office. During his term, President Endara made great progress in restoring functioning political institutions after 21 years of military-controlled government, and under his administration, a new civilian Public Force replaced Noriega's Panama Defense Forces. But Endara had difficulties in meeting high public expectations, and the demilitarization process was difficult, with some police and former military members at times plotting to destabilize, if not overthrow, the government.

Pérez Balladares Government (1994-1999)

In May 1994, Panamanians went to the polls to vote in presidential and legislative elections that observers called the freest in almost three decades. Ernesto Pérez Balladares, candidate of the former pro-Noriega Democratic Revolutionary Party (PRD), who led a coalition known as "United People," won with 33% of the vote. Placing a surprisingly strong second, with 29% of the vote, was the Arnulfista Party (PA) candidate, Mireya Moscoso de Gruber, heading a coalition known as the "Democratic Alliance."

In the electoral race, Pérez Balladares campaigned as a populist and advocated greater social spending and attention to the poor. He stressed the need for addressing unemployment, which he termed Panama's fundamental problem. Pérez Balladares severely criticized the Endara government for corruption, and he was able to overcome attempts to portray him as someone closely associated with General Noriega. (Pérez Balladares served as campaign manager during the 1989 elections for candidate Carlos Duque, who the Noriega regime had tried to impose on the electorate through fraud.) Instead, Pérez Balladares focused on the PRD's ties to the populist policies of General Omar Torrijos, whose 12-year (1969-1981) military rule of Panama ended when he died in a plane crash in 1981.

President Pérez Balladares implemented an economic reform program that included liberalization of the trade regime, privatization of state-owned enterprises, the institution of fiscal reform, and labor code reform. Tariffs were reduced to an average of 8%.

Pérez Balladares also worked closely with the United States as the date of the Panama Canal turnover approached. Under his government, Panama and the United States held talks on the potential continuation of a U.S. military presence in Panama beyond the end of 1999 (the date Panama was to assume responsibility for defending the Canal). Ultimately negotiations ended without such an agreement.

Although Panama's constitution does not allow for presidential reelection, President Pérez Balladares actively sought a second term in 1999. In 1997, the PRD had begun studying the possibility of amending the constitution to allow a second bid for the presidency in the May 1999 elections. Ultimately, a referendum was held on the issue in August 1998 but failed by a large margin.

Late in his administration, Pérez Balladares became embroiled in a scandal involving the illegal sale of visas to Chinese immigrants attempting to enter the United States via Panama. As a result, U.S. officials cancelled the former president's U.S. tourist visa in November 1999.¹

Moscoso Government (1999-2004)

In her second bid for the presidency, Arnulfista Party (PA) candidate Mireya Moscoso was victorious in the May 1999 elections. Moscoso, who was inaugurated September 1, 1999, for a five-year term, captured almost 45% of the vote and soundly defeated the ruling PRD's candidate Martin Torrijos (son of former populist leader Omar Torrijos), who received almost 38% of the vote. Until March 1999, Torrijos had been leading in opinion polls, but as the election neared, the two candidates were in a dead heat. A third candidate, Alberto Vallarino, heading a coalition known as Opposition Action, received about 17% of the vote.

President Moscoso, a coffee plantation owner and Panama's first female president, ran as a populist during the campaign, promising to end government corruption, slow the privatization of state enterprises, and reduce poverty. She also promised to ensure that politics and corruption did not interfere with the administration of the Canal. The memory of her husband Arnulfo Arias, a nationalist who was elected three times as president, but overthrown each time, was a factor in the

¹ "Ex-Leader of Panama Linked to Visa Sales," *Washington Post*, November 27, 1999; Pablo Bachelet, "U.S. Uses Visas to Combat Corruption," *Miami Herald*, February 21, 2006.

campaign, particularly since Arias was last overthrown in 1968 by General Omar Torrijos, the father of the PRD's 1999 and 2004 presidential candidate.

Although Moscoso took the presidency, the PRD-led New Nation coalition won a majority of 41 seats in the 71-member unicameral Legislative Assembly. Just days before her inauguration, however, Moscoso was able to build a coalition, with the support of the Solidarity Party, the Christian Democratic Party (which later became the Popular Party), and the National Liberal Party, that gave her government a one-seat majority in the Assembly. In August 2000, the Christian Democrats deserted the coalition and formed an alliance with the principal opposition, the PRD. However, corruption scandals in 2002 led to five PRD legislators defecting to support the Moscoso government, once again giving the president majority support in the Legislative Assembly.

The Moscoso government partially reversed the trade liberalization process of the Pérez Balladares by raising tariffs on some agricultural products, some of which reached the maximum rate allowed under Panama's World Trade Organization obligations.²

As noted above, Moscoso was elected as a populist, with pledges to end government corruption and reduce poverty, but her campaign pledges proved difficult to fulfill amid high-profile corruption scandals and poor economic performance. As a result, the president's popularity declined significantly from a 70% approval rating when she first took office in 1999 to only 15% in 2004.³

Torrijos Government (2004-2009)

In the May 2004 presidential race, Martín Torrijos of the PRD won a decisive victory with 47.5% of the vote, defeating former President Guillermo Endara, who received 30.6% of the vote, and former Foreign Minister José Miguel Alemán, who received 16.4% of the vote. Torrijos' electoral alliance also won a majority of seats in the unicameral National Assembly (formerly known as the Legislative Assembly), 43 out of 78 seats, which should provide him with enough legislative support to enact his agenda. Elected at 40 years of age, Torrijos—the son of former populist leader General Omar Torrijos (1968-1981)—spent many years in the United States and studied political science and economics at Texas A&M University. He served four years under the Pérez Balladares government as deputy minister of interior and justice, and as noted above, became the PRD's presidential candidate in the 1999 elections.

Leading up to the election, Torrijos had been topping public opinion polls, with 42%-49% support. In the campaign, he emphasized anti-corruption measures as well as a national strategy to deal with poverty, unemployment, and underdevelopment. He was popular among younger voters and had a base of support in rural areas. Torrijos maintained that his first priority would be job creation.⁴ He called for the widening of the Canal, a project that would cost several billion dollars, and would seek a referendum on the issue. During the campaign, all three major candidates supported negotiation of a free trade agreement with the United States, maintaining that it would be advantageous for Panama. Endara and Alemán appeared to emphasize the

² United States Trade Representative, *2006 National Trade Estimate Report on Foreign Trade Barriers*, p. 501.

³ "Toss Up Between Torrijos and Endara," *Caribbean and Central America Report*, February 17, 2004.

⁴ Frances Robles, "Ex-leader's Son Wins Presidency in Panama," *Miami Herald*, May 3, 2004.

protection of some sensitive Panamanian sectors such as agriculture, while Torrijos stressed that such an agreement would make Panama's economy more competitive and productive.⁵

During his five years in office, President Torrijos faced such major challenges as dealing with the deficits of the country's social security fund (Caja de Seguro Social, CSS); developing plans for the expansion of the Panama Canal; combating unemployment, poverty, and increasing crime; and contending with the effects of the global financial crisis and U.S. recession on the Panamanian economy.

After protests and a protracted strike by construction workers, doctors, and teachers in June 2005, the Torrijos government was forced to modify its plans for reforming the social security fund. After a national dialogue on the issue, Panama's National Assembly approved a watered-down version of the original plan in December 2005. The enacted reform did not raise the retirement age but will gradually increase required monthly payments into the system and introduces a dual pension system that combines aspects of privatization with the current system.⁶ In mid-December 2007, an almost six-week strike by doctors in the public healthcare system was resolved, with the government offering a 26.7% increase in salaries equivalent and a commitment not to privatize the system.⁷

In April 2006, the government unveiled its ambitious plans to build a third set of locks that would double the Canal's capacity, and allow larger post-Panamax ships to transit the Canal. Panama's Cabinet approved the expansion plan in June, and the National Assembly approved it in July 2006. A referendum on the expansion project took place on October 22, 2006, with 78% supporting the project. The referendum was viewed as a victory for the Torrijos government, which advanced the project as integral to Panama's future economic development and one that helped restore the president's popularity.⁸

The Torrijos government's agenda also included judicial, penal and anti-corruption reforms, as well as an economic development strategy to target poverty and unemployment. The government implemented a new penal code in May 2008 that took a tougher stance on crime by increasing sentences on serious crimes and other measures. In early July 2008, Panama's National Assembly gave President Torrijos powers to carry out security sector reforms over the next two months. In August 2008, President Torrijos enacted five decree laws reorganizing Panama's law enforcement and security services, including the establishment of a National Border Service and a National Intelligence and Security Service (SENIS). Some critics fear that the actions will lead to Panama's re-militarization, while Torrijos maintains that the new agencies are needed to combat growing drug crimes.⁹ In mid-December 2008, the Torrijos government approved additional

⁵ "Panama: Presidential Candidates Remark on FTA with US," *La Prensa* (Panama), January 24, 2004, translated by Foreign Broadcast Information Service.

⁶ Marion Barbel, "Panamanian Congress Approves Modified Social Security Reform," *World Markets Research*, December 22, 2005.

⁷ "Panama: Country Report," *Economist Intelligence Unit*, January 2008, p. 2.

⁸ Richard Lapper, "Good Luck, Good Timing," *Financial Times*, July 24, 2007.

⁹ "Panama: Torrijos to Undertake Security Reform by Decree," *Latin American Weekly Report*, July 3, 2008; "Torrijos Forges Ahead with Security Decrees," *Latin American Regional Report, Caribbean and Central America*, September 2008.

changes to the penal code that increased penalties for the illegal possession of firearms and introduced sentences for attacking a police official.¹⁰

In order to deal with the effects of the global financial crisis, President Torrijos announced the establishment of a \$1.1 billion fund in January 2009 to allow for eased credit access and loans to financial institutions in Panama. The fund—financed with support from the Inter-American Development Bank, the Andean Development Corporation, and the National Bank of Panama—was established in order to counter the tightening of credit because of the global financial crisis.¹¹

Martinelli Government (2009-2014)

May 2009 Elections

Because Panama's Constitution does not allow for immediate reelection, Torrijos was ineligible to run in the May 3, 2009, presidential election, which supermarket mogul and former government minister Ricardo Martinelli of the small center-right Democratic Change (CD) party won in a landslide. Despite strong economic growth and reductions in poverty, support for the Torrijos government in its last year in office eroded because of concerns about rising crime, the effects of the global financial crisis, and problems in improving infrastructure and public services. This contributed to the PRD's poor showing in the 2009 presidential and legislative elections.

While initially in 2008 it appeared that the candidate of the ruling PRD, former housing minister Balbina Herrera, was favored to win, opinion surveys late in the year reflected a significant shift in favor of Ricardo Martinelli. Polls in January 2009 showed Martinelli with 43% support compared to 25% for Herrera and almost 15% for Juan Carlos Varela of the center-right Panameñista Party (PP).¹² In late January 2009, Martinelli and Varela struck a deal to run together in a four-party coalition dubbed the Alliance for Change, with Martinelli leading the ticket and Varela as his running mate. The new alliance further widened Martinelli's lead in opinion polls. Ultimately, Martinelli captured 60% of the vote compared to almost 38% of the vote for Herrera.¹³

Martinelli's Alliance for Change also won a majority of seats in the unicameral National Assembly that will increase the chances that the president will be able to secure enough votes to enact his legislative agenda. The Alliance for Change parties captured 42 out of 71 seats in the legislature, with Martinelli's CD winning 15 and the PP winning 21 seats. The opposition PRD, however, still remains the largest single party in the legislature, with 26 seats although internal divisions could weaken its power.¹⁴ The Alliance for Change coalition faces some internal divisions that could jeopardize its cohesion, especially if President Martinelli's popularity begins to falter.

¹⁰ "Panama: Torrijos Pushes Through Changes to Penal Code," *Latin American Weekly Report*, December 18, 2008.

¹¹ Marion Barbel, "President Unveils U.S. \$1.1 billion Anti-Crisis Fund in Panama," *Global Insight*, January 23, 2009.

¹² "Panama: Martinelli's Presidential Prospects Strengthen," *Latin American Weekly Report*, January 15, 2009,

"Panama Mogul Extends Lead in Election Race – Poll," *Reuters*, January 11, 2009.

¹³ Tribunal Electoral de Panama, "Elecciones Generales del 3 de mayo de 2009."

¹⁴ Asamblea Nacional de Panama, listing of deputies, available at: <http://www.asamblea.gob.pa/diputados/index.html>

Challenges for the Martinelli Government

President Martinelli still retains high approval ratings, measured at over 70% in December 2010,¹⁵ although this strong popularity masks some of the difficulties that the president has faced since taking office. Moreover, the president has been criticized by civil society groups for taking a heavy-handed approach toward governing and not being consultative with civic groups.¹⁶ In early January 2011, a bill initiated by a deputy from President Martinelli's CD that would have amended the constitution to allow for consecutive presidential re-election was rejected by a congressional committee. Panama's next presidential election is scheduled for May 2014. During the 2009 presidential race, Martinelli reportedly agreed that the Panameñista Party would head the coalition in 2014, although some reports indicate that there are concerns that President Martinelli will not adhere to this and might support another candidate.¹⁷

In 2009, a significant economic challenge facing the Martinelli government was dealing with the fallout stemming from the global financial crisis, but the economy weathered the storm and avoided the contraction experienced by many Latin American economies. Panama's service-based economy had been booming in recent years, largely because of the Panama Canal expansion project, but the global financial crisis and the related decline in U.S. import demand stemming from the U.S. recession slowed Panama's economic growth. The economy grew 12.1% in 2007 and 10.1% in 2008. Initially, some economists were predicting that the economy would contract in 2009, but the economy ended up growing an estimated 3.2%. This made Panama's economy one of the few in the region registering positive economic growth in 2009. In 2010, the economy grew even faster, with an estimated growth rate approaching 7%, and the forecast for 2011 is for growth over 6%.¹⁸

Although Panama is categorized by the World Bank as having an upper-middle-income economy because of its relatively high per capita income level of \$6,180 (2008), one of the country's major challenges is highly skewed income distribution with large disparities between the rich and poor.¹⁹ In order to tackle poverty, the previous Torrijos government initiated a social support program of conditional cash transfers to poor families (Red de Oportunidades) and in mid-2008, the government extended the program to include the elderly living in extreme poverty. Poverty rates have been reduced from almost 37% in 2002 to almost 26.4% in 2009. Extreme poverty or indigence in Panama declined from 18.6% in 2002 to 11.1% in 2009.²⁰ Since taking office, President Martinelli has fulfilled his campaign pledge to provide \$100 a month to poor seniors.

During the 2009 presidential campaign, Martinelli pledged to simplify the tax system by the introduction of a flat tax for individuals and for corporations in order to discourage tax evasion. Instead, however, the government enacted two tax reform measures, the first in September 2009 and the second in March 2010, that increased reliance on indirect taxes, reduced income tax rates, and broadened the tax base. These measures are expected to increase government revenue by more than 2%, according to the International Monetary Fund.²¹ The tax reform in March 2010

¹⁵ "Re-Election Motion Chucked Out in Panama," *LatinNews Daily*, January 6, 2011.

¹⁶ "Country Report: Panama," *Economist Intelligence Unit (EIU)*, January 2011, p. 11.

¹⁷ *Ibid.*, p. 10; and "Re-Election Motion Chucked Out in Panama," *LatinNews Daily*, January 6, 2011.

¹⁸ "Country Report: Panama," *EIU*, March 2011, p. 14.

¹⁹ World Bank, *World Development Report 2010*.

²⁰ U.N. Economic Commission for Latin America and the Caribbean, *Social Panorama of Latin America 2010*.

²¹ International Monetary Fund, "Panama: 2010 Article IV Consultation—Staff Report," October 2010, IMF Country (continued...)

reduced corporate and personal income tax rates, and offset the loss of revenue by raising the sales tax from 5% to 7% (not including food) and raising other taxes on banks, casinos, airlines, and the free-trade zone, with a projected net increase in revenue. The government maintains that additional revenue from the reform will be used to augment social expenditures (such as scholarships and cash transfers to the elderly), but critics of the measure maintain that the poor will be hit by an increase in the cost of living. The tax measure in 2010 prompted protests against the government in March, with violent clashes between police and demonstrators, and some 200 people were detained.²² The tax measure, however, also led to an upgrading of Panama's investment-grade credit rating that could improve the country's financing costs and its attractiveness for foreign investment.²³

During the 2009 campaign, Martinelli also called for a number of large public infrastructure projects, including a subway system for Panama City, a light rail system on the outskirts of Panama City, regional airports and roads, and a third bridge over the Canal. The government has already begun to move ahead on some projects. It has set up a body to oversee a plan to construct a subway system in Panama City, and in October 2010 awarded the \$1.4 billion project to a Brazilian and Spanish construction consortium.

Another challenge for the Martinelli government has been dealing with Panama's rising crime, which increased significantly in 2008 and 2009, but declined in 2010. From 2000-2006, the annual homicide rate averaged between 10 and 11 homicides per 100,000 inhabitants.²⁴ The rate subsequently increased from 13 per 100,000 in 2007 to 19 in 2008 and 24 in 2009. Panama had 806 murders in 2009, up 23% from 2008, with drug trafficking the driving force behind the increase.²⁵ During the 2009 electoral campaign, Martinelli proposed a safe streets program that included increasing the number of police and raising police pay. In February 2010, President Martinelli announced an expansion of the national police force with an additional 4,000 officers that would raise the total force to over 15,000.²⁶ In late 2010, Panama's minister of public security said that the number of murders in 2010 had declined about 15% to 692.²⁷

The Martinelli government initiated a number of anti-corruption investigations against officials from the PRD who served in government, including former President Ernest Pérez Balladares (1994-1999), but the PRD maintains that Martinelli is using an anti-corruption crusade to prosecute its political opposition. In late January 2010, Panama's Supreme Court voted to suspend Attorney General Ana Matilde Gomez on allegations of abuse of authority. Gomez had been appointed by the Torrijos government in 2005 to a 10-year post, but the Martinelli

(...continued)

Report No. 10/314.

²² Inti Landauro, "Panama Approves Tax Bill to Boost Revenue, Cut Deficit," *Dow Jones Newswires*, March 16, 2010; Sean Mattson, "Panama: President Ricardo Martinelli Moves His Agenda Forward," *Noticen: Central American & Caribbean Affairs*, March 18, 2010; "Panama Unions Show New Signs of Life," *Latin American Regional Report: Caribbean & Central America*, April 2010.

²³ "Panama: Credit Update," *EIU – Business Latin America*, March 29, 2010.

²⁴ U.N. Development Program, *Informe Sobre Desarrollo Humano Para América Central 2009-2010: Abrir Espacios a la Seguridad Ciudadana y el Desarrollo Humano*, October 2009.

²⁵ "Panama: Drug-Fueled Violence on the Increase," *Noticen, Central American & Caribbean Affairs*, January 28, 2010.

²⁶ "Panama Politics: President's Popularity Slips," *EIU ViewsWire*, March 23, 2010.

²⁷ "Panama, Colombia Build Police Stations on Border to Control Crime," *BBC Monitoring Americas*, December 28, 2010.

government had criticized her for failing to act in cases involving former high-ranking PRD government officials. Gomez's interim successor, Giuseppe Bonissi (reportedly a close associate of Martinelli), resigned in December 2010 after accusations that some government prosecutors had given preferential treatment to suspected drug-traffickers. President Martinelli then appointed career official José Ayú Prado to finish out the rest of Gómez's term until 2015. The appointment reportedly was lauded by civic groups who had feared that President Martinelli would again designate a close ally.²⁸

Some observers have criticized President Martinelli for undermining the independence of the judiciary because of his nomination of two political allies to the Supreme Court in December 2009. The National Assembly quickly approved the nominations, and the two justices took office in January 2010. A complaint on this and the broader issue of problems with Panama's judicial system was heard by the Inter-American Commission on Human Rights in March 2010, with representatives of the Citizens Alliance for Justice (Alianza Ciudadana Pro Justicia). The alliance represents 20 Panamanian civil society organizations dedicated to implementing judicial reform and improving the administration of justice.²⁹ In January 2011, Panama's Supreme Court revived legislation approved in 1999 under the Pérez Balladares government that expanded the court from 9 to 12 judges and established a "court of constitutional guarantees" within the Supreme Court. President Moscoso's government subsequently repealed the legislation expanding the court and the membership of the court returned to 9 members. But in January 2011, the Supreme Court declared the Moscoso government's action unconstitutional so that the court will return to 12 members. Critics maintain that it will give President Martinelli more influence over the court.³⁰ In mid-April 2011, Supreme Court Justice José Abel Almengor resigned after accusations emerged that he had conspired to unseat former Attorney General Ana Matilde Gomez.³¹

In July 2010, Panama experienced labor unrest in response to controversial legislation that would have allowed companies to suspend contracts of striking workers, allowed companies to hire replacement workers during strikes, and ended the obligatory payment of union dues. Two striking workers in the banana sector were killed in clashes with police in Bocas del Toro and hundreds were injured. The strike was suspended after the Martinelli government agreed to suspend some of the controversial aspects of the law. In October 2010, the government agreed to repeal the controversial labor provisions as well as provisions that would have relaxed environmental standards. The law had included provisions that would have allowed the government to eliminate environmental-impact studies for public works deemed of "social interest."³²

On February 10, 2011, Panama's National Assembly approved legislation initiated by the Martinelli government that amended the country's mining law to facilitate foreign government investment in the sector. Changes to the law were reportedly motivated by plans of Canada's

²⁸ "Country Report: Panama," *EIU*, January 2011, p. 9; "People Profile, José Eduardo Ayú Canals, Panama," *Latin NewsDaily*, January 25, 2011

²⁹ See the website of the Citizens Alliance for Justice at: <http://www.alianzaprojusticia.org.pa/>; The Washington, D.C.-based Due Process of Law Foundation has also done work on the issue of Panama's judicial system. For more information, see: http://www.dplf.org/index.php?c_ID=395&catID=1

³⁰ "Country Report: Panama," *EIU*, February 2011, p. 10.

³¹ "Country Report: Panama," *EIU*, April 2011, p. 10.

³² Sean Mattson, "Panamanian President Ricardo Martinelli Reverses Course on Controversial Legislation," *Noticen, Central & Caribbean Affairs*, November 11, 2010; "Panama: Martinelli Performs Major U-Turn," *Latin American Regional Report, Caribbean & Central America*, October 2010.

Inmet Mining company to secure financing from Singapore and South Korea for a mining project known as Cobre Panama.³³ Indigenous and environmental groups protested the amendment of the mining law and called for its repeal. President Martinelli vowed that his administration would not approve any mining concession in indigenous areas, including in the Cerro Colorado, believed to hold the country's largest copper reserves, which lies in the indigenous Ngöbe-Buglé comarca (semi-autonomous region) in Chiriquí province. Despite Martinelli's action, indigenous and environmental groups vowed more protests, with some calling for a referendum to settle the dispute.³⁴ Ultimately, on March 3, 2011, in response to indigenous protests and concerns over the mining law, the President relented and called for its repeal, which was completed on March 18. The government maintains that the repeal of the law will not affect the development of the Cobre Panama project.³⁵

Human Rights Issues

The Panamanian government generally respects human rights, but, as noted by the State Department in its 2010 human rights report (issued in April 2011), human rights problems continue in a number of areas. Among the problems cited was excessive force used by police during protests. In July 2010, two protestors were killed during labor protests in clashes with security forces, and hundreds of people were injured. Other problems cited included: harsh prison conditions; prolonged pretrial detention; corruption, ineffectiveness, and alleged political manipulation of the judicial system; corruption in the executive and legislative branches and security forces; discrimination and violence against women and other forms of societal discrimination; trafficking in persons; and violations of some worker rights.

Administration of Justice. As noted above, there has been some criticism in Panama regarding the administration of justice and the independence of the judicial branch. Some observers have criticized President Martinelli for undermining the independence of the judiciary because of his nomination of two political allies to the Supreme Court in December 2009. A complaint on the issue regarding the justice system was heard by the Inter-American Commission on Human Rights on March 23, 2010, with representatives of the Citizens Alliance for Justice (Alianza Ciudadana Pro Justicia). The alliance represents 20 Panamanian civil society organizations dedicated to implementing judicial reform and improving the administration of justice.³⁶ The State Department's human rights report maintained that the judiciary was subject to corruption and outside influence and reportedly was manipulated by other branches of government.

Freedom of the Press. In past years, Panama had been criticized by the State Department and international human rights groups for vestiges of "gag laws" used by the government to silence those criticizing policies or officials, but the legislature repealed these laws in May 2005. Nevertheless, the legislature approved penal code amendments in May 2007 that allow for the prosecution of journalists who violate the privacy of public officials or who publish classified

³³ "Panama: Martinelli Hits Another Nerve," *Latin American Weekly Report*, February 24, 2010.

³⁴ "Decree Fails to Resolve Panama Mining Row," *Agence France Presse*, February 23, 2011.

³⁵ "Govt Assures Inmet That Repeal of Law 8 Will Not Affect Current Contracts, Concessions," *Business News Americas*, March 24, 2011.

³⁶ See the website of the Citizens Alliance for Justice at: <http://www.alianzaprojusticia.org.pa/>; The Washington, D.C.-based Due Process of Law Foundation has also done work on the issue of Panama's judicial system. For more information, see: http://www.dplf.org/index.php?c_ID=395&catID=1

information. The new penal code went into effect in May 2008. Nongovernmental organizations assert that the new code threatens freedom of speech and press.

As noted in the State Department's 2010 human rights report, the government has used a variety of means to impede freedom of expression and attempt to silence criticism of its actions. International press rights groups such as the Committee to Protect Journalists and Reporters Without Borders have expressed concern about several cases.

In September 2008, a judge ordered the seizure of a local newspaper, *El Periódico*, because it published the tax returns of a prominent businessman. The paper subsequently went out of business, but the case remains under appeal.

In February 2009, a Panamanian court sentenced Jean Marcel Chéry, the director of the daily *El Siglo*, to two years in prison for trespassing in connection with reporting on alleged corruption involving a Supreme Court Justice. Chéry is still appealing the decision, but he and the other two journalists have not been imprisoned since the law requires commutation of sentences into fines in cases where a final ruling has not been made within two years. In May 2010, Chéry filed a complaint with the Inter-American Commission on Human Rights alleging that the government had launched a campaign of intimidation after his newspaper ran a story on government failure to collect garbage in poor neighborhoods of Panama City.

In September 2009, a Panamanian court convicted a journalist from *La Prensa* of libel against a former vice president, and the case remains under appeal. In May 2010, the Supreme Court fined *La Prensa* for "moral damages" after it reported on the 2005 firing and subsequent reinstatement of a prosecutor; the case remains under appeal.

In late September 2010, a Panamanian court convicted two television journalists of defamation and banned them from working as journalists for a year, although President Martinelli subsequently issued a pardon after their conviction. Press rights groups welcomed Martinelli's action, but called for legal reforms to fully decriminalize defamation.³⁷

In early January 2011, a draft law that would have allowed anyone convicted of insulting the president or an elected official to be sentenced to prison was withdrawn from consideration in the National Assembly. The bill had been criticized by journalists and press rights groups, and President Martinelli had warned that he would veto the measure.³⁸

Past Human Rights Abuses Under Military Rule. In an attempt to redress human rights abuses that occurred under military rule (1968-1989) and to prevent their recurrence, the Moscoso government established a Truth Commission in 2001 that documented 70 cases of murder and 40 disappearances, but progress has been slow in investigation and prosecution of these cases. In 2008, Panama's attorney general announced that investigations had either been opened or reopened in 47 of these cases because of new evidence. According to the State Department's 2009 human rights report, more than half of these cases have been temporarily dismissed or closed, but 19 were at various stages of the trial process. The 2010 State Department human rights report maintained that a number of cases remain underway or under consideration.

³⁷ "In Panama, Defamation Conviction Draws Outcry," Committee to Protect Journalists, October 7, 2010.

³⁸ "Withdrawal of Proposal to Introduce Jail Terms for Insulting the President," Reporters Without Borders, January 12, 2011.

In 2008, the Panamanian government opened an investigation into the alleged killings of more than 20 persons who reportedly were thrown from helicopters in the Darién region in 1982-1983. The State Department's 2010 human rights report maintained that there were no known developments in investigations.

In November 2009, Panama's attorney general asked a court to call to trial former Minister of Government and Justice Daniel Delgado for a killing in 1971 when he was a member of Panama's National Guard. The Supreme Court acceded to the request, but a court date has not been set.

In July 2006, just as a human rights trial was approaching an end, a former military officer implicated in the 1970 killing of activist Heliodoro Portugal died from an apparent heart attack. In September 2008, the Inter-American Commission on Human Rights ordered the Panamanian government to pay restitution to the family of Portugal. In April 2010, a Panamanian court agreed to try eight former members of the National Guard, including former Manuel Antonio Noriega, for alleged involvement in the disappearance and killing of Portugal.

Displaced Persons. Over the years, violence from the civil conflict in neighboring Colombia has resulted in thousands of displaced persons seeking refuge in the neighboring Darién province of Panama. Many of the Colombians have lived in Panama for years, have given birth to children in Panama, and do not want to return to Colombia because of family and cultural ties to local Panamanian communities. According to the Department of State, the Panamanian government restricts the movement of some 1,200 Colombians in the Darién region covered under "temporary humanitarian protection." While the majority of the displaced are Afro-Colombians, there have also been indigenous people from Colombia who have fled to Panama because of the violence.

In addition to those under "temporary humanitarian protection," the State Department's 2010 human rights report notes that there were 1,213 officially recognized refugees in Panama, while the Office of the U.N. High Commissioner for Refugees (UNHCR) classifies some 15,000 people in Panama as "persons of concern" in need of international protection. (Some nongovernmental organizations maintain that the number could be as high as 75,000.³⁹) UNHCR has a permanent office in Panama and was generally allowed access to provide services to refugees, internally displaced persons, and persons under temporary humanitarian protection.

In April 2008, UNHCR lauded Panama for the approval of a new law that allows long-standing refugees (those residing 10 years or more) the opportunity to apply for permanent residency until November 2010. According to UNHCR, the new law largely affected refugees from Nicaragua and El Salvador who arrived in Panama during the Central American conflicts of the 1980s.⁴⁰ According to the State Department's 2010 human rights report, 277 out of 300 applications for permanent residency were approved under the law by the time of its expiration.

Worker Rights. With regard to worker rights in Panama, the State Department's 2010 human rights report notes that while Panamanian law recognizes the right of private-sector workers to form and join unions of their choice, the law requires a minimum of 40 persons to form a union, and only one trade union is allowed per business. The International Labor Organization (ILO) Committee of Experts criticizes both provisions as violations of workers' rights to organize.

³⁹ Refugee Council USA, *Living on the Edge: Colombian Refugees in Panama and Ecuador*, 2011.

⁴⁰ "UNHCR Welcomes New Panama Law," *UNHCR Briefing Notes*, April 1, 2008; and UNHCR, "Panama," September 2010.

Public servants may not form unions, but they may form associations, which can bargain collectively, and there is a limited right to strike with the exception of those areas vital for public welfare and security. The National Federation of Public Servants (FENASEP), an umbrella organization of 21 public-sector worker associations, is not permitted to call strikes, and the ILO has expressed concerns about this. As noted above, Panama experienced labor unrest in July 2010 after the government approved legislation weakening labor laws in several respects, but the government subsequently repealed those provisions. The State Department report also noted that child labor was a problem, with violations occurring most frequently in rural areas at harvest time and in the informal sector, but the report also described efforts by the government to combat the problem. This has included adoption of a national plan to eliminate the worst forms of child labor by 2015 and all illegal child labor by 2020. (For additional discussion of labor issues raised in the context of the proposed free trade agreement, see “Remaining FTA Issues,” below.)

Human Trafficking. According to the State Department’s 2010 Trafficking in Persons (TIP) report, issued in June 2010, Panama is a source, transit, and destination country for women and children trafficked domestically for commercial sexual exploitation. Non-governmental organizations report that some Panamanian children are subjected to involuntary domestic servitude. The report maintained that the government showed little evidence of progress in combating human trafficking, with weak law enforcement, no penal code prohibition against forced labor, and failure to provide adequate assistance to trafficking victims and to identify trafficking victims among vulnerable populations. As a result, Panama was placed on the Tier 2 Watch List.⁴¹

Panama previously had been on the State Department’s Tier 2 Watch List in 2008 for failing to show evidence of increasing efforts to combat human trafficking and for failing to provide adequate victim assistance. After the 2008 TIP report was issued, the government increased prevention efforts, enacted a legislative reform package to strengthen its anti-trafficking laws, and eliminated a special visa category that had been used to facilitate the trafficking of Colombian women into the sex trade. As a result Panama was placed on the Tier 2 List in June 2009 because of the government’s anti-trafficking efforts.

U.S.-Panama Relations

Since the 1989 U.S. military intervention that ousted the regime of General Manuel Antonio Noriega from power (see “Background on the 1989 U.S. Military Intervention”), the United States has had close relations with Panama, stemming in large part from the extensive history of linkages developed when the Panama Canal was under U.S. control and Panama hosted major U.S. military installations. Today, about 27,000 U.S. citizens reside in Panama, many retirees of the former Panama Canal Commission, and there are growing numbers of other American retirees in the western part of the country.⁴²

The current U.S. relationship with Panama is characterized by extensive cooperation on counternarcotics efforts; support to promote Panama’s economic, political, and social development; and a proposed bilateral free trade agreement (FTA) that was signed in 2007.

⁴¹ U.S. Department of State, “Trafficking in Persons Report,” June 2010. Also see CRS Report RL33200, *Trafficking in Persons in Latin America and the Caribbean*, by Clare Ribando Seelke.

⁴² U.S. Department of State, Background Note: Panama, September 16, 2010.

Panama is seeking the FTA because it would make trade rules with the United States permanent, and perhaps more significantly, because it would be a means to increase U.S. investment in the country. The United States has stressed that an FTA with Panama, in addition to enhancing trade by giving the United States greater access to Panama's growing market, would also provide greater access to Panama's large services market. According to the U.S. officials, Panama's strategic location as a major shipping route (with about 10% of U.S. international trade passing through the Canal), enhances the significance of the FTA for the United States.⁴³

The United States turned over control of the Canal to Panama at the end of 1999, according to the terms of the 1977 Panama Canal Treaty, at which point Panama assumed responsibility for operating and defending the Canal. All U.S. troops were withdrawn from Panama at that time and all U.S. military installations reverted to Panamanian control. However, under the terms of the Treaty on the Permanent Neutrality and Operation of the Panama Canal, or simply the Neutrality Treaty, the United States retains the right to use military force if necessary to reopen the Canal or restore its operations.

U.S. Foreign Aid and Other Support

Because of Panama's relatively high per capita income level, the United States has not provided large amounts of foreign aid to Panama in recent years. Nevertheless, aid has included development assistance to improve business competitiveness and trade-led economic growth; child, survival, and health assistance to help in the fight against HIV/AIDS; and security assistance to improve Panama's counterterrorism capabilities, security programs, and maritime interdiction. In recent years, U.S. bilateral assistance (not including Peace Corps assistance) amounted to \$3.7 million in FY2008, \$7.6 million in FY2009, and \$7.3 million in FY2010.

For FY2011, the Obama Administration requested \$10.6 million in assistance for Panama, including \$7.5 million in Development Assistance and \$2.1 million in Foreign Military Financing (FMF). According to the State Department's FY2011 Congressional Budget Justification for Foreign Operations, the United States will work in partnership with Panama to advance common interests in improving citizen safety, strengthening democratic institutions, enhancing the health and education of all citizens, addressing income inequality, and supporting sustainable economic growth. Congressional action on FY2011 assistance has not yet been completed. FY2012, the Administration did not request any Development Assistance, but requested \$2.79 million in assistance, with \$1.8 million in FMF and \$800,000 in International Military Education and Training (IMET).

These figures for regular bilateral assistance do not reflect additional assistance that Panama has been receiving since FY2008 under the Mérida Initiative, a program providing assistance to Mexico and Central American countries in their efforts to combat drug trafficking, gangs, and organized crime. In March 2009, Panama and the United States signed a letter of agreement for \$2 million in funding under the initiative; overall, Panama will receive an estimated \$11 million in Mérida Initiative assistance for FY2008/2009. For FY2010, instead of funding under the Mérida Initiative, Panama is receiving a portion of the \$95 million in assistance under the Central America Regional Security Initiative (CARSI), a successor to the Mérida Initiative for Central

⁴³ Office of the United States Trade Representative, Statement by Ambassador Miriam Sapiro, Deputy United States Trade Representatives, Statement before the House Committee on Ways and Means, Subcommittee on Trade, March 30, 2011.

America.⁴⁴ For each of FY2011 and FY2012, the Obama Administration requested \$100 million in assistance for CARSI. The lack of details for actual and proposed country funding for Panama under the Mérida Initiative and CARSI makes it difficult to provide an overall picture of U.S. assistance going to Panama.

A number of U.S. agencies provide support to Panama. The U.S. Agency for International Development has a mission in Panama administering U.S. foreign aid programs, and the Peace Corps has over 180 volunteers in the country working on a range of development projects. The State Department, the Drug Enforcement Administration, the U.S. Coast Guard, and the Department of Homeland Security are involved in providing counternarcotics support to Panama. The Department of Health and Human Services provided support in 2007 to launch a Regional Training Center for health-care workers in Panama City that trains students from throughout Central America. The U.S. Southern Command (Southcom) also provides support to Panama through military exercises providing humanitarian and medical assistance, and at times provides emergency assistance in the case of natural disasters such as floods or droughts. Southcom also has sponsored annual multinational training exercises since 2003 focused on the defense of the Panama Canal. Panama also hosts the Smithsonian Tropical Research Institute dedicated to studying biological diversity.

Port Security and Other Counterterrorism Efforts

Panama also participates in the Container Security Initiative (CSI) operated by the U.S. Customs and Border Protection of the Department of Homeland Security, and the Megaports Initiative run by the National Nuclear Security Administration of the Department of Energy. Three Panamanian ports—Balboa, Colón, and Manzanillo—participate in the CSI, while those three ports plus the port of Cristobal participates in the Megaports Initiative. The CSI uses a security regime to ensure that containers that pose a potential risk for terrorism are identified and inspected at foreign ports before they are placed on vessels destined for the United States. The Megaports Initiative involves deploying radiation detection equipment in order to detect nuclear or radioactive materials.

The State Department's Country Reports on Terrorism, 2009, issued in August 2010, maintained the main terrorist concerns in Panama remained the presence of the Revolutionary Armed Forces of Colombia (FARC) in the Darién province bordering Colombia and potential actions against the Panama Canal. The report noted that Panama continued to work in both areas. A small number of FARC members from the guerrilla group's 57th Front were reported to operate in the Darién, using the area as a safe haven and drug trafficking base. The members also were responsible for the kidnapping of a U.S.-Cuban citizen near Panama City in April 2008 who was held until February 2009. Panama turned over several FARC members to the United States for prosecution in 2009. In January 2010, three FARC members were killed and two were captured in a clash with Panamanian forces in the Darién. In late 2010, Panama and Colombia agreed to establish police stations near each side of the border in order.

With regard to the Panama Canal, the United States and Panama have continued to work together to plan for potential incidents that could close the Canal. Since 2003, Panama has participated in annual PANAMAX exercises with the United States and a number of other Latin American

⁴⁴ For additional information on CARSI, see CRS Report R41731, *Central America Regional Security Initiative: Background and Policy Issues for Congress*, by Peter J. Meyer and Clare Ribando Seelke.

countries focused on ensuring the security of the Canal. The most recent exercise was held in August 2010 involving 16 nations in the region in addition to the United States and Panama.

Drug Trafficking and Money Laundering

An important concern for U.S. policymakers over the years has been securing Panamanian cooperation to combat drug trafficking and money laundering.

Panama is a major transit country for illicit drugs from South America to the U.S. market because of its geographic location and its large maritime industry and containerized seaports. The State Department's March 2011 *International Narcotics Control Strategy Report (INCSR)* maintains that Colombian and Mexican drug trafficking operations (DTOs) located in Panama, along with Colombia's FARC operating in the remote Darién region, actively seek to move drugs through Panamanian territory. Traffickers use Panama's coastline and its transportation infrastructure, including four major containerized seaports, the Pan-American highway, and Panama City's international airport to facilitate the movement of illicit drugs.

In the March 2011 *INCSR*, the State Department maintains the Martinelli government is continuing Panama's history of close cooperation with the United States on counternarcotics operations. Panama seized 49.5 metric tons of cocaine in 2010, compared to 54 metric tons in 2009. Since 2009, the Martinelli government has established several air and naval anti-drug bases on both the Pacific and Caribbean sides of the country in an effort to increase the ability of its security forces to interdict suspected trafficking vessels.

U.S. counternarcotics support has included programs to improve Panama's ability to intercept, investigate, and prosecute illegal drug trafficking; strengthen Panama's judicial system; improve Panama's border security; and promote strict enforcement of existing laws. The United States also has provided resources to modernize, train, and maintain vessels and facilities of the National Air-Naval Service (SENAN), the National Border Service (SENAFRONT), the National Police (PNP), and the newly created Ministry of Public Security; assisted with training and maintenance for aircraft involved in interdiction efforts; supported and encouraged Panamanian jungle-survival training by Colombian police; and supported reform efforts for all of Panama's security services to combat corruption. Looking ahead, the State Department encourages Panama to devote more resources to the modernization of its security and justice services and to continue with reform efforts that improve public sector accountability and transparency.

In addition to being a transit country, Panama's service-based economy, with a large financial sector and free trade zone, the Colón Free Zone (CFZ), makes the country vulnerable to money laundering. According to the State Department (in its 2010 *INCSR*), the majority of money laundering in Panama relates to proceeds from drug trafficking (especially the sale in the United States and Europe of cocaine produced in Colombia) or from the transshipment of smuggled, pirated, and counterfeit goods through the CFZ.

Panama has made significant progress in strengthening its anti-money-laundering regime since June 2000, when it was cited as a non-cooperative country in the fight against money laundering by the Financial Action Task Force (FATF), a multilateral anti-money-laundering body. Subsequently, the government undertook a comprehensive effort to improve its anti-money-laundering regime by enacting two laws and issuing two decrees in 2000. As a result of these efforts, the FATF removed Panama from its non-cooperative country list in June 2001.

According to the 2011 *INCSR*, Panama has made progress over the past year on the policy front in improving the transparency of its financial system. The government is moving to ensure its removal from the OECD's gray list. It signed a Tax Information Exchange Agreement (TIEA) with the United States in November 2010 and has signed a number of double taxation agreements with other countries. (Also see "Tax Haven Status" and "Remaining FTA Issues," below.) For a number of years, the State Department has expressed concern in the 2011 *INCSR* about Panama's use of bearer shares, often associated with money laundering, and maintained that the government should take steps to eliminate or immobilize these financial instruments. Panama took action on this issue on February 1, 2011, when President Martinelli signed into law bearer shares or "know your client" legislation.⁴⁵

Nevertheless, while Panama has made significant progress in improving its anti-money laundering regime, the State Department maintains in the 2011 *INCSR* that the government's lack of enforcement has undercut this progress. It notes that Panama's judicial system has not sentenced anyone under the current money laundering laws. The *INCSR* encourages Panama to continue enhancing its efforts to prevent, detect, investigate, and prosecute financial crimes and money laundering.

Tax Haven Status⁴⁶

While there is no single accepted definition for a tax haven, the Organization for Economic Co-operation and Development (OECD) has stated four criteria can be used to identify tax haven jurisdictions.⁴⁷ The criteria are no or nominal taxes and three criteria related to transparency and the exchange of information.

Whereas the OECD recognized that the determination of appropriate tax policy is a national concern, the organization has stated that the areas of transparency and information exchange require a multilateral solution. Following this belief, the OECD has an ongoing project, the Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum), working to increase transparency and information exchange.⁴⁸ In April 2002, Panama committed itself to meet the OECD principles on transparency and information exchange, thus averting a designation as a non-cooperative tax haven.

As of February 2011, Panama remained on the OECD's so-called "gray list" as one of just six remaining jurisdictions worldwide that have committed to the internationally agreed tax standard to help prevent tax evasion, but that have not yet substantially implemented the standard.⁴⁹ To date, however, Panama has made significant progress in moving toward implementing that tax standard. Since late 2009, it has negotiated agreements with 11 countries for the exchange of tax

⁴⁵ Information provided to CRS by the Department of State, February 15, 2011.

⁴⁶ Prepared by Donald J. Marples, Specialist in Public Finance, ext. 7-3739

⁴⁷ A full discussion of the criteria can be viewed at http://www.oecd.org/document/23/0,3343,en_2649_33745_30575447_1_1_1_1,00.html and a broader discussion of tax havens can be found in CRS Report R40623, *Tax Havens: International Tax Avoidance and Evasion*, by Jane G. Gravelle.

⁴⁸ For background, see as CRS Report R40114, *The OECD Initiative on Tax Havens*, by James K. Jackson.

⁴⁹ Organization for Economic Co-operation and Development, "A Progress Report on the Jurisdictions Surveyed by the OECD Global Forum in Implementing the Internationally Agreed Tax Standard," April 7, 2011, up-to-date list available at: <http://www.oecd.org/dataoecd/50/0/43606256.pdf>.

information. These include double taxation agreements with 10 countries,⁵⁰ and most significantly, a Tax Information Exchange Agreement (TIEA) with the United States signed in November 2010. Jurisdictions that have signed at least 12 such agreements for the exchange of tax information are considered by the OECD to have substantially implemented the tax standard and are removed from the “gray list.” Panama has additional double taxation agreements in the works and their conclusion could lead to the country being removed from the “gray list.” It should be noted, however, that even if Panama is removed from the OECD’s “gray list,” the country would still be subject to Global Forum peer reviews of its legal and regulatory system for the exchange of information for tax purposes.⁵¹

As noted below (see “Remaining FTA Issues”), Panama’s National Assembly approved “know your client” legislation in early February 2011 requiring the identification of the owners of bearer shares, an action set forth in the joint declaration to the U.S.-Panama TIEA. The TIEA entered into force on April 18, 2011, and covers all civil and criminal tax matters for tax years beginning after November 30, 2007.⁵² In addition, Panama does have a Mutual Legal Assistance Treaty (MLAT) with the United States, which covers the exchange of tax information if the income is effectively tied to an illegal activity, such as unreported income from drug trafficking.

It is not clear the extent to which Panama is used as a corporate tax haven. According to the most recent IRS data, 159 U.S. corporations have subsidiaries in Panama. This accounts for less than 2% of all U.S. corporations. Focusing on larger corporations, 18 of the 100 largest publicly traded companies and 14 of the 100 largest federal contractors had subsidiaries in Panama.⁵³ The revenue cost of these subsidiaries to the United States is unknown.

Panama’s corporate tax is more similar to the United States’ than other possible tax havens. The Panamanian corporate tax rate of 27.5% is at nearly the level of the top U.S. corporate tax rate of 35%.⁵⁴ In comparison, other commonly cited tax havens, such as the Cayman Islands, do not levy a tax on corporate income. As a result, the corporate tax rate is unlikely the motivating factor for the location of U.S. subsidiaries in Panama.

Non-tax factors could provide motivation for U.S. corporations to have subsidiaries in Panama. In the case of Panama, it, along with Liberia, is commonly used as a flag of convenience. Traditional reasons for choosing a flag of convenience include protection from income taxes, wage scales, and regulations. A specific example of the type of advantage flying a flag of convenience offers is bypassing the 50% duty the United States government charges on repairs performed on

⁵⁰ The 10 countries are Mexico, Barbados, Portugal, Qatar, Luxemburg, Netherlands, Singapore, Spain, South Korea, and Italy. Three additional double taxation agreements with France, Belgium, and Ireland are reportedly in the works. See: CRS Report RL32540, *The Proposed U.S.-Panama Free Trade Agreement*, by J. F. Hornbeck.

⁵¹ In September 2010, the OECD published a phase 1 peer review report that highlighted significant problems with Panama’s legal and regulatory framework for transparency and exchange of information for tax purposes as of May 2010. See: Global Forum on Transparency and Exchange of Information for Tax Purposes, “Peer Review Report, Phase 1, Legal and Regulatory Framework: Panama,” September 2010.

⁵² U.S. Department of the Treasury, “Treasury: U.S.-Panama Tax Information Exchange Agreement Now in Effect,” Press Release, April 18, 2011, available at: <http://www.treasury.gov/press-center/press-releases/Pages/tg1144.aspx>

⁵³ U.S. Government Accountability Office, *International Taxation: Large U.S. Corporations and Federal Contractors with Subsidiaries in Jurisdictions Listed as Tax Haven or Financial Privacy Jurisdictions*, GAO-09-157, December 18, 2008.

⁵⁴ In 2012 the Panamanian corporate income tax rates is scheduled to fall to 25%. In addition, companies in the energy, telecommunication, financial, insurance, banking, and mining industries are currently taxed at a rate of 30%, falling to 27.5% in 2012, and 25% in 2014.

American-flagged ships in foreign ports. Other non-tax factors could also motivate U.S. corporations to have subsidiaries in Panama.

Over the years, Panama's lack of tax transparency and information exchange agreements could have been factors in making the country a destination for tax evasion. In 2007 testimony before the Senate Committee on Finance, several speakers commented that a lack of transparency and strong bank secrecy laws were commonly found in tax evasion destinations.⁵⁵ Other commentators specifically identified Panama as being an ideal location for tax evasion activities.⁵⁶ However, Panama's recent negotiation of tax sharing agreements with a number of countries, including a TIEA with the United States that entered into force in April 2011, and its recent passage of "know your client" legislation could be factors that deter the country from being used as a destination for tax evasion.

U.S. Trade Relations

Panama has largely a service-based economy, which historically has run a merchandise trade deficit with the United States. In 2010, the United States ran a \$5.7 billion trade surplus with Panama, exporting almost \$6.1 billion in goods and importing \$379 million. Panama was the 36th-largest U.S. export market in 2010. Panama's major exports to the United States include fish and seafood, gold, sugar, and fresh fruits. Major imports include oil, machinery and other capital goods, consumer goods, and foodstuffs.⁵⁷ The stock of U.S. direct foreign investment in Panama was estimated at \$7.8 billion in 2009, with over 60% concentrated in depository institutions and holding companies. This almost equaled the combined U.S. foreign investment in the five other Central American nations.⁵⁸

With the exception of two years (1988-1989), when the United States was applying economic sanctions on Panama under General Noriega's rule, Panama has been a beneficiary of the U.S. preferential import program known as the Caribbean Basin Initiative (CBI), begun in 1984. The program was amended several times and made permanent in 1990. CBI benefits were expanded in 2000 with the enactment of the Caribbean Basin Trade Partnership Act (CBTPA) (Title II, P.L. 106-200), which provided NAFTA-equivalent trade benefits, including tariff preferences for textile and apparel goods, to certain CBI countries, including Panama. In May 2010, Congress approved an extension of CBTPA benefits through September 2020 (P.L. 111-171). The program continues in effect until then, or the date on which a free trade agreement enters into force between the United States and a CBTPA beneficiary country.

Potential Free Trade Agreement

Panama and the United States began negotiations for a free trade agreement in April 2004. There had been expectations that the negotiations would be completed in early 2005, but continued contention over several issues and a lengthy hiatus prolonged the negotiations until December

⁵⁵ U.S. Congress, Senate Committee on Finance, *Offshore Tax Evasion: Stashing Cash Overseas*, 110th Cong., 1st sess., May 3, 2007.

⁵⁶ Martin A. Sullivan, "Ah, Panama," *Tax Notes*, June 25, 2007, p. 1246.

⁵⁷ Department of Commerce statistics, as presented by Global Trade Atlas.

⁵⁸ U.S. Department of Commerce, Bureau of Economic Analysis, "U.S. Direct Investment Abroad Tables," *Survey of Current Business*, September 2010, p. 71.

2006. Issues included market access for agricultural products, considered sensitive by Panama; procurement provisions for the Panama Canal Authority regarding expansion activities; and sanitary control systems governing the entry of U.S. products and animals to the Panamanian market. Negotiations were suspended for some time in 2006 until after Panama held its Canal expansion referendum in October, but a 10th round led to the conclusion of negotiations on December 19, 2006.

Under the proposed agreement, over 88% of U.S. exports of consumer and industrial goods would become duty-free immediately, while remaining tariffs would be phased out over 10 years. Over 50% of U.S. agricultural exports to Panama would become duty-free immediately, while tariffs on most remaining farm products would be phased out within 15 years. In December 2006, Panama and the United States also signed a bilateral agreement on sanitary and phytosanitary measures in which Panama will recognize the equivalence of the U.S. food safety inspection to those of Panama and will no longer require individual plant inspections. Under the FTA, U.S. companies would be guaranteed a fair and transparent process to sell goods and services to Panamanian government entities, including the Panama Canal Authority.⁵⁹

When the negotiations were concluded, then-U.S. Trade Representative Susan Schwab stated that the agreement would be subject to additional discussions on labor, and that the Administration would work with both sides of the aisle in Congress to ensure strong bipartisan support before submitting it to Congress.⁶⁰ On May 10, 2007, congressional leaders and the Bush Administration announced a bipartisan trade deal whereby pending free trade agreements would include enforceable key labor and environmental standards. This included an obligation to adopt and maintain in practice five basic internationally recognized labor principles: freedom of association; recognition of the right to collective bargaining; elimination of forced or compulsory labor; abolition of child labor; and elimination of discrimination in respect of employment and occupation.

The United States and Panama ultimately signed the proposed FTA on June 28, 2007, with the enforceable labor and environmental standards outlined in the bipartisan trade deal. Panama's National Assembly ratified the agreement on July 11, 2007, by a vote of 58 to 3, with one abstention.

The U.S. Congress had been likely to consider implementing legislation for the agreement in the fall of 2007, but the September 1, 2007, election of Pedro Miguel González of the ruling PRD to head Panama's legislature for one year delayed consideration of the FTA. González is wanted in the United States for his alleged role in the murder of U.S. Army Sergeant Zak Hernández and the attempted murder of U.S. Army Sergeant Ronald Marshall in June 1992. The State Department issued a statement expressing deep disappointment about the election of González because of his October 1992 indictment in the United States for the murder of Sergeant Hernández. Although González was acquitted in Panama in 1997 for the Hernández murder, observers maintain that the trial was marred by jury rigging and witness intimidation. González denies his involvement, and his lawyer asserts that ballistic tests in the murder were inconclusive. While polls in Panama in 2007 showed that Panamanians believed that González should have stepped down, the case also

⁵⁹ Office of the United States Trade Representative, "Free Trade with Panama, Brief Summary of the Agreement," December 19, 2006.

⁶⁰ Rosella Brevetti, "Panama, United States Conclude Negotiations on Free Trade Pact," but Labor Issues Remain," *International Trade Daily*, December 20, 2006.

energized the populist anti-American wing of the ruling PRD.⁶¹ González did not seek a second term as president of the National Assembly when his term expired on September 1, 2008, and another PRD official, Raúl Rodríguez, was elected Assembly president. This essentially removed the issue as an impediment to U.S. congressional consideration of the FTA.

Remaining FTA Issues

The Obama Administration focused on working out final issues with Panama related to labor rights and tax transparency, and on April 18, 2011, United States Trade Representative Ron Kirk maintained that that completion of action on these issues cleared the way for technical discussions with Members of Congress on the draft implementing bill for the Panama FTA.⁶²

The United States raised labor issues related to restrictions on collective bargaining rights in Panama's export processing zones (EPZs) and the right to strike in companies less than two years old. Legislation addressing both issues was approved by Panama's National Assembly in late March 2011 and signed into law by President Martinelli on April 5, 2011. The legislation eliminated restrictions on collective bargaining in EPZs and also eliminated the prohibition against the right to strike in companies less than two years old.⁶³

Another labor issue raised by the United States relates to labor rights in a special economic zone in Panama's Barú region in the western province of Chiriquí. The law that had established the special zone made collective bargaining discretionary for six years.⁶⁴ In late March 2011, Panama's National Assembly approved legislation that extended full collective bargaining rights to workers in the special economic zone in Barú, and President Martinelli signed the measure into law on April 5, 2011.⁶⁵

In addition, as noted above (see "Human Rights Issues"), certain provisions of Panama's labor laws that restrict unions have been criticized by the ILO. These include a requirement that a minimum of 40 people are needed to form a union. The Martinelli government has not agreed to make changes to Panama's labor code to reduce the number of members needed to start a union from 40 to 20, reportedly because there is no support for such a change, even from Panama's labor sector.⁶⁶ According to the State Department's 2010 human rights report on Panama, the Panamanian government, private sector, and unions support keeping the figure at 40 individuals.

With regard to tax transparency issues, some Members of Congress had wanted to delay consideration of the Panama FTA until the United States and Panama signed a Tax Information

⁶¹ Marc Lacey, "Fugitive from U.S. Justice Leads Panama's Assembly," *New York Times*, November 28, 2007.

⁶² Office of the United States Trade Representative, "Ambassador Ron Kirk Announces Next Step for U.S.-Panama Trade Promotion Agreement," April 18, 2011. Also see: White House, Office of the Press Secretary, "Fact Sheets: U.S.-Panama Trade Promotion Agreement," April 19, 2011, available at <http://www.whitehouse.gov/the-press-office/2011/04/19/fact-sheets-us-panama-trade-promotion-agreement>.

⁶³ Information provided to CRS by the Department of State, April 12, 2011.

⁶⁴ "U.S. Focused on Labor Laws for New Panama Economic Zone," *Inside U.S. Trade*, February 17, 2011. Also see: U.S. Department of State, "Country Reports on Human Rights Practices: Panama," April 8, 2011.

⁶⁵ Office of the United States Trade Representative, Statement by Ambassador Miriam Sapiro, Deputy United States Trade Representatives, Statement before the House Committee on Ways and Means, Subcommittee on Trade, March 30, 2011; and "Panama Moves Closer to Completing All Steps Necessary for FTA Vote," *Inside U.S. Trade*, April 1, 2011.

⁶⁶ Information provided to CRS by the Department of State, February 15, 2011.

Exchange Agreement (TIEA). This ultimately occurred on November 30, 2010, and led some Members of Congress to maintain that the TIEA could pave the way for action on the FTA. According to the Treasury Department, the agreement, which entered into force on April 18, 2011, provides the United States with access to information it needs to enforce U.S. tax laws, including information related to bank accounts in Panama. It permits both countries to seek information from each other on all types of national taxes in both civil and criminal matters for tax years beginning on or after November 30, 2007.⁶⁷

In a joint declaration at the signing of the TIEA, both countries agreed that the agreement would take effect as soon as practicable after Panama approves implementing legislation under its domestic laws, expected before the end of 2011, to comply fully with the terms of the agreement. As noted in the declaration, Panama maintained that it would enact legislation requiring the identification of the owners of bearer shares, an issue that U.S. officials have raised with Panama for a number of years.⁶⁸ Such legislation on bearer shares, also referred to as “know your client” legislation, was signed into law by President Martinelli on February 1, 2011. Panamanian Vice President and Foreign Minister Juan Carlos Varela maintained during a mid-February 2011 visit to Washington, DC, that he expected Panama’s National Assembly to approve the TIEA before the end of April 2011. Ultimately, the National Assembly approved the TIEA on April 13, 2011, and the measure was enacted into law on April 18, 2011.

In the 112th Congress, several measures have been introduced in support of the FTA with Panama. S.Res. 20 (Johanns), introduced January 25, 2011, would express the sense of the Senate that the United States should immediately approve FTAs with Panama, Colombia, and South Korea. S. 98 (Portman), introduced January 25, 2011, would, among other provisions, express the sense of Congress that the President should submit the Panama, South Korea, and Colombia FTAs to Congress and that Congress should approve those agreements. H.Res. 86 (Frelinghuysen), introduced February 11, 2011, would express the sense of the House that the Panama, Colombia, and South Korea FTAs should be implemented immediately.

Several hearings have been held in the 112th Congress touching on the proposed FTA with Panama. On January 25, 2011, the House Ways and Means Committee held a hearing on the pending FTAs with Colombia, Panama, and South Korea.⁶⁹ On February 8, 2011, a Senate Foreign Relations Committee minority staff report urged the Administration to invest the political capital needed to secure approval of the Panama and Colombia FTAs.⁷⁰ The House Committee on Ways and Means, Subcommittee on Trade, and the Senate Finance Committee held respective hearings on February 9 and March 9 on the President’s trade agenda featuring United States Trade Representative Ron Kirk. The House Committee on Foreign Affairs Subcommittee on the Western Hemisphere, held a hearing on the Colombia and Panama free trade agreements on March 17. Most recently, on March 30, 2011, the House Committee on Ways and Means,

⁶⁷ U.S. Department of the Treasury, Press Release, “U.S., Panama Sign New Tax Information Exchange Agreement,” December 1, 2010. See the full text of the TIEA, available at: <http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/PanamaTIEA10.pdf>

⁶⁸ U.S.-Panama Tax Information Exchange Agreement, Joint Declaration, November 30, 2010, available at: <http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/PanamaTIEAnote.pdf>

⁶⁹ See the witness testimony from the hearing, available at: <http://waysandmeans.house.gov/Calendar/EventSingle.aspx?EventID=220430>

⁷⁰ U.S. Congress, Senate Committee on Foreign Relations, *Losing Jobs and Alienating Friends: The Consequences of Falling Behind on Free Trade with Colombia and Panama*, committee print, 112th Cong., 1st sess., February 8, 2011, S. Prt. 112-?? (Washington: GPO, 2011), available at: <http://lugar.senate.gov/issues/foreign/lac/FTA.pdf>

Subcommittee on Trade, held a hearing on the Panama FTA featuring Deputy United States Trade Representative Miriam Sapiro and outside witnesses.

For details on the bilateral FTA, see CRS Report RL32540, *The Proposed U.S.-Panama Free Trade Agreement*, by J. F. Hornbeck.

Operation and Security of the Panama Canal

Historical Background and the Panama Canal Treaties

When Panama proclaimed its independence from Colombia in 1903, it concluded a treaty with the United States for U.S. rights to build, administer, and defend a canal cutting across the country and linking the Pacific and Atlantic oceans. (See **Figure 1, Map of Panama.**) The treaty gave the United States rights in the so-called Canal Zone (about 10 miles wide and 50 miles long) “as if it were sovereign” and “in perpetuity.” Construction of the Canal was completed in 1914. In the 1960s, growing resentment in Panama over the extent of U.S. rights in the country led to pressure to negotiate a new treaty arrangement for the operation of the Canal. Draft treaties were completed in 1967 but ultimately rejected by Panama in 1970.

New negotiations ultimately led to the September 1977 signing of the two Panama Canal Treaties by President Jimmy Carter and Panamanian head of government General Omar Torrijos. Under the Panama Canal Treaty, the United States was given primary responsibility for operating and defending the Canal until December 31, 1999. (Subsequent U.S. implementing legislation established the Panama Canal Commission to operate the Canal until the end of 1999.) Under the Treaty on the Permanent Neutrality and Operation of the Panama Canal, or simply the Neutrality Treaty, the two countries agreed to maintain a regime of neutrality, whereby the Canal would be open to ships of all nations. The U.S. Senate gave its advice and consent to the Neutrality Treaty on March 16, 1978, and to the Panama Canal Treaty on April 18, 1978, both by a vote of 68-32, with various amendments, conditions, understandings, and reservations. Panama and the United States exchanged instruments of ratification for the two treaties on June 16, 1978, and the two treaties entered into force on October 1, 1979.

Some treaty critics have argued that Panama did not accept the amendments, conditions, reservations, and understandings of the U.S. Senate, including the DeConcini condition to the Neutrality Treaty. That condition states: “if the Canal is closed, or its operations are interfered with, the United States of America and the Republic of Panama shall each independently have the right to take such steps as each deems necessary, in accordance with its constitutional processes, including the use of military force in the Republic of Panama, to reopen the Canal or restore the operations of the Canal, as the case may be.” However, others argued that Panama, in fact, had accepted all U.S. Senate amendments. The State Department asserted that Panama expressly accepted all amendments, conditions, and understandings to the two treaties, including the DeConcini condition. The United States and Panama signed the instruments of ratification for both treaties, which incorporated all the Senate provisions. The two countries cooperated throughout the years on matters related to the Canal and established five binational bodies to handle these issues. Two of the bodies were set up to address defense affairs and conducted at least 16 joint military exercises between 1979 and 1985 involving Panamanian and U.S. forces.

Canal Transition and Current Status

Over the years, U.S. officials consistently affirmed a commitment to follow through with the Panama Canal Treaty and turn the Canal over to Panama at the end of 1999. That transition occurred smoothly on December 31, 1999. The Panama Canal Treaty terminated on that date, and the Panama Canal Commission (PCC), the U.S. agency operating the Canal, was succeeded by the Panama Canal Authority (ACP), a Panamanian government agency established in 1997.

Under the terms of the Neutrality Treaty, which has no termination date, Panama has had responsibility for operating and defending the Canal since the end of 1999. As noted above, both Panama and the United States, however, in exercising their responsibilities to maintain the regime of neutrality (keeping the Canal secure and open to all nations on equal terms) independently have the right to use military force to reopen the Canal or restore its operations. This is delineated in the first condition of the Neutrality Treaty.

The secure operation of the Panama Canal remains a U.S. interest since the Canal is important for U.S. ocean-borne trade. The Canal's largest trade route in FY2010 for ocean-borne cargo was between the east coast of the United States and Asia, which comprised almost 41% of total Panama Canal long tons cargo traffic. The Canal's second-largest trade route in FY2010 was between the east coast of the United States and the west coast of South America, which comprised almost 12% of total Panama Canal long tons cargo traffic. The United States provides assistance to Panama to improve its ability to provide security for the Canal and to enhance port and maritime security. U.S. officials have consistently expressed satisfaction that Panama is running the Canal efficiently, and since 2003, the U.S. military has conducted exercises with Panama and other countries to protect the Canal in case of attack.

Headed by Alberto Alemán Zubieta, the Panama Canal Authority has run the Canal for more than 10 years and has been lauded for increasing Canal safety and efficiency. In January 2006, the Martín Torrijos government established a social investment fund backed by Panama Canal revenues that invests in schools, hospitals, bridges, roads, and other social projects. The initiative, according to the government, was designed to show Panamanians that the Canal is contributing to economic development and improving the quality of life for Panamanians.⁷¹

Canal Expansion Project

In April 2006, the Panama Canal Authority presented to President Torrijos its recommendation to build a third channel and new set of locks (one on the Atlantic and one on the Pacific) that would double the capacity of the Canal and allow it to accommodate giant container cargo ships known as post-Panamax ships. The project would also widen and deepen existing channels and elevate Gatun Lake's maximum operating level. The estimated cost of the seven-year project is \$5.25 billion, to be self-financed by the ACP through graduated toll increases and external bridge financing of about \$2.3 billion that would be paid off in about 10 years. According to the ACP, the overall objectives of the expansion project are to (1) achieve long-term sustainability and growth for the Canal's financial contributions to the Panamanian national treasury; (2) maintain

⁷¹ Rainbow Nelson, "Canal Cash to Pay for Social Development," *Lloyd's List*, January 18, 2006.

the Canal's competitiveness; (3) increase the Canal's capacity to capture the growing world tonnage demand; and (4) make the Canal more productive, safe, and efficient.⁷²

President Torrijos and his Cabinet approved the expansion project in June 2006, and the Legislative Assembly overwhelmingly approved it in July 2006, with 72 out of 78 deputies voting for the project. Pursuant to Panama's Constitution (Article 319), the project had to be submitted to a national referendum. The Torrijos government chose to hold the referendum on October 22, 2006, close to the anniversary of October 23, 1977, the date when Panamanians approved the two Panama Canal treaties in a national plebiscite by a two-to-one margin. The expansion project was approved by 78% of the vote.

There had been some vocal opposition to the Canal expansion project. The organization known as the Peasant Coordinator Against the Dams (CCCE, *Coordinadora Campesina Contra los Embalses*), consisting of agricultural, civil, and environmental organizations, asserted that the expansion project would lead to flooding and would drive people from their homes. An umbrella protest group known as the National Front for the Defense of Economic and Social Rights (*Frenadeso*), which was formed in 2005 during protests against social security reforms, called for a "no" vote.⁷³ Former Presidents Jorge Illueca and Guillermo Endara, as well as former Panama Canal administrator Fernando Manfredo, also opposed the expansion project, maintaining that the price was too high and too much of a gamble. Critics feared that the total price tag could rise considerably and expressed concern that toll increases could make alternative routes more economically attractive.⁷⁴

The ACP is moving ahead with the Canal expansion project. The Panamanian government officially launched the project on September 3, 2007, with a ceremony led by former President Jimmy Carter, whose Administration negotiated the Panama Canal Treaties. The project is expected to be completed by 2014. In March 2009, three multinational consortiums placed bids for the multi-billion dollar contract to build the new set of locks.⁷⁵ The ACP announced in July 2009 that the consortium *Grupo Unidos por el Canal* (United for the Canal) led by Spanish construction company Sacyr Vallehermoso was the winner of the contract after posting a bid of \$3.12 billion. The consortium also includes Italian, Belgian, and Panamanian companies, as well as two U.S. companies—Montgomery Watson Harza and Tetra Tech—involved as design subcontractors.⁷⁶ In January 2010, the ACP awarded the fourth and final dry excavation contract to a consortium made up of Spanish, Mexican, and Costa Rican companies. The excavation work will create an access channel linking the new Pacific locks with the Gaillard Cut, which is the narrowest stretch of the Canal.

⁷² Autoridad del Canal de Panama (ACP), "Proposal for the Expansion of the Panama Canal, Third Set of Locks Project," April 24, 2006.

⁷³ "Torrijos Appeals for Approval of Canal Expansion," *Latinnews Daily*, September 1, 2006.

⁷⁴ "Panama: Torrijos Reveals Plans to Expand Canal," *Latinnews Daily*, April 25, 2006; Chris Kraul and Ronald D. White, "Panama is Preparing to Beef up the Canal," *Los Angeles Times*, April 24, 2006; John Lyons, "Panama Takes Step Toward Expanding the Canal," *Wall Street Journal*, April 24, 2006.

⁷⁵ "Panama: Groups Bid on Canal Expansion," *Economist Intelligence Unit, Business Latin America*, March 9, 2009.

⁷⁶ "Unidos por El Canal Virtual winner of ACP contract," *Business News Americas*, July 8, 2009; and "Panama Canal Announces 'Best Value' Proposal for New Set of Locks Expansion Contract," *States News Service*, July 9, 2009.

Background on the 1989 U.S. Military Intervention

The December 20, 1989, U.S. military intervention in Panama, known as Operation Just Cause, was the culmination of almost two and a half years of strong U.S. pressure, including economic sanctions, against the de facto political rule of General Noriega, Panama's military commander. Political unrest had erupted in mid-1987 when a high-ranking Panamanian military official alleged that Noriega was involved in murder, electoral fraud, and corruption, which prompted the formation of an opposition coalition that challenged his rule. The regime nullified the results of May 1989 national elections, which international observers maintain were won by the opposition by a 3-1 margin. It also harassed U.S. citizens in Panama, including the killing of a U.S. Marine lieutenant. President George H. W. Bush ultimately ordered U.S. forces into combat to safeguard the lives of Americans in Panama, to defend democracy, to combat drug trafficking, and to protect the operation of the Panama Canal.

In early January 1990, with the restoration of democracy and Noriega's arrest to face trial in the United States on drug charges, President Bush announced that the objectives of the U.S. intervention had been achieved. In terms of casualties, 23 U.S. soldiers and three U.S. civilians were killed, while on the Panamanian side, some 200 civilians and 300 Panamanian military were killed. While Congress was not in session during the intervention, in general, Members were strongly supportive of the action. In February 1990, the House overwhelmingly approved a resolution, H.Con.Res. 262, stating the President acted appropriately to intervene in Panama after substantial efforts to resolve the crisis by political, economic, and diplomatic means.

Status of Manuel Noriega

In the aftermath of the 1989 U.S. military intervention, General Manuel Noriega was arrested in January 1990 and brought to the United States to stand trial on drug charges. After a seven-month trial, Noriega was convicted on 8 out of 10 drug trafficking charges in U.S. federal court in Miami in 1992, and sentenced to 40 years in prison. That sentence was subsequently reduced to 30 years, and then to 20 years. With time off for "good behavior," Noriega was scheduled to be released from jail on September 9, 2007, but remained in U.S. custody pending appeals of his extradition to France. Noriega's defense filed a final appeal with the Supreme Court in July 2009 on the grounds that Noriega was granted "prisoner of war" status under the Geneva Convention in a 1992 U.S. court ruling and therefore was entitled to return to Panama. Noriega lost that appeal, and was extradited to France on April 26, 2010. In France, Noriega faced a 10-year prison sentence for his conviction in absentia in 1999 on money laundering charges. He was eligible for a new trial upon his extradition to France and in July 2010 was again convicted of drug money laundering and sentenced to seven years in prison.

When he was released from the United States, Noriega wanted to return to Panama in order to appeal his convictions in absentia, including for two murders: the brutal killing of vocal critic Hugo Spadafora in 1985; and the killing of Major Moisés Giroldi, the leader of a failed 1989 coup attempt. Panamanian courts sentenced Noriega to at least 60 years in prison, but the law only allows him to serve a maximum sentence of 20 years, and according to some reports, 18 years of Noriega's imprisonment in the United States could be subtracted from his sentence in Panama.⁷⁷ Nevertheless, there are additional outstanding cases against Noriega, including alleged

⁷⁷ Kathia Martinez, "A Homecoming for Noriega after Miami Release? Many Hope Not," *Associated Press Newswires*, August 12, 2007.

responsibility for the deaths of several members of the Panamanian Defense Forces involved in the failed 1989 coup.⁷⁸

Noriega's attorneys argued that since Noriega had been recognized as a prisoner of war in the U.S. courts, the United States should have repatriated him to his native Panama, insisting that this complies with the Geneva Conventions. U.S. officials argued that France's extradition should be honored because Panama by law does not extradite its nationals.⁷⁹ Panama had filed an extradition request for Noriega in 1991.

While Panamanian officials called for Noriega's extradition to Panama, they did not oppose the possibility of Noriega being extradited to France and stated that the government would respect the decision of the U.S. courts on this matter. Some observers maintained that Panamanian officials were reluctant to have Noriega return because of changes to Panama's penal code that could allow Noriega to serve little, if any, of his sentence.⁸⁰ In response to Noriega's extradition to France, Panama's Foreign Minister Juan Carlos Varela maintained that the Panamanian government respected the United States' sovereign decision, but that it would pursue legal and diplomatic means to return Noriega to Panama to serve sentences handed down by Panamanian courts.⁸¹

On January 12, 2011, Panama requested Noriega's extradition from France for the 1989 killing of Major Moisés Giroldi, the leader of a failed coup. According to Panama's Ministry of Foreign Affairs, Panama previously had requested Noriega's extradition from France for the 1985 killing of vocal critic Hugo Spadafora and is awaiting a response.⁸²

⁷⁸ "Torrijos on Edge over Noriega Release," *Latin American Regional Report, Caribbean and Central America*, August 2007.

⁷⁹ Carmen Gentile, "Noriega Court Bid Called a Charade; Aims to Avoid Extradition," *Washington Times*, August 14, 2007.

⁸⁰ Marc Lacey, "An Ambivalent Panama Weighs Noriega's Debt and Threat," *New York Times*, July 29, 2007.

⁸¹ "Panama's Noriega Extradited to France," *LatinNews Daily*, April 27, 2010.

⁸² República de Panamá, Ministerio de Relaciones Exteriores, Comunicado de Prensa, "Extradición de Manuel Antonio Noriega por el caso Giroldi," January 12, 2011.

Appendix A. Links to U.S. Government Reports

Background Note, Panama

Date: September 16, 2010

Full Text: <http://www.state.gov/r/pa/ei/bgn/2030.htm>

Congressional Budget Justification for Foreign Operations FY2012, Annex: Regional Perspectives (p. 813-815 of pdf)

Date: March 2011

Full Text: <http://www.state.gov/documents/organization/158268.pdf>

Country Reports on Human Rights Practices 2010, Panama

Date: April 8, 2011

Full Text: <http://www.state.gov/g/drl/rls/hrrpt/2010/wha/154514.htm>

Country Reports on Terrorism 2009 (Western Hemisphere Overview)

Date: August 5, 2010

Full Text: <http://www.state.gov/s/ct/rls/crt/2009/140888.htm>

International Religious Freedom Report 2010, Panama

Date: November 17, 2010

Full Text: <http://www.state.gov/g/drl/rls/irf/2010/148770.htm>

International Narcotics Control Strategy Report 2011, Vol. I (Panama, pp. 445-448 of pdf)

Date: March 2011

Full Text: <http://www.state.gov/documents/organization/156575.pdf>

International Narcotics Control Strategy Report 2011, Vol. II (Panama, pp. 155-158 of pdf)

Date: March 2011

Full Text: <http://www.state.gov/documents/organization/156589.pdf>

National Trade Estimate Report on Foreign Trade Barriers 2011 (Panama, pp. 290-294 of pdf)

Date: March 2011

Full Text: http://www.ustr.gov/webfm_send/2751

Trafficking in Persons Report 2010 (Panama, pp. 265-266 of pdf)

Date: June 14, 2010

Full Text: <http://www.state.gov/documents/organization/142979.pdf>

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