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## What is Economic Substance?

**Economic substance describes the economic (operational) reality of a corporate structure which has been put in place because of international tax optimisation reasons.**

A considerable number of international tax planning structures (finance companies, holding and sub-holding companies, intellectual property (IP) structures and trading companies) have been/are being established to benefit from tax laws of other foreign jurisdictions or in order to benefit from the favourable conditions of double taxation treaties signed between two countries.

This can, for example, be the case when country A has not signed a double taxation treaty with country B and therefore an additional company is interposed in country C with which both country A and country B have signed a beneficial double taxation treaty. The only goal of the interposed corporate entity in country C is to benefit from the favourable conditions of the applicable double taxation treaties. But due to the lack of economic necessity these kinds of interposed structures are often lacking genuine economic activity.

Foreign entities are thus often put in place for financial and/or fiscal reasons, but not so much because they are really 'economically' necessary in the worldwide operational activities of the company. The term economic substance (or tax substance) stands for the actual activity of and the effective role a company plays in the broader context of an internationally operating company. Is the company in Switzerland (or elsewhere) (really) necessary from an economic perspective in the overall corporate structure of an enterprise?