



ATOZ ALERT

Luxembourg enacts its new carried interest tax framework: Key highlights

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Today, Luxembourg enacted a significant reform modernising and clarifying the tax regime applicable to carried interest received by individuals managing alternative investment funds (“AIF”). First introduced in 2013, the framework has now been reshaped to provide greater legal certainty and better reflect today’s market realities.

Driven by the ambitions set out in the 2023 – 2028 coalition agreement which expressly prioritises strengthening Luxembourg’s competitiveness as a fund domicile, this reform goes beyond mere technical adjustments.

By refining the applicable tax rules and clarifying their scope, the reform seeks to enhance the country’s ability to attract and retain qualified front-office professionals active in AIFs and digital assets – reinforcing Luxembourg’s strategic positioning in an increasingly competitive European asset-management landscape.

In this alert, we highlight the key takeaways of the reform.

Key Takeaways

CONFIRMATION OF TAX CLASSIFICATION

- Carried interest is confirmed as **miscellaneous income** (speculative gains), not employment or professional income.

EXPANDED SCOPE OF BENEFICIARIES

- The regime now includes **also non-employees** entitled to carried interest such as:
 - Independent board members
 - Partners in management companies
 - Employees of affiliated advisory firms
- The regime excludes purely administrative roles.
- The goal is to remain **flexible while preventing abuse**, such as disguising fixed compensation/bonus as carried interest.

CLARIFICATION OF CARRIED INTEREST TYPES AND TAX TREATMENT

- **Contractual Carried Interest:** Not linked to fund participation - granted without investment.
 - The quarter-rate tax (1/4 of the progressive income tax rate) becomes permanent and available to all beneficiaries of the regime, not just impatriates.
- **“Invested” Carried Interest:** Linked to actual fund “ordinary” investment or carry shares.
 - Taxable if the investment is realised within a 6-month deadline.
 - Exempt if investment is held more than 6 months, unless the provisions of Article 100 come into effect
 - Without the need of realisation of the participation held in the AIF.
 - Only genuine carried interest qualifies for favourable tax treatment; other income follows the common regime.

TAX TRANSPARENCY EXCEPTION

- Solely for the purpose of applying the carried interest regime, the tax transparency of AIFs will be disregarded.
- This ensures consistent treatment regardless of the fund’s legal structure.

REMOVAL OF CAPITAL RETURN CONDITION

- The requirement that investors must first recover their full investment before carried interest is paid is removed.
- This change accommodates deal-by-deal carry structures, not just whole-of-fund models.

ENTRY INTO FORCE

- The new carried interest regime applies from tax year 2026.

FORMALITIES

- The availability of the carried interest regime is not subject to any administrative formalities or specific formal applications.

Insights

The clarifications introduced by the new law align with the widely held interpretation and application of the previous Luxembourg carried interest tax regime. Thus, it should not call the validity of past implementations into question, and it provides clear and positive guidance on how the highly favourable tax regime will be applied going forward.

In addition, the new law extends the scope of application of the regime, innovates with the tax transparency exception and provides for a more favourable tax treatment of contractual (non-invested) carried interest.

This reform aligns with Luxembourg’s ambition to attract front-office fund management and support the growth of alternative and digital asset funds. It reflects a shift toward a more inclusive and competitive tax framework, while maintaining safeguards against abuses.

Do you have any questions?



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