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Client Alert

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International: Carried interest tax reforms: overview for fund managers — update Q3 2025

In brief

Carried interest, i.e., the share of profits from a private investment fund (like private equity or venture capital) that is paid to the fund manager as an incentive linked to the performance of the fund, has been and continues to be a contentious point of discussion in tax policy across various jurisdictions. Changing political landscapes and worsening economic climates have put carried interest regimes and private capital under significant pressure. Some governments are seeking to cut back on favorable regimes for carried interest and private funds. Thus, governments are increasingly scrutinizing these types of regimes, viewing them as overly favorable compared to regular taxation regimes, such as the taxation of employment income. In response to these pressures, several countries are considering measures to reduce the preferential tax treatment of carried interest. Other countries, such as Luxembourg, are currently reviewing the taxation of carried interest in view of an attractive framework. These changes could significantly impact fund managers, potentially reducing the net income related to carried interest and altering the attractiveness of private capital as a career.

Contents

This updated article delves into specific developments in the US, the UK, the Netherlands, Spain, Belgium, France, Switzerland and Luxembourg, providing a comparative analysis of how each jurisdiction is addressing the matter. By examining these aspects, the article aims to provide a comprehensive overview of the current state and future direction of carried interest taxation in these key regions.

Key takeaways

With the changing geopolitical and economic climate, some (but not all) governments are looking to scale back on favorable regimes designed to attract talent and investors, aiming to balance fairness through taxation. Private capital as an industry is seen as a source of significant income and is, therefore, often scrutinized in this respect as well.

An emerging trend in various countries shows governments seeking to increase taxation on high income earning individuals. This is done by implementing laws that generally target high income earning or high net-worth individuals. France, for example, implemented this via its Finance Bill for 2025. Additionally, certain countries are enacting legislation specifically targeting common forms of remuneration in the private capital sector, such as carried interest, by increasing the tax burden for carried interest recipients. Among other things, this can be done by taxing carried interest at the same rates as employment income or trading income, instead of as capital gains or dividend income. The US government is currently researching the feasibility of such initiatives, the Netherlands and the UK are consulting and have consulted (respectively) on legislation intended to take effect from 1 January 2026 in the Netherlands and 6 April 2026 in the UK, whereas Spain and Belgium have recently undergone such a process already (although a preferential tax treatment may still apply in specific cases). Luxembourg, for its part, has tabled a draft bill that aims to enhance its competitiveness by attracting front-office fund activities and talent.

We note that the actual implementation of these initiatives may be quite uncertain, as they are often subject to heavy criticism. Among others, this can be due to the effects that any amendments may have on the economic attractiveness of a country, the current political uncertainty in certain jurisdictions, etc. However, despite this uncertainty of implementation, it still pays to be mindful of the current geopolitical and economic climate when planning private funds. After all, future changes to current legal frameworks may have a significant (fiscal and financial) impact on the models commonly being used.

These developments highlight the need for coordinated advice to ensure tax-efficient and legally compliant solutions for the US and European private capital markets alike. If there are any substantial legislative changes affecting the tax treatment, we advise contacting your regular Baker McKenzie adviser to address potential consequences. Fund managers and executives who are internationally mobile may consider relocating to regions with more favorable tax regimes, for example. Furthermore, restructuring carried interest payouts may be considered, to "lock in" the current tax treatment before any new legislation takes effect. Additionally, it may be prudent to reconsider future strategies if these legislative changes are adopted, if this is feasible under the applicable laws.

If you have any questions about how these developments may affect your organization, please feel free to reach out to the Baker McKenzie expert for your country.

Tax treatment and developments by country

1. US

Current tax treatment

In the US, "carried interest" refers to a profits interest in a partnership granted to the manager of an investment fund in exchange for services. The manager generally receives a separate management fee as compensation (i.e., ordinary income), but the carried interest is generally taxed as capital gain at a 20% rate, the top rate applicable to long-term capital gains. Long-term capital gains treatment applies only to carried interest held for more than three years. With the Tax Cuts & Jobs Act (TCJA) coming into effect in 2018, sales of this carried interest (or the fund's underlying property) before the end of the three years result in tax at ordinary income rates. The top federal tax rate on ordinary income (e.g., earned income) for individuals is 37%, which was made permanent with the enactment of the The One Big Beautiful Bill Act (OBBBA) (Pub. L. No. 119-21) on 4 July 2025. Both short- and long-term capital gains are subject to the net investment income tax at a rate of 3.8% as well.

Recent developments

Over the years, members of Congress have drafted numerous bills attempting to ignore the form of the profits interest in order to treat income with respect to carried interest as compensation taxed as ordinary income. As mentioned above, the TCJA extended the minimum holding period for "applicable partnership interests" to receive long-term capital gain treatment to three years by adding a provision to the Internal Revenue Code (Section 1061) that recharacterizes gain from sales with shorter holding periods as short-term capital gain (which is taxed at ordinary income rates). The three-year holding period applies to both a sale of the applicable partnership interest and a sale of the underlying partnership assets. The effects of this change are generally limited to carried interest of hedge funds and private equity funds that hold assets for a short period, and it allows for the more favorable capital gains tax treatment for carried interest held by managers of funds holding real estate, more traditional private equity and other longer-term investments. Legislative attempts to extend the holding period to five years have historically failed.

Unsatisfied with the tax-rate disparity that remains between many carried interest holders and employees, members of Congress continue to introduce versions of familiar bills that, if enacted, would tax some or all carried interest as ordinary income or treat the granting of a carried interest as a subsidized loan. For example, Congressional Democrats reintroduced the Carried Interest Fairness Act of 2025 (S. 445, H.R. 1091), which proposed to add a new section to the Internal Revenue Code that recharacterizes as ordinary income any net long-term capital gain allocated with respect to an "investment services partnership interest". Related capital losses would be recharacterized as ordinary losses to offset this ordinary income (but the amount treated as ordinary loss would be limited to the amount of recharacterized gain).

President Trump has expressed support for ending the preferential treatment of carried interest. However, while Congress considered further proposals to further limit the applicability of long-term capital gains rates to carried interest in connection with the OBBBA legislative process, the OBBBA notably did not alter the status quo as far as carried interest taxation. This conceivably could be, at least in part, due to the current liquidity drought in the private equity space – with lesser exits, IPOs and liquidity events due to the climate of geopolitical uncertainty, carry realization events are more scarce and increasing the tax burden thereon would only put more stress on liquidity pressures.

2. UK

Current tax treatment

In the UK, carried interest that arises from a long-term investment activity is typically subject to capital gains tax where certain conditions are met, currently at a rate of 32% since 6 April 2025 (although if the nature of the underlying return that gives rise to carried interest is income, the effective rate of tax could be as high as 45%). There are separate rules for "income-based carried interest" (IBCI), which can attract tax rates of up to 47% (including Class 4 National Insurance contributions). Broadly, carried interest is IBCI if the average holding period for the investment is less than 36 months (and for carried interest with average investment-holding periods between 36 and 40 months, a proportion of the carried interest will be subject to income tax and Class 4 National Insurance contributions). To the extent that carried interest arises in respect of employment-related securities, it is outside the scope of the IBCI rules, and this has been a particularly important exclusion for many private credit funds.

In the UK, the capital gains tax treatment of carried interest for fund managers has sparked considerable debate in recent years. Before the general election on 4 July 2024, the Labour Party was clear that it was committed to reforming the rules with promises to "close the loophole".

Recent developments

Following the general election, the new Labour government was quick to act on its manifesto promise and published a call for evidence on 29 July 2024. The call for evidence confirmed the government's intention to reform the tax treatment of carried interest and sought input from stakeholders on a number of areas. In response to concern raised in the industry, the government emphasized that it would:

> "… seek to protect the United Kingdom's position as a world-leading asset management hub, recognizing that the sector channels vital investment across the UK and will play an important role in this government's mission to boost economic growth."

Following this engagement with stakeholders over the summer of 2024, the Chancellor announced a package of reforms to the taxation of carried interest in the Autumn Budget 2024. As an interim measure, the capital gains tax rates of 18% and 28% that applied to carried interest were consolidated into a single rate of 32%, with effect from 6 April 2025. IBCI continues to be taxed at the current income tax rates.

More substantial proposed reform has followed. Draft legislation for the new carried interest regime was published for Finance Bill 2025-26 on 26 July 2025 and was subject to a technical consultation that closed on 15 September 2025. Under the draft legislation, from 6 April 2026 all carried interest proceeds will be treated as receipts of a deemed trade carried on by the recipient and subject to income tax at 45% for additional rate taxpayers and Class 4 National Insurance contributions. Crucially, however, a 72.5% multiplier will be applied to "qualifying carried interest" to reduce the amount subject to the marginal income tax rate. Assuming that the individual is an additional rate taxpayer, this means that the effective tax rate (including Class 4 National Insurance contributions) will be 34.1%. The new rules will apply to employees and non-employees (e.g., partners) and with effect from 6 April 2026 the existing exemption from the IBCI rules for carried interest that is an employment related security will be removed.

It was recognized that the removal of the existing employment related securities exemption under the IBCI rules would disproportionately affect credit funds due to the way in which the average holding period is calculated with respect to the relevant investments of a fund. It is currently difficult in practice for credit funds to have an average holding period of at least 40 months in part because the current legislation is formulaic and does not cater well for scenarios where a credit fund may have its economic exposure to an investment split across multiple debt instruments and legal entities or where a credit fund syndicates debt. Even the narrowly drafted relaxation of the current legislation in relation to calculation of the average holding period for prepayment of primary loans has proved hard to apply in practice with a significant diligence burden. The proposed rules simplify matters significantly by including a specific regime for calculating the average holding period of a credit fund that covers multiple acquisitions of debt in the same borrower group and enhances the existing prepayment rules.

There will be scope for qualifying carried interest receipts for employees to also be within the scope of other taxing provisions, including the employment-related securities rules. However, there will be mechanisms introduced to the new legislation to prevent double taxation.

Following consultation, the government decided against implementing additional requirements for carried interest to be 'qualifying' that are seen in certain other European jurisdictions, such as a minimum co-investment requirement and an additional minimum holding period that would have applied to the carried interest itself (which would have been in addition to the average holding period that already exists for underlying fund investments). The existing average holding period requirement for fund assets of at least 40 months under the IBCI rules will remain.

One of the material implications of carried interest being brought within the income tax framework (and outside of the capital gains tax framework) is that, alongside UK tax residents, non-UK residents will be charged to UK income tax (subject to terms of any relevant double tax treaty) to the extent relating to investment management services performed in the UK. The amount of tax arising under the proposed legislation will depend on the number of "UK workdays" and the government has narrowed the scope of these rules as they relate to non-residents by setting out 3 categories of workday that are not UK workdays:

- any UK workday prior to 30 October 2024;

- any UK workday in a tax year where the individual is non-UK tax resident and spends less than 60 workdays in the UK in the relevant tax year; and
- any UK workday prior to a period of 3 or more years in which the individual has been non-UK tax resident and spends less than 60 workdays in the UK in the relevant tax year.

The above exclusions for non-UK tax residents may enable fund managers, including those that may have ceased UK tax residence ahead of or following the recent abolition of the "res non-dom" regime, to work in the UK for short periods without jeopardizing their UK tax position with respect to such receipts, which may help with continuity of business if the private equity manager is required in the UK from time to time.

Another material implication of carried interest being brought into the income tax framework is that carried interest payments will fall under the scope of the "payments on account" rules that require individuals to make advance payments of estimated tax before the final due date. As payments on account are generally based on the previous year's profits, there is some scope for unpredictable and uneven payments of carried interest to cause problems under these rules.

The next step will be for the proposed legislation to be finalized and enter into force. Following the closing of the consultation on 15 September 2025, it is intended that legislation will be included in the Finance Bill 2025-26 in the autumn, to take effect from 6 April 2026. You can find further details on the draft legislation in our client alert here.

3. The Netherlands

Current tax treatment

The Dutch lucrative interest scheme aims to tax the income from carried interest structures, which are commonly used for investment managers. A lucrative interest is defined as shares, receivables or similar entitlements, including debts for which a future waiver can be expected (under certain conditions), if it can reasonably be assumed that one of the purposes of these items is to remunerate the taxpayers' (employment) activities. Indications for this purpose may be the existence of special conditions or (leaver) provisions, or the fact that the return on the interest depends on certain management or shareholder objectives, e.g., IRR, profit or turnover. The legal text of the lucrative interest scheme only focuses on the following:

1. Those classes of shares that are subordinated to other classes of shares, and constitute less than 10% of the total share capital;
2. Those classes of shares with a preference percentage of at least 15%;
3. Certain loans/receivables and rights similar to the aforementioned shares and loans/receivables.

However, the explanatory notes to the lucrative interest scheme are much more elaborate. They clarify that the lucrative interest scheme aims to tax any and all income or gains arising from lucrative interests, which, according to the notes, may cover common management participation plan instruments, including leveraged structures, (cumulative) preference shares and ratchet shares (both ordinary and reverse ratchets).

Based on the lucrative interest scheme, all income and gains derived from lucrative interests (i.e., typically dividends and alienation proceeds) are taxed at the progressive tax rates of "Box 1" (on income from work and the private abode), with a maximum of 49.5% (for 2025). However, if the interests are held through a holding company of which the beneficiary is a substantial interest holder, the Dutch personal income tax may (under conditions) be levied at the lower progressive rates that apply to "Box 2" (on income from substantial shareholdings), i.e., up to 31% (for 2025). To qualify as a substantial interest holder of the holding company, the beneficiary should own, or be entitled to purchase, 5% or more of the capital issued on a class of shares of the holding company.

If a holding company is used, careful structuring may be required to ensure application of the Dutch participation exemption for corporate tax purposes. Without the participation exemption, the combined corporate tax and income tax rate may be less favorable. The personal holding company will have to make a (taxable) distribution of at least 95% of the benefits under the lucrative interest plan to the participants. Please note that any benefit that occurs when entering into the lucrative interest structure (e.g., shares acquired for less than the fair market value) may still be taxed at the progressive "Box 1" rates with a maximum of 49.5% (for 2025).

Recent developments

The Dutch lucrative interest regime had remained relatively stable since its introduction in 2009. However, the past few years have seen some movement in this area. In April 2024, for example, the Dutch House of Representatives adopted a motion to adjust the regime so that managers in the private equity sector would always be taxed at the progressive "Box 1" rates with a maximum of 49.5% (2025), while repealing the tax-mitigating measure via a holding company as explained above. This would significantly increase the tax burden for certain private equity executives making use of this structure. The motion explicitly mentioned "carried interest", but seems designed to bring about a broader adjustment of the lucrative interest regime.

In February 2025, a further investigation of the lucrative interest regime indicated that the current rules and regulations were comparable to those of other countries from a tax-burden perspective. Additionally, the investigation noted that other alternatives were not necessarily easier to implement and to execute administratively. The investigation therefore advised against making significant changes to the lucrative interest regime until the current uncertainty regarding the Dutch "Box 3" tax (on income from savings and investments) has been resolved.

Meanwhile, the Dutch government opened an online consultation to gather public opinion on two alternatives that had been proposed to the current lucrative interest rules. The first alternative was to classify lucrative interests as either "taxable wages" or "taxable result from other activities" under "Box 1". The second alternative was to classify lucrative interests under "Box 2", under application of a multiplier, leading to a higher specific tax rate in "Box 2" for income from lucrative interests.

New legislative proposal: Box 2 multiplier

On 3 July 2025, the Dutch House of Representatives adopted a motion to revise the taxation of income generated through investment structures commonly used by private equity professionals. The focus lies on profits derived from "lucrative interests" that are indirectly held via personal holding companies, where individuals typically maintain a substantial ownership stake and may benefit from favorable tax treatment if the ownership is structured appropriately, as described above. The resulting proposal seeks to raise the effective tax rate on such income to 36%, starting 1 January 2026. Importantly, the scope of this measure extends beyond private equity managers, targeting a broader group of taxpayers who fall within the definition of carried interest arrangements under Dutch tax law.

To implement the proposed tax increase, the Dutch 2026 Tax Plan introduces a method that recalculates the taxable base for indirectly held lucrative interests. This is done by applying a factor derived from the ratio between the Box 3 tax rate (set at 36%) and the highest applicable Box 2 rate (31%). For instance, if an individual earns € 300,000 in profit, the adjusted taxable amount would be approximately (36%/31%) * € 300,000 =) € 348,387. When the 31% Box 2 rate is applied to this recalculated figure, the resulting gross tax liability is € 108,000, effectively mirroring a 36% tax on the original earnings.

No transitional rules are expected to accompany the proposed changes, which mean that existing arrangements will likely be impacted immediately. In light of this, we would advise reviewing all current structures, as highlighted in the key takeaways section of this alert. Taxpayers may wish to explore options such as restructuring ownership (where feasible and possible) or accelerating vesting, to be able to apply the current tax treatment before the new rules come into effect.

Lastly, please note that it remains uncertain whether this measure will be implemented, given the current uncertain political landscape in The Netherlands and the upcoming elections for the Dutch House of Representatives. However, if the proposal is in fact adopted, it is expected to take effect on 1 January 2026.

4. Spain

Current tax treatment

The tax treatment of carried interest in Spain falls under the category of employment income within the scope of the personal income tax (PIT), which is taxed at a progressive tax rate of up to 50%. This rate is higher than the one applicable to other income, such as dividends or capital gains, which is taxed at a progressive rate up to 30% from FY 2025 onwards. This treatment comes from the "start-up" law in force since January 2023. In practice, before January 2023, this characterization was established in certain tax rulings, depending on the relationship between the recipient of the carry and the payor. Specifically, the PIT does not refer to carried interest but to income ("economic rights") directly or indirectly resulting from the investment in certain entities. The current regime foresees that only 50% of the carried interest should be integrated into the taxable base of the taxpayer, if certain requirements are met, as follows:

1. These economic rights must be obtained from closed-end alternative investment funds (AIF Directive 2011/61/EU) and derived from activities as managers or employees of the managing entity or another entity within the same group.
2. Other investors must obtain a minimum return defined in the entity's bylaws (i.e., a waterfall of returns to the investors is required).
3. Such economic rights should be maintained for a minimum period of five years, unless they are transferred upon death, liquidated early or rendered ineffective due to a change in the management entity.
4. These economic rights cannot originate from an entity resident in a tax haven.

Failure to meet any of the above requirements implies that the entire income (100%) should be integrated into the taxable base of the taxpayer.

Recent developments

Two rulings from the Spanish General Directorate of Taxes (DGT), published on 31 July 2023 and 7 November 2024, and a recent tax ruling published on 26 August 2025, included a review of the requirements in certain scenarios.

On the one hand, they confirmed that the regime is also applicable to foreign venture capital entities, if they meet the characteristics set out in the Spanish Venture Capital Entities Act. This inclusion is significant as it broadens the scope of the carried interest special regime, although it is highly recommended to review each case individually as it might not fit within the scope.

On the other hand, the DGT confirmed that the carried interest regime can also apply to bonuses or incentives received by employees and managers of the managing entity. This income is considered part of the carried interest, if all other requirements for its application are met.

These rulings also determined that administrators, managers or employees of the entities covered by the regime who receive bonuses or incentives linked to carried interest, can also apply the new regime, even if the income is received after they have ceased their activities.

In addition, the DGT clarified that the early collection of the carried interest prior to the completion of the five-year holding period does not preclude the application of the current carried interest regime. Specifically the DGT clarified that early collections (before the five-year period) are allowed provided that the underlying economic rights continue to be held by the taxpayer until the end of the five-year period.

Finally, the last ruling rejects the application of the regime in case the carried interest is not reflected in the entity's bylaws but in a private agreement.

5. Belgium

The Belgian Law of 18 July 2025 introduced a specific carried interest income tax regime. Under such new regime, carried interest income received by a carried interest beneficiary is as a rule classified as “investment income” and is subject to a flat tax rate of 25%.

According to the new law:

- Carried interest is:
    - The part of the profit of a carried interest-vehicle, paid by or through the carried interest vehicle to a carried interest beneficiary in whatever form, minus the acquisition price paid for the underlying rights by said beneficiary and with the exception of the part of the profit that is proportional in comparison to the part acquired by an investor who is not a carried interest beneficiary (i.e., the catch-up);
    - The capital gain realized by a carried interest beneficiary when transferring their rights in the carried interest vehicle minus the acquisition price paid for said rights by said beneficiary and with the exception of the part of the capital gain that is proportional in comparison to the capital gain acquired by an investor who is not a carried interest beneficiary (i.e., the catch-up);
    - The purchase bonus and/or liquidation surplus received by the carried interest beneficiary, minus the acquisition price paid for the underlying rights by said beneficiary and with the exception of the part of these proceeds that is proportional in comparison to the proceeds acquired by an investor who is not a carried interest beneficiary (i.e., the catch-up);
- A carried interest beneficiary is a natural person or party related thereto, who directly or indirectly performs activities for a carried interest vehicle or its manager;
- A carried interest vehicle is – in essence - a Belgian or foreign institution for collective investment qualifying as a Collective Alternative Investment Fund as per the law of 19 April 2014 (“AICB” / “OPCA”).

In addition, the following should be noted:

- The new law explicitly determines that carried interest does not include the income (of whatever nature) received in respect of shares acquired by the carried interest beneficiary through the exercise of stock options as per the Belgian Stock Option Law of 26 March 1999 (i.e., stock options taxed at grant).
- Even though the new income tax regime applies on all carried interest paid or granted as of its entry into force on 29 July 2025, it will not apply on carried interest paid or granted by carried interest vehicles that are put into liquidation on said date.
- When determining proportional part of the profit/capital gain/proceeds granted by the carried interest vehicle, the agreements concluded between the different investors at the date of incorporation as well as any other agreements concluded between the parties involved are to be considered.

- A withholding tax (at 25%) must as a rule be levied on the carried interest paid by the debtor of same. In principle, this would be the carried interest vehicle if the carried interest consists out of the distribution of profits, purchase bonus or liquidation surplus, and the purchaser of the shares when capital gains are involved. Absent treaty protection, such movable withholding tax obligation would also apply if the carried interest beneficiary is a tax non-resident of Belgium.
- Carried interest received by a company is out of scope of the new income tax regime (as a consequence of which the new law is not affecting certain current structure being relied upon in the market). It must however be noted that, as of assessment year 2026, the new legislation no longer allows company-shareholders of carried interest vehicles to book a so-called liquidation reserve.

6. France

The carried interest regime, subject to the fulfilment of specific conditions, allows directors and fund managers investing in these funds to benefit from a flat rate withholding tax of 30%, including income tax at the rate of 12.8% and social security contributions at the rate of 17.2%.

To qualify for capital gains tax treatment, the following criteria must notably be met:

- The directors or managers working in these companies or funds must receive fair remuneration for their employment contract or corporate mandate;
- The carried interest must be subscribed to, or acquired, at fair market value; and
- Carried interest units or shares must be identified as such, represent a long-term investment (no payment before the fifth anniversary of the setup of the fund or the subscription) and relate to a fund established in France, UE or EEE funds.

Minimum investment thresholds apply:

- 1% of total subscriptions for structures with assets ≤ EUR 1 billion;
- 0.5% for structures with assets > EUR 1 billion; and
- 0.25% for structures investing in innovative companies or SMEs.

Failure to meet these requirements results in reclassifying income or gains from the carried interest shares as employment income. This income is then subject to a progressive tax rate of up to 45% and a specific employee social security contribution of 30% for the carry holder.

Additionally, carried interest is subject to exceptional contribution on high income at a rate of 3% to 4% depending on the amount of the taxable income.

Recent developments

The French Finance Act for 2025 (Law No. 2025-127 of 14 February 2025) introduced a new differential surtax aimed at ensuring a minimum taxation rate of 20% on the high income received by taxpayers. If the combined tax burden (12.8% income tax and up to 4% exceptional contribution on high income) results in an effective taxation rate below 20% (based on the taxable reference income that is adjusted), the differential surtax will apply to reach this 20% tax threshold.

Key compliance requirements for 2025:

- Taxpayers must report income online between 1 December 2025 and 15 December 2025 if subject to this new surtax;
- An advance payment of the 95% of the estimated surtax is required and due within same timeframe; and
- Failure to comply will result in a 20% penalty.

Carried interest is likely to fall within the scope of this new surtax. Taxpayers are strongly advised to consult their tax advisors.

There remains uncertainty regarding whether this new differential surtax will be extended to 2026 and beyond and whether a new type of wealth tax may be introduced in 2026.

7. Switzerland

Current tax treatment

Switzerland does not have a carried interest regime or preferential tax treatment for carried interest. However, this disadvantage can be mitigated by properly structuring the fund and fund management activities and obtaining a tax ruling from the relevant tax authority.

Swiss income taxation of carried interest depends on the legal form of the Swiss-based fund manager and the structure of the collective investment scheme. Income from fund management will be treated as self-employment income in the hands of a Swiss resident individual, and as taxable profit in the hands of a Swiss resident corporation. However, if Swiss resident fund managers employed by the fund management company hold their own units in the collective investment scheme (if they invest on the same terms as third-party investors) or participations in the fund management company, these units and participations may qualify as private assets. In that case, the capital gains realized upon the sale of these units and participations would qualify as tax-free private capital gains.

In addition, given the very low tax rates in some Swiss cantons and municipalities (with income tax rates in the highest bracket as low as approximately 19.6%, and corporate income tax rates as low as approximately 11.3%), the ordinary tax rules may already provide an attractive tax environment for fund managers and fund management companies.

Recent developments

Switzerland remains a stable and attractive market for private equity investments, with no changes expected for carried interest. The country's robust legal framework, favorable tax environment and strong financial infrastructure continue to make it an appealing destination for investors. Switzerland's commitment to maintaining a stable and predictable investment climate ensures that it remains an attractive choice for private equity firms seeking reliable opportunities.

8. Luxembourg

Current tax treatment

Luxembourg offers an attractive toolbox and significant flexibility for structuring private equity transactions. Carried interest can be structured in many different ways. In practice, various vehicles, such as special limited partnerships and unregulated SOPARFIs, are commonly used for carried interest vehicles or co-investment structures. The resulting tax treatment varies significantly depending on how carried interest is structured. In addition, as the beneficiaries may be tax resident in various jurisdictions, the tax treatment of the carried interest should also be assessed in each jurisdiction. Long-term capital gains generally enjoy a better tax treatment in most of the jurisdictions where beneficiaries are tax resident.

For Luxembourg tax resident beneficiaries, the tax treatment for carried interest depends on the nature of the income they derive. Generally, capital gains are not taxed in Luxembourg after a six-month holding period and if the carried interest holder does not hold directly or indirectly more than 10% of the capital of the underlying vehicle. Dividends are taxable at a progressive income tax rate of up to 45.78%, with a 50% exemption available under certain conditions.

In addition, although a specific regime for carried interest for employees of alternative investment fund (AIF) managers or management companies of AIFs was introduced several years ago, the favorable provision was transitional and restrictive in scope, considering the number of conditions to be met.

Recent developments

In light of this, on 24 July 2025, draft bill No. 8590 was introduced before the Luxembourg Parliament to clarify and broaden the tax treatment of carried interest, with the aim of aligning with AIF industry trends and enhancing Luxembourg's competitiveness by attracting front-office fund activities and talent in the alternative investment space.

Among its key aspects, the draft bill outlines the tax treatment applicable to Luxembourg tax-resident individuals entitled to carried interest across the various structuring options commonly used in the market:

- **Contractual carried interest**, received exclusively on a contractual basis with no required investment from the carried interest holder in the AIF, should benefit from favorable taxation at one-quarter of the standard global income tax rate in the hands of the Luxembourg tax-resident carried interest holder (up to 11.45%);
- **Participation-linked carried interest**, received exclusively on a contractual basis (but for which it is compulsory for the carried holder to also take a direct or indirect ordinary holding in the AIF) should, for the portion of income that constitutes a profit-sharing based on outperformance, not be subject to tax in the hands of the Luxembourg tax-resident carried interest holder, if the participation has been held for more than six months and the individual does not hold a substantial shareholding (i.e., does not hold more than a 10% shareholding, as defined in Article 100 of the Luxembourg amended income tax law of 4 December 1967);
- **Carried invest**, received via an ad hoc vehicle (such as a Luxembourg special limited partnership or a foreign partnership) that invests in the AIF, should, for the portion of income that constitutes a profit sharing based on outperformance, not be subject to tax in the hands of the Luxembourg tax-resident carried interest holder, under the same conditions as mentioned above.

To avoid complicating the taxation of Luxembourg tax-resident carried interest holders in cases where the AIF is transparent for Luxembourg tax purposes, this transparency should be disregarded for the sole purpose of applying the carried-interest tax regime to these individuals (i.e., no need to assess the nature of the income received by the tax-transparent AIF).

Finally, the draft bill proposes to abolish the specific transitional tax regime for carried interest introduced a few years ago. If certain managers still benefit from this regime, they should automatically switch to one of the categories of carried interest mentioned above, which should not be less advantageous.

The draft bill still requires parliamentary and State Council approval, but swift adoption is expected. Once enacted, the law should apply from the 2026 tax year.

You can find additional details in our client alert here.

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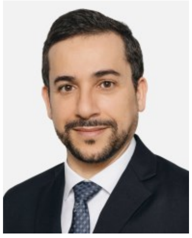

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