

Peter Kleingarn | Partner
Peter.kleingarn@aiqunited.com



Luxembourg publishes new circular on Art. 168quater (2) L.I.R.

On 22 August 2025, the Luxembourg tax authorities issued a Circular on Article 168quater (2) of the Luxembourg Income Tax Law (“L.I.R.”) (Circular No. 168quater/2), clarifying the definition of a “Collective Investment Vehicle” (“CIV”) within the meaning of Article 168quater (2) L.I.R. as interpreted by the tax administration.

Background: Article 168quater L.I.R., implementing the European ATAD II Directive with effect from the tax year 2022, provides that the income of a Luxembourg partnership is subject to corporate income tax in Luxembourg insofar as such income is not otherwise taxed under Luxembourg tax law or the law of another jurisdiction. The purpose should be to prevent untaxed income arising due to differences in the qualifications of the Luxembourg partnership, for example, where such partnership is treated as a partnership in Luxembourg but as a corporation in the jurisdiction of its investors. The rule under Article 168quater L.I.R. applies where one or more non-resident associated enterprises within the meaning of Article 168ter (1)(18) L.I.R. jointly hold, directly or indirectly, at least 50% of the voting rights, capital interests, or profit rights in the Luxembourg partnership. “Associated enterprises” within the meaning of Article 168ter (1)(18) L.I.R. are defined as:

- a) an entity in which the taxpayer (i.e. one of the non-resident partners of the Luxembourg partnership) holds, directly or indirectly, 50% or more of the voting rights or capital, or is entitled to receive 50% or more of the profits;
- b) a person or entity that holds, directly or indirectly, 50% or more of the voting rights or capital of the taxpayer, or is entitled to receive 50% or more of the taxpayer’s profits;
- c) an entity belonging to the same consolidated group for accounting purposes as the taxpayer;
or
- d) an entity over whose management the taxpayer exercises significant influence, or which exercises significant influence over the management of the taxpayer.

The provision makes an exception for undertakings for collective investment and investment funds, respectively. Under this provision, these are defined as undertakings that are widely held, maintain a diversified portfolio of securities and are subject to the investor protection rules of their country of domicile. Until the publication of the Circular, however, the above terms were not defined either legally or otherwise.

AIQUTAX 1, Hauptstrooss · L-6869 Wecker

Tel +352 26 20 23 32 · hello@aiqunited.com · www.aiqunited.com

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The Circular now provides clarity and confirms the established practice that Luxembourg

- Undertakings for collective investment within the meaning of the law of 17 December 2010 on undertakings for collective investment (UCIs);
- Specialized investment funds within the meaning of the law of 13 February 2007 on specialized investment funds (SIFs); and
- Reserved alternative investment funds within the meaning of the law of 23 July 2016 on reserved alternative investment funds (RAIFs)

are considered collective investment undertakings and are therefore exempt from the application of the provision.

For undertakings that do not fall into one of the three categories, the three cumulative criteria must be assessed:

- a) widely held (*“participation large”*),
- b) diversified securities portfolio, and
- c) investor protection regulations in the country of residence.

a) Widely held

This criterion is considered to be met if the units or shares in the entity are held by several independent investors. According to the Circular, to determine whether this criterion is met, a number of factors must be considered, which may be either factual or intentional in nature. The Circular thus offers flexibility in assessing this criterion and allows for the following:

- a limited number of investors at launch, provided that a wider investor base can reasonably be expected within 36 months, and
- exceptions during the liquidation phase, where the absence of a broad investor base is due to the liquidation process.

A fund is deemed to meet the condition of broad investor participation if no single investor directly or indirectly holds or controls more than 25% of the capital or voting rights.

Further, investors must not be regarded as associated investors. Associated investors exist where an investor directly or indirectly holds at least 50% of the voting rights or capital of the other, where a natural or legal person directly or indirectly holds at least 50% of the voting rights or capital of both investors, where a family relationship exists between the investors (e.g. spouse, partner, children, parents, siblings, grandparents, grandchildren or adopted children), or where one investor controls the other or both are under common control. In the case of master investment vehicles held by one or more

feeder funds, a look-through approach applies (i.e. in this case, the criterion is assessed by reference to the number of investors in the feeder fund(s)).

b) Diversified securities portfolio

For the purposes of Article 168quater (2) L.I.R., the term “securities” is to be understood broadly and includes:

- shares, company shares and other equivalent securities that grant or may grant access to the capital of a company,
- profit shares,
- bonds and other debt instruments,
- units in undertakings or investment funds,
- deposits with credit institutions and
- derivative financial instruments, provided that the underlying asset consists of securities.

The diversification of the securities portfolio is assessed based on the investment policy set out in the administrative regulations or the formation documents and the market risk (including direct and indirect counterparty risk), taking into account the investment policy pursued.

An undertaking is not considered diversified if the risk allocation does not comply with the requirements for specialised investment funds within the meaning of the 2007 SIF Law. Accordingly, an investment company or investment fund is, as a rule, not deemed to have a diversified securities portfolio where more than 30% of its assets or subscription commitments are invested in securities of the same issuer, unless a proper justification exists that warrants a higher investment in securities of that issuer.

c) Investor protection regulation

This condition is deemed to be met if the fund is subject to supervision by the *Commission de Surveillance du Secteur Financier* (CSSF) or, in the case of an alternative investment fund, if it is managed by an authorised AIFM in line with the AIFM Directive.

Conclusion

With this circular, the Luxembourg tax authorities have created legal certainty regarding the interpretation of Article 168quater (2) L.I.R., in particular that Luxembourg UCIs, SIFs and RAIFs are considered undertakings for collective investment and are therefore exempt from the application of reverse hybrid rules. For all other types of funds, however, the three cumulative criteria must be used to determine whether they qualify as CIVs.