

consideration of only those partnership items which are effectively connected (or treated as effectively connected) with the conduct of a trade or business in the United States. For purposes of determining the section 1446 withholding tax (1446 tax) under § 1.1446–3, partnership ECTI allocable under section 704 to foreign partners is the sum of the allocable shares of ECTI of each of the partnership's foreign partners as determined under paragraph (b) of this section. The calculation of partnership ECTI allocable to foreign partners as set forth in paragraph (b) of this section, and the determination of the partnership's withholding tax obligation, is a partnership-level computation solely for purposes of determining the 1446 tax. Therefore, any deduction that is not taken into account in calculating a partner's allocable share of partnership ECTI (e.g., percentage depletion), but which is a deduction that under U.S. tax law the foreign partner is otherwise entitled to claim, can still be claimed by the foreign partner when computing its U.S. tax liability and filing its U.S. income tax return, subject to any restriction or limitation that otherwise may apply.

(b) *Computation*—(1) *In general*. A foreign partner's allocable share of partnership ECTI for the partnership's taxable year that is allocable under section 704 to a particular foreign partner is equal to that foreign partner's distributive share of partnership gross income and gain for the partnership's taxable year that is effectively connected and properly allocable to the partner under section 704 and the regulations thereunder, reduced by the foreign partner's distributive share of partnership deductions for the partnership taxable year that are connected with such income under section 873 or 882(c) and properly allocable to the partner under section 704 and the regulations thereunder, in each case, after application of the rules of this section. For these purposes, a foreign partner's distributive share of effectively connected gross income and gain and the deductions connected with such income shall be computed by considering allocations that are respected under the rules of section 704 and § 1.704–1(b)(1), including special allocations in the partnership agreement (as defined in § 1.704–1(b)(2)(ii)(h)), and adjustments to the basis of partnership property described in section 743 pursuant to an election by the partnership under section 754 (see § 1.743–1(j)). The character of effectively connected partnership items (capital versus ordinary) shall be separately

considered only to the extent set forth in paragraph (b)(3)(v) of this section.

(2) *Income and gain rules*. For purposes of computing a foreign partner's allocable share of partnership ECTI under this paragraph (b), the following rules with respect to partnership income and gain shall apply.

(i) *Application of the principles of section 864*. The determination of whether a partnership's items of gross income are effectively connected shall be made by applying the principles of section 864 and the regulations thereunder.

(ii) *Income treated as effectively connected*. A partnership's items of gross income that are effectively connected includes any income that is treated as effectively connected income, including partnership income subject to a partner's election under section 871(d) or section 882(d), any partnership income treated as effectively connected with the conduct of a U.S. trade or business pursuant to section 897, and any other items of partnership income treated as effectively connected under another provision of the Code, without regard to whether those amounts are taxable to the partner.

(iii) *Exempt income*. A foreign partner's allocable share of partnership ECTI does not include income or gain exempt from U.S. tax by reason of a provision of the Internal Revenue Code. A foreign partner's allocable share of partnership ECTI also does not include income or gain exempt from U.S. tax by operation of any U.S. income tax treaty or reciprocal agreement. In the case of income excluded by reason of a treaty provision, such income must be derived by a resident of an applicable treaty jurisdiction, the resident must be the beneficial owner of the item, and all other requirements for benefits under the treaty must be satisfied. The partnership must have received from the partner a valid withholding certificate, that is Form W–8BEN or Form W–8IMY (see § 1.1446–1(c)(2)(iii) regarding when a Form W–8BEN or Form W–8IMY is valid for purposes of this section), containing the information necessary to support the claim for treaty benefits required in the forms and instructions to those forms. In addition, for purposes of this section, the withholding certificate must contain the beneficial owner's taxpayer identification number.

(3) *Deduction and losses*. For purposes of computing a foreign partner's allocable share of partnership ECTI under this paragraph (b), the following rules with respect to deductions and losses shall apply.

(i) *Oil and gas interests*. The deduction for depletion with respect to oil and gas wells shall be allowed, but the amount of such deduction shall be determined without regard to sections 613 and 613A.

(ii) *Charitable contributions*. The deduction for charitable contributions provided in section 170 shall not be allowed.

(iii) *Net operating losses and other suspended or carried losses*. The net operating loss deduction of any foreign partner provided in section 172 shall not be taken into account. Further, the partnership shall not take into account any suspended losses (e.g., losses in excess of a partner's basis in the partnership, see section 704(d)) or any capital loss carrybacks or carryovers available to a foreign partner.

(iv) *Interest deductions*. The rules of this paragraph (b)(3)(iv) shall apply for purposes of determining the amount of interest expense that is allocable to income which is (or is treated as) effectively connected with the conduct of a trade or business for purposes of calculating the foreign partner's allocable share of partnership ECTI. In the case of a non-corporate foreign partner, the rules of § 1.861–9T(e)(7) shall apply. In the case of a corporate foreign partner, the rules of § 1.882–5 shall apply by treating the partnership as a foreign corporation and using the partner's pro-rata share of the partnership's assets and liabilities for these purposes. For these purposes, the rules governing elections under § 1.882–5(a)(7) shall be made at the partnership level.

(v) *Limitation on capital losses*. Losses from the sale or exchange of capital assets allocable under section 704 to a partner shall be allowed only to the extent of gains from the sale or exchange of capital assets allocable under section 704 to such partner.

(vi) *Other deductions*. No deduction shall be allowed for personal exemptions provided in section 151 or the additional itemized deductions for individuals provided in part VII of subchapter B of the Internal Revenue Code (section 211 and following).

(vii) *Limitations on deductions*. Except as provided in paragraph (b)(3) or (4) of this section, any limitations on losses or deductions that apply at the partner level when determining ECTI allocable to a foreign partner shall not be taken into account.

(4) *Other rules*—(i) *Exclusion of items allocated to U.S. partners*. In computing ECTI allocable to a foreign partner, the partnership shall not take into account any item of income, gain, loss, or deduction to the extent allocable to any