A. WHO MUST MAKE A RETURN.—For each taxable year a return of income shall be made by every citizen of the United States, whether residing at home or abroad, and every individual residing within the United States though not a citizen thereof, whether or not he is the head of a family or the head of a family or other dependent. Where the return is actually prepared by another person, either a return must be signed by the person whose income is reported or by his legal representative or agent. The return may be signed by—

(a) the individual whose income is reported; (b) the husband or common law husband of such individual; (c) the wife or common law wife of such individual; or (d) any other legal representative or agent of such individual.

Where the return is prepared by a legal representative or agent, the return must be signed, under penalty of perjury, by the agent and, if the return is for a minor, by the parent or guardian of the minor, except that the return of a deceased individual shall be signed by such individual’s legal representative or agent.

B. WHO MUST USE FORM 1040.—Form 1040 must be used by all individuals (except nonresident aliens), who are required to make returns and whose net incomes are $5,000 or over, or whose return is made on an accrual basis, or whose return is made on a cash basis and report all income received or constructively received in the United States or of any State, Territory, or possession of the United States, or of the District of Columbia, whether received in cash or credited to an account, and any interest on obligations of the United States or of any State, Territory, or possession of the United States, or of the District of Columbia, whether received in cash or credited to an account.

C. RETURNS OF INCOME OF DECEASED.—If the net income of a decedent to the date of his death was $1,000 or over, or if, in excess of the credit allowed him by section 25 (b) (1) and (3) (computed without regard to his status as the head of a family), if married and living with spouse, or if his gross income for the period was $5,000 or over, the executor of the estate, or the surviving spouse, if a joint return is made, must file Form 1040 or Form 1040A. The return for a decedent shall include all items of income and deductions accrued up to the date of death (except deductions under section 23(g)) regardless of the fact that the decedent may have kept his books on a cash basis or an accrual basis.

D. PERIOD TO BE COVERED BY RETURN.—The return must be for the calendar year beginning in 1938 and ending in 1939.

E. WHEN AND WHERE THE RETURN MUST BE FILED.—On or before the 15th day of the third month following the close of your taxable year, you must file your return of income and deductions of each year covered by your return (or such later date as the Department shall prescribe). The return may be filed at any time during the taxable year, but not after the 15th day of the sixth month following the close of your taxable year.

F. AFFIDAVITS.—The affidavit must be executed by the person whose income is reported or his legal representative or agent. The return may be made by an individual (a) if, by reason of illness or infirmity, he is unable to make the return, or (b) if the taxpayer is unable to make the return by reason of continuous absence from the United States for a period of at least 60 days past the date described by law for making the return. Whenever a return is made by an agent, it must be accompanied by a power of attorney on Form 935, or, in the case of husband and wife, on Form 936 (copies of which may be obtained from any collector of internal revenue).

G. WHEN AND TO WHOM THE TAX MUST BE PAID.—The tax may be paid by sending or bringing with the return a check or money order payable to the Treasurer of the United States. Do not send cash by mail, nor pay it in person except at the collector’s office.

H. PENALTIES.—The law imposes severe penalties for failing to make a return or for making a false or fraudulent return. Penalties are also imposed for failing to file a return on time.

I. RECEIVED OR ACCRUED INCOME.—If your books of account are kept on the accrual basis, report all income accrued, even though it has not been actually received or entered on the books, and expenses incurred for the taxable year, as of the date of the close of the taxable year, whether paid or not.

J. ITEMS PARTIALLY AND WHOLLY EXEMPT FROM TAX.—All items of income received and claimed to be wholly exempt should be explained in Schedule I, except interest to be reported in Schedule B.

K. TREATMENT OF DEPRECIATION AND DEPLETION.—A reasonable allowance for the exhaustion, waste and tear, including obsolescence, of property used in the trade or business may be deducted. All depreciation and depletion claims must be made in the manner prescribed by the Commissioner of Internal Revenue. If the reason for the claimed deduction for obsolescence is explained, explain why the useful life is less than the actual life.

L. THE AMOUNT OF DEPRECIATION ON PROPERTY ACQUIRED BY PURCHASE SHOULD BE DETERMINED UPON THE BASIS OF THE ORIGINAL COST (NOT REPLACEMENT COST) OF THE PROPERTY AND THE PROBABLE NUMBER OF YEARS IN WHICH IT WILL REMAIN USEFUL, EXCEPT IF THE PROPERTY WAS PURCHASED PRIOR TO MARCH 1, 1913, IT WILL
Salaries, wages, interest, rents, commissions, or other fixed or determinable salaries or other compensation for personal services aggregating less than each recipient, except that a return need not be made for payments of income of $1,000 or more during the calendar year 1938, to an individual, a $2,500 made to a married individual. These forms will be furnished by any collector of internal revenue upon request and must be forwarded to the Commissioner of Internal Revenue Sorting Section, Washington, D. C., in time to be received not later than February 15, 1939.

M. STOCK OWNED IN FOREIGN CORPORATIONS AND PERSONAL HOLDINGS

If you own any stock during the taxable year you owned directly or indirectly any stock of a foreign corporation (including a foreign personal holding company, as defined in section 331, in which you owned less than 5 percent in value of the outstanding stock of such company) or a personal holding company, as defined in section 331, you must include in your return as a dividend the amount required to be included in your gross income by section 337. If you owned 5 percent or more in value of the outstanding stock of such foreign personal holding company, set forth in an attached statement in complete detail the information required by section 337 (d).

SPECIFIC INSTRUCTIONS

The following instructions are numbered to correspond with item numbers on page 1 of the return.

Salaries and other compensation for personal services.—Any amount claimed as a deduction for ordinary and necessary expenses against salaries, etc., such as traveling expenses while away from home in connection with your occupation, should be fully explained in Schedule A or in an attached statement. Traveling expenses ordinarily include expenditures for transportation, meals, and lodging. The expenses of a commuter in traveling to and from work are not deductible.

Dividends.—Dividends on share accounts in Federal savings and loan associations. Earnings of minor children should also be entered in Schedule A.

Interest received which are claimed to be nontaxable, and include in item 11 the following: (a) Gross sales; (b) cost of goods sold; (c) gross profits; (d) percentage of profits to gross sales; (e) amount collected; and (f) gross profit on amounts mentioned above subject to approval by the Commissioner upon examination of the return. If the installment method is used, attach to the return

Inventories.—Include in Schedule C giving the

Inventories shall be computed on the fair market value of such property as of that date or its original cost (less depreciation actually sustained before that date), whichever is less. If the property was acquired in any other manner than by purchase, see section 114.

See sections 23 (m) and 114 and Regulations 101 with respect to additional forms and information required if a deduction is claimed for depletion.

L. INFORMATION AT SOURCE.—Every person making payments of salaries, wages, interest, rents, commissions, or other fixed or determinable income of $1,000 or more during the calendar year 1938, to an individual, a partnership, or a fiduciary, is required to make a return on Forms 1096 and 1099, showing the name and address of each such individual or entity, the name and address of each such company and the total number of shares of each class of outstanding stock owned by you during the taxable year. If you owned stock at any time during the taxable year in a foreign personal holding company, as defined in section 331, you must include in your return as a dividend the amount required to be included in your gross income by section 337. If you owned 5 percent or more in value of the outstanding stock of such foreign personal holding company, set forth in an attached statement in complete detail the information required by section 337 (d).
business, but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale to customers in the ordinary course of his trade or business, or property, used in the trade or business at the time of the sale or exchange, or property which is subject to the allowance for depreciation. The exclusion from the term “capital assets” of property used in the trade or business of a taxpayer which is subject to allowance of depreciation provided in section 23 (l) is limited to property used by the taxpayer in the trade or business at the time of the sale or exchange. It has no application to the arising of or diminution of the value of the trade or business to the extent that such gain or loss is allocable to the land, as distinguished from depreciable improvements upon the land.

**Description of property.**—Every sale or exchange of property, even though no gain or loss may be indicated, must be reported in detail. Enter full description of each item of property sold or exchanged. Such description should include the following facts: (a) description of the property as determined by a description of land, description of improvements, details explaining depreciation (column 7 of Schedule F) ; (b) for bonds or other evidences of indebtedness, name of issuing corporation, description of the particular issue, denomination, and amount; and (c) for stocks, name of corporation, class of stock, number of shares, capital changes affecting basis (non taxable stock dividends, other nontaxable dividends, stock rights, etc.).

**Basis.**—If the property was acquired before March 1, 1913, the “basis” for the property is not subject to the same rule for reporting gains as for losses. In such case, the “basis” for determining GAIN is the cost or the fair market value at March 1, 1913, whichever is greater, but in determining LOSS the basis is cost so adjusted. If the property was acquired after March 1, 1913, basis for both gain and loss is the cost of such property, except as otherwise provided in section 111. The exception for gains is that such property may be sold without request, tax-free exchange, involuntary conversion, wash sale of stock; and in such cases section 113 provides the basis that shall be used. If the amount shown as the basis is other than actual cash cost of the property sold or exchanged, full details must be furnished regarding the acquisition of the property.

Enter in column 7 of Schedule F, or in column 6 with respect to Schedule G, the amount of depreciation, exhaustion, wear and tear, obsolescence, or depletion which has been allowed (but not less than the amount allowable in respect of such property since date of acquisition, or since March 1, 1913, if property is properly before that date. In addition, if the property was acquired before March 1, 1913, the cost shall be reduced by the depreciation actually sustained before that date.

Subsequent improvements include expenditures for additions, improvements, and renewals and replacements made to restore the property or prolong its useful life. They do not deduct ordinary repairs, interest, or taxes in computing gain or loss.

**Losses on securities becoming worthless.**—If any securities (as defined below) are ascertainable to be worthless and charged off within the taxable year and are capital assets, the loss resulting therefrom shall, in the case of a taxpayer other than a bank, as defined in section 1104, be considered as a “loss” from the sale or exchange, on the last day of such taxable year, of capital assets.

**Definition of securities.**—As used for this purpose, the term “securities” means bonds, debentures, notes, or certificates, or other evidences of indebtedness, issued by a state, its political subdivisions, or any other corporation, public or private, a trust, partnership, or other person or association, whether domestic or foreign, that are or are held for investment. For the purposes of this date, securities which are held for sale to customers or held primarily for the production of income shall not be considered as securities.

**Losses on stocks or stock rights becoming worthless.**—If any shares of stock in a corporation or rights to subscribe for or to receive such shares become worthless during the taxable year, and are capital assets, the loss resulting from the sale or exchange, on the last day of such taxable year, of capital assets.

**Classification of capital gains and losses.**—Section 117 (a) (2) to (9), inclusive, defines “short-term capital gain,” “short-term capital loss,” “long-term capital gain,” “long-term capital loss,” “net short-term capital gain,” “net short-term capital loss,” “net long-term capital gain,” and “net long-term capital loss.” The phrase “short-term” applies to the category of gains and losses arising from the sale or exchange of capital assets held for 18 months or less; the phrase “long-term,” to the category of gains and losses arising from the sale or exchange of capital assets held for more than 18 months.

In the case of individuals, gains and losses from sales or exchanges of capital assets held for not more than 18 months (described as short-term capital gains and short-term capital losses) shall be segregated from gains and losses arising from the sale or exchange of such assets held for more than 18 months (described as long-term capital gains and long-term capital losses).

**Percentage of capital gain or loss taken into account.**—In computing the net income of an individual, the following percentages of the gain or loss recognized from the sale or exchange (a capital gain or loss) shall be taken into account in computing net income:

- **100%** if the capital asset has been held for not more than 18 months; 0% if the capital asset has been held for more than 18 months and not more than 24 months.
- **50%** if the capital asset has been held for more than 24 months.

**Limitation on short-term capital losses.**—Section 117 (d) (2) provides a limitation on deductions for short-term capital losses of individuals, that is, losses from sales or exchanges of capital assets held for 18 months or less shall be allowed as deductions only to the extent of the gains from sales or exchanges of capital assets held for 18 months or less. However, subsection (e) provides that in the case of an individual having in any taxable year (beginning after December 31, 1937) a net short-term capital loss, he may carry over such loss, in an amount not in excess of his net income for such year (the year in which the loss is realized), to the next succeeding taxable year for offset against such a long-term capital loss. The carry-over is thus applied in such succeeding year to offset any short-term capital gains in such succeeding year not already offset by short-term capital losses in such year. The carry-over is restricted to one year, namely the succeeding taxable year, and hence the amount of the net short-term capital loss carried over may not incurring a new short-term capital loss which can be carried over to the succeeding taxable year. In the case of individuals, there is no limitation on deductions for long-term capital losses.

**Alternative tax in case of net long-term capital gain or loss.**—In the case of a net long-term capital gain of an individual, subsection (c) (1) of section 117 imposes an alternative tax in lieu of the normal tax and surtax imposed upon net income, if and only if such alternative tax is less than the tax otherwise imposed. The tax is imposed at the normal tax and surtax rates on the net income of the taxpayer decreased by the amount of such net long-term capital gain, plus (2) 30 percent of the net long-term capital gain.

In the case of a net long-term capital loss of an individual, an alternative tax is imposed in lieu of the normal tax and surtax imposed on net income, if and only if such alternative tax is greater than the tax otherwise imposed. This alternative tax is the excess of (1) a tax, computed at the normal tax and surtax rates on the net income of the taxpayer decreased by the amount of such net long-term capital loss, over (2) 30 percent of the net long-term capital loss.

**Determination of period for which capital assets are held.**—If property was acquired in certain transactions described in sections 112, 113, and 118, the period for which such property is considered to have been held by the taxpayer is not computed from the date such property was acquired by the taxpayer but from a prior date, as provided in section 117 (b).

**Agriculture and year-end life.**—In the application of section 117 to short-term capital gains and losses, a husband and wife, regardless of whether a joint return or separate returns are made, are considered to be separate taxpayers. Accordingly, the limitation under section 117 (d) (2) on the allowance of losses of one spouse from the sales or exchanges of capital assets held for more than 18 months is in all cases to be computed without regard to gains and losses of the other spouse upon sales or exchanges of capital assets held for not more than 18 months. In the case of a joint return of a husband and wife, capital transactions of each should be reported in separate schedules.

**Losses from sales or exchanges of capital assets held for not more than 18 months.**—See section 117 (g). As to gains and losses from distributions in liquidation of corporations, see section 115 (c).

**Losses not allowable. — Wash sales.**—In the case of any loss claimed to have been sustained from any sale or other disposition of shares of stock or securities where it appears that, within a period beginning 30 days before the date of sale or disposition and ending 30 days after such date, the taxpayer acquired has (by purchase or by an exchange upon which the entire amount of gain or loss was recognized by law), or has entered into a contract or option so to acquire, substantially identical stock or securities, then no deduction for the loss shall be allowed unless the claim is made in connection with the tax period of the taxpayer (section 117 (f) (8)).

**Losses in transactions between certain persons.**—No deduction shall be allowed in respect of losses from sales or exchanges of property, directly or indirectly:

- A. Between members of a family, which is defined for the purpose of this paragraph to include one or more of the taxpayer’s brothers and sisters (whether by the whole or half blood), spouse, ancestors, and lineal descendants;
- B. Except in the case of distributions in liquidation, between an individual and a corporation owned by him, or to which he makes a substantial contribution, or to which he contributes, in connection with his trade or business. (See section 118.)
- C. Between a grantor and a beneficiary of any trust; or
- D. Between a beneficiary of a trust and a beneficiary of such trust.

For the purposes of determining ownership of stock in applying this paragraph, see section 24 (b) (2).

**11. Other income.**—If you had any taxable income, space for reporting which is not provided elsewhere on the return, enter it as item 11, and explain its nature, using a separate sheet if necessary for that purpose. Include in this item taxable income from annuities and insurance proceeds. Include any income from gifts or bequests of property which is not provided elsewhere on the return. Exceptions are the income from gifts or bequests of property, which shall be included in gross income to the extent of 3 percent of the aggregate premiums or consideration paid for such annuity. If the aggregate of the amounts received and excluded from gross income in years previous to the taxable year equals the aggregate premiums or consideration paid for such annuity, the entire amount received must be included in gross income. (Section 22 (b) (2).)

Amounts received during the taxable year under a life insurance or endowment policy (other than amounts paid by reason of the death of the insured, interest payments on such amounts, and amounts received as annuities) shall be included in gross income if the amounts so received (when added to the amounts excluded before the taxable year under such policy) exceed the total premiums or consideration paid.
13. Contributions paid.—Enter as item 13 the contributions or gifts reported in Schedule H, payment of which was made within the taxable year for or on account of—

(a) The United States, any State, Territory, or any political subdivision thereof, or the District of Columbia, for public purposes;

(b) A domestic corporation, or domestic trust, or domestic community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals; or

(c) A domestic foundation, society, order, or association, operating under the local system, but only if such contributions or gifts are to be used exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals.

The amount claimed shall not exceed 15 percent of your net income computed with reference to item 11. See section 43 for limitations on this deduction.

14. Interest.—Enter as item 14 interest on personal indebtedness as distinguished from business indebtedness (which should be deducted under Schedules C and D). Do not include interest on indebtedness incurred or continued to purchase or carry obligations (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from taxation. Any deductions on account of interest should be explained and itemized in Schedule H.

Attention is called to the following limitations on deductions for unpaid expenses and interest provided in section 24 (c):

(c) Unpaid expenses and interest.—In computing net income no deduction shall be allowed for unpaid expenses or interest in respect of any transaction which inures to the benefit of any private shareholder or individual, and no substantial part of the activities of which are carried on or done for the benefit of individuals who are not shareholders or individuals.

15. Taxes.—Enter as item 15 taxes imposed upon you and paid or accrued during the taxable year, not including taxes on property used in your business or profession and those assessed against the Federal Government of a kind tending to increase the value of the property assessed. Do not include Federal income taxes, nor estate, inheritance, legacy, succession, gift taxes, taxes imposed upon your interest as shareholder of a corporation which are paid by the corporation without reimbursement from you, nor income taxes claimed as a credit in item 33. Tax withheld or paid under section 801 of the Social Security Act for or in behalf of the employee is a Federal income tax and is not deductible by the employee. Do not include sales taxes unless such taxes are imposed solely upon you directly by your State. Deductions allowable for any portion of foreign income and profits taxes if a credit is claimed in item 33.

Any deduction on account of taxes should be explained and itemized in Schedule H.

16. Losses from fire, storm, shipwreck, or other casualty, or theft.—Enter as item 16 losses of property not connected with your business or profession, sustained during the year, if arising from fire, storm, shipwreck, or other casualty, or from theft, and if not compensated for by insurance or otherwise.

Explain and itemize losses claimed in Schedule H, setting forth a description of the property, date acquired, cost, subsequent improvements, depreciation allowable since acquisition, insurance, salvage value, and deductible loss.

17. Bad debts.—Enter as item 17 all bad debts other than those claimed as a deduction in Schedule D. State in Schedule H (a) of what the debts consisted, (c) what, if anything, was outstanding, and (d) the date or dates when they were created, (e) when they became due, (f) what efforts were made to collect, and (g) how they were actually determined to be worthless. Bonds which are ascertainable to be worthless and charged off within the taxable year, and which were written off before treated as bad debts, but the loss resulting therefrom shall be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets and should be reported in Schedule F.

18. Other deductions.—Enter as item 18 any other authorized deductions for which no space is provided on page 1 of the return. Do not deduct losses incurred in transactions which were neither connected with your trade or business nor entered into for profit. Losses from wagering transactions and losses from capital assets should be reported in Schedule F. Any deduction claimed should be explained in Schedule H.

Stock and stock rights which become worthless during the taxable year, and which are disposed of before the close of the year, should be reported in Schedule H, but the loss resulting therefrom shall be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets and should be reported in Schedule F.

In case you are in business in connection with exempt income (other than interest) or owned any property the income from which is exempt, see section 24 (a) (5) and Regulations 101.

22. Credit for personal exemption and dependents.—Enter as items 22 and 23 the amounts explained in Schedule J–1 and J–2. A single married person (other than husband or wife), or entitled to a personal exemption of $1,000. A person who, during the entire taxable year, was the head of a family or was married and living with husband or wife, is entitled to an exemption of $2,500. If husband and wife file separate returns, the personal exemption may be taken by either or divided between them.

A head of a family, if married, is entitled to a credit of $200 in each of two individuals.

If the status of the taxpayer, insofar as it affects the personal exemption or credit for dependents, changes during the taxable year, the personal exemption and credit shall be apportioned in accordance with the number of months before and after such change. For the purpose of such apportionment a fractional part of a month shall be disregarded unless it amounts to more than half a month, in which case it shall be considered as a month. For example, if a child became 18 years of age on June 16, 1938, the taxpayer will be allowed a credit of $200 for such dependent.

25. Credit for interest on Government obligations, etc.—Enter as item 25 the annual interest on Government obligations, etc., reported in item 5, and any dividends on share accounts in Federal savings and loan associations reported in item 11.

26. Earned income credit.—Enter as item 26 the amount of earned income computed in Schedule K–1 or K–2, and the taxable year in which or with which the taxable year of the taxpayer ends; and (3) If, by reason of the method of accounting of the person to whom the payment is to be made, the amount thereof is not, unless paid, includable in the gross income of such person for the taxable year or portion thereof in which or with which the taxable year of the taxpayer ends, and

(3) If, at the close of the taxable year of the taxpayer or at any time within two and one-half months thereafter, both the taxpayer and the person to whom the payment is to be made are persons between whom losses would be disallowed under section 24 (b).

15. Taxes.—Enter as item 15 taxes imposed upon you and paid or accrued during the taxable year, not including taxes on property used in your business or profession and those assessed against the Federal Government of a kind tending to increase the value of the property assessed. Do not include Federal income taxes, nor estate, inheritance, legacy, succession, gift taxes, taxes imposed upon your interest as shareholder of a corporation which are paid by the corporation without reimbursement from you, nor income taxes claimed as a credit in item 33. Tax withheld or paid under section 801 of the Social Security Act for or in behalf of the employee is a Federal income tax and is not deductible by the employee. Do not include sales taxes unless such taxes are imposed solely upon you directly by your State. Deductions allowable for any portion of foreign income and profits taxes if a credit is claimed in item 33.

Any deduction on account of taxes should be explained and itemized in Schedule H.

16. Losses from fire, storm, shipwreck, or other casualty, or theft.—Enter as item 16 losses of property not connected with your business or profession, sustained during the year, if arising from fire, storm, shipwreck, or other casualty, or from theft, and if not compensated for by insurance or otherwise.

Explain and itemize losses claimed in Schedule H, setting forth a description of the property, date acquired, cost, subsequent improvements, depreciation allowable since acquisition, insurance, salvage value, and deductible loss.

17. Bad debts.—Enter as item 17 all bad debts other than those claimed as a deduction in Schedule D. State in Schedule H (a) of what the debts consisted, (c) what, if anything, was outstanding, and (d) the date or dates when they were created, (e) when they became due, (f) what efforts were made to collect, and (g) how they were actually determined to be worthless. Bonds which are ascertainable to be worthless and charged off within the taxable year, and which were written off before treated as bad debts, but the loss resulting therefrom shall be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets and should be reported in Schedule F.

18. Other deductions.—Enter as item 18 any other authorized deductions for which no space is provided on page 1 of the return. Do not deduct losses incurred in transactions which were neither connected with your trade or business nor entered into for profit. Losses from wagering transactions and losses from capital assets should be reported in Schedule F. Any deduction claimed should be explained in Schedule H.

Stock and stock rights which become worthless during the taxable year, and which are disposed of before the close of the year, should be reported in Schedule H, but the loss resulting therefrom shall be considered as a loss from the sale or exchange, on the last day of such taxable year, of capital assets and should be reported in Schedule F.

In case you are in business in connection with exempt income (other than interest) or owned any property the income from which is exempt, see section 24 (a) (5) and Regulations 101.

32. Income tax paid at the source.—Enter as item 32, 2 percent of interest on bonds on which a Federal income tax was paid at the source by the corporation.