

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date June 27, 1941

To Mr. Despres

Subject: The British Forced Savings

From Mr. Jaszi G.J

Scheme

A forced savings scheme was introduced in Great Britain as a part of the Budget for 1941-42.

The scheme applies to two classes of taxpayers: those subject to excess profits tax and those subject to individual income tax. 20 per cent of excess profits tax liability is to be set aside as a postwar credit; and individual income taxpayers will be credited with an amount equal to that part of their increased income tax liability under the new budget which is due to the lowering of exemptions and of the earned income credit. A ceiling of £ 65 is imposed on the postwar credit that can be accumulated by an individual income taxpayer.

The credit with respect to excess profits tax liability is a concession to those who argued that the 100 per cent excess profits tax now in force in Great Britain destroys all incentive for the efficient conduct of business. The 100 per cent tax rate is retained, but businesses may now have an incentive to operate efficiently, because this will add to their postwar credit. The scheme will also ease the financial problems of postwar reconstruction by putting funds into the hands of businesses at that time.

With regard to individual income taxpayers, the main motivation must have been to make more palatable the increase of the tax burden to the 2,000,000 persons who, under the new tax laws, become liable to income tax for the first time, and to other low income taxpayers whose tax burden is sharply increased.

The thought that the spending of these credits will mitigate the postwar slump was also a consideration in establishing the scheme. But the £ 65 ceiling provision and the particular formula used for determining forced savings indicate that, so far at least, there is no serious intention to build up a substantial amount of forced savings. The maximum figure which a married taxpayer without dependents will save under the scheme is less than 7 per cent of income. This percentage declines rapidly for larger incomes.

It is estimated that about £ 125 million will be accumulated as post war credits of individuals in the first full year of operation of the scheme. The annual postwar credit of businesses may amount to another £ 50 million. These are moderate sums as compared with the scale of total government financing, and unless the scheme is considerably expanded the repayment of credits after the war should not give rise to serious financial problems. The manner of repayment has not yet been decided upon.