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March 22, 2005

ALAN GREENSPAN
CHAIRMAN

The Honorable Connie Mack
Chairman
President's Advisory Panel
on *Federal Tax Reform*
1440 New York Avenue, N.W.
Suite 2100
Washington, D.C. 20220

Dear Mr. Chairman:

It was a pleasure seeing you at the meeting of the Tax Reform Panel, and I appreciate having had the chance to share some thoughts with the group. Because I did not get a chance to answer your last question at the meeting, I would like to follow up with a response. In particular, you raised the issue of whether a shift toward a consumption tax could, in the short run, lead to a reduction in consumption and a shortfall in aggregate demand.

As you know, the current tax system is a hybrid, with elements of both an income tax and a consumption tax. Thus, a new tax system with some consumption tax elements, such as expanded 401(k) plans, would not necessarily represent a dramatic shift from the current system. More broadly, in designing a new tax system, policymakers will need to balance tradeoffs among the objectives of simplicity, fairness, and economic efficiency. A tax system that appropriately balanced these goals would help to create an environment conducive to favorable underlying, or long-run, rates of economic growth. Because a new tax system is likely to be in place for a considerable period of time, I believe that the primary focus of tax reform efforts should be on these longer-run objectives. Moreover, if changes to the tax code were to have short-run implications for the economy, the code likely would provide for a considerable phase-in period, which would give policymakers ample time to assess the situation and put in place any appropriate actions.

Again, thanks for the opportunity to meet with the panel. I look forward to seeing the results of your work.

Sincerely,
A handwritten signature in black ink, appearing to read "Alan Greenspan".