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The Bermuda Inversion

Treasury Secretary Paul O'Neill is the only person involved in the corporate tax debate who seems to be thinking past the next election.

Treasury issued a timely report Friday on corporate "inversion," which is when U.S. multinationals relocate their headquarters offshore to avoid the high and complex income taxes that their foreign competitors don't have to pay. "If the tax code disadvantages U.S. companies competing in the global marketplace, then we should address the anti-competitive provisions of the code," said Mr. O'Neill, getting to the root of the problem.

In recent years a number of large firms, including Tyco International and Ingersoll-Rand, have nominally reincorporated in tax havens like Bermuda to stay competitive. The U.S. tax code, as the Treasury report notes, puts U.S. firms at a disadvantage by taxing income earned in other countries, something most other nations don't do.

Mr. O'Neill is concerned that Congress's efforts to address the problem are shortsighted (imagine that!) and, according to the report, could "have the unintended effect of encouraging a shift to other forms of transactions to the detriment of the U.S. economy in the long run."

He may have in mind Representative Nancy Johnson (R., Conn.), who wants a "temporary" ban on inversions. Ms. Johnson is in a re-election battle in a redrawn district with Democrat Jim Maloney. Their state is home to Stanley Works, the toolmaker that wants to change its nominal domicile to Bermuda and save $30 million per year in taxes. Maybe they'd rather have Stanley lay off workers instead.

Others have proposed punitive measures, claiming the U.S. tax base is in jeopardy. But these are political arguments, not economic ones. The corporate income tax accounted for 28% of federal tax receipts in the 1950s but now makes up just 10.4%. This amounts to around $200 billion out of $2 trillion in total government receipts, a relatively small chunk of change in Uncle Sam's pocket.