Jan. 14 (Bloomberg) -- The Internal Revenue Service, reversing an earlier position, proposed rules making it more likely informants will collect a reward when they blow the whistle on tax-dodging employers, neighbors or family members.

The agency proposed regulations today that make it easier for whistleblowers whose information results in denial of refunds or a reduction in deductible losses to get rewards of as much as 30 percent of the amount involved. Earlier guidance tied reward payments to a portion of additional taxes paid as a result an informant’s tip.

“These regulations are good news for whistleblowers,” Iowa Senator Charles Grassley, who authored the 2006 law enhancing reward payments for informants, said in a statement.

The shift helps position the IRS to begin making large payouts for the first time under a 2006 law mandating higher rewards to whistleblowers. The new regulations were written by Heather Maloy, a top official in charge of services and enforcement who serves as a deputy to IRS Commissioner Doug Shulman.

“It’s the first time IRS senior management has paid attention and looked at this program,” said Dean Zerbe, a lawyer representing whistleblowers who wrote the statute when he was an aide to Grassley.

Sending a Signal

“It sends a signal up and down the lines of the IRS that ‘hey, senior management likes this program and want this program to be a success,’” Zerbe said.

IRS spokesman Frank Keith said the regulations, issued in proposed form, “alters the computation of the award they’re entitled to.” He said the rules demonstrate “the IRS is completely and totally committed to implementing the whistleblower statute.”

Congress enhanced the IRS whistleblower program in 2006 to increase rewards and mandate the agency pay more of them. Under the law, whistleblowers may collect 15 percent to 30 percent of taxes collected as a result of the information they provided. Tips, many claiming cases of fraud involving more than $2 million, have poured in since.

Tips Increase

In an annual report to Congress submitted last month, the IRS said it received 460 submissions in fiscal year 2009, which ended Sept. 30, 2009. The tipsters identified 1,941 taxpayers, each suspected of avoiding at least $2 million in tax. That compares with 475 submissions identifying 1,246 alleged tax cheaters in the previous year.

Even so, the agency has yet to pay a single reward under the new program. Grassley said in December that the program was being “underused” after the IRS said it had failed to pay an award for the third consecutive year since the law was enacted.

George Clarke, a partner at the Miller and Chevalier law firm in Washington, said the proposed regulations are apt to encourage more claims. “I think it will definitely cause more growth in the cottage industry,” he said. “There’s now a very clear other set of taxpayer filings that can be put in jeopardy by information from a whistleblower.”

Jack Blum, a Washington attorney representing two whistleblowers including Heinrich Kieber, the Liechtenstein computer technician who reported clients of LGT Group to tax authorities around the world, said the biggest signal the IRS could send that it is serious would be to pay up.

Paying Rewards

“These guys are still, as far as I can tell, not paying anything,” Blum said. “As far as I know that office is deadwood,” he said, referring to the IRS’s whistleblower office.

The regulations proposed today remove two barriers to payment that the IRS had affirmed as recently as July.

Under those procedures, informants could receive payment only if their information resulted in an additional collection of taxes by the government. Awards were denied if the information merely stopped fraudulent refunds. They were also blocked when an accused taxpayer had too many losses to owe taxes even after the IRS disallowed a fraudulent transaction.

Payment would be denied, for example, if a bank’s tax director informed the IRS of a bogus $100 million transaction that made the bank appear to have a net loss. The agency would deny half of the transaction as a result of the information.

Previous Rules

Under the previous procedures, the informant would receive nothing. The new rule would allow the informant to claim a share of the $50 million, Keith said.

“A lot of those things fall into those buckets,” Zerbe said of whistleblower tips. Among others, Zerbe represents Bradley Birkenfeld, a former Swiss banker at
UBS AG who blew the whistle on clients including Igor Olenicoff, a California billionaire convicted of cheating on his taxes. Despite providing information to U.S. authorities, Birkenfeld was imprisoned for helping Olenicoff and others.

Blum said the regulations likely won’t affect claims such as those by his clients. Those claims involved people who hid income from the IRS in undeclared overseas accounts.

“That’s probably not going to affect the kind of stuff I’ve been involved in because these people simply didn’t report income,” he said.

The 2006 law spurred a legal industry built around submitting claims.

After the law was enacted, the Miami-based Ferraro Law Firm, which had specialized in personal-injury cases involving cancers related to asbestos, opened a Washington office that recruits and represents clients making whistleblower claims. The firm has said it made several claims alleging more than $1 billion in unpaid taxes.

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