



The Importance of Regulations in Tax Law, Especially After Kentucky's Recent Tax Reform – Part 1

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The importance of regulations in the world of tax is often overlooked, but in many cases, regulations cut both ways – being a taxpayer's best friend for guidance purposes or the government's first line of defense when enforcing tax laws. (You can [view Part 2 to this article by clicking here.](#))

Kentucky is no different, especially after it recently passed substantial tax reform legislation in 2018, as well as the likely passing of a tax cleanup bill in 2019 (HB 354). The Kentucky Department of Revenue ("Department") has also begun slowly rolling out its view of the new tax laws through the repeal, creation and amending of dozens of administrative regulations. In this blog post, we explore the basics and authority of regulations and their role in tax administration. In the next post, we will take a dive into many of the important regulations the Department recently released to the public and their likely effect on the business community.

Basics and Authority of Administrative Regulations in State and Local Taxes

One of the basic rules you learn in law school is the hierarchy of authorities at both the federal and state level. The Constitution is the law of the land, with statutes being the next level of authority, and then finally there are regulations. The primary purpose of regulations is for an agency that oversees a certain subject area to provide its reasonable interpretation of statutes passed by Congress or a state legislature and while providing the general public with additional guidance on same. Although a regulation has the force and effect of law, this is only true if several things occur, including that a proposed regulation follows strict filing, notice and comment rules, is formally promulgated, and is a reasonable and lawful interpretation of the law.

Kentucky, for example, has very strict requirements for the promulgation of administrative regulations and, unlike many states, has its own detailed version of an Administrative Rulemaking Procedure Act, found in KRS Chapter 13A. In general terms, KRS Chapter 13A empowers an administrative body or agency, such as the Department, with authority to formally promulgate an administrative regulation, but only if it is “consistent with applicable statutes,” as a means of providing additional guidance for such statute(s).[\[i\]](#)

KRS Chapter 13A was primarily created to ensure that the public is notified of, and able to participate in, an agency’s attempted creation or modification of administrative guidance. In fact, an agency such as the Department is prohibited from creating and enforcing any sort of policy, practice or procedure which interprets tax statutes unless it has done so through a formal administrative regulation by following all procedural requirements, including notice and comment to the public and review by legislative committees. This is important as it helps prevent the Department from enforcing “secret laws” which can be used against, and to the detriment of, unsuspecting taxpayers.[\[ii\]](#) Thus, any sort of policy, guidance, memorandum, standard or any similar writing by an administrative agency – here, the Department – does not have the force and effect of law unless such a writing has been duly promulgated, and Kentucky courts have consistently enforced this rule.[\[iii\]](#)

Moreover, if an administrative body violates KRS Chapter 13A by attempting to use, implement or enforce a non-promulgated policy or writing, then such an “administrative body memorandum, internal policy, or other form of action...is null, void and unenforceable.” As a result, Kentucky courts have not been scared to strike down various internal policies, circulars, procedures and other writings created, used and enforced by an administrative body, including the Department, as well as strike down promulgated regulations.[\[iv\]](#)

Finally, despite an agency’s adherence to all requirements for filing and promulgating an administrative regulation, if its interpretation of the statutes in the formal regulation is not reasonable, or it enlarges, limits or contradicts the terms of the statute itself, the regulation is also prohibited as a matter of law and can be stricken down.[\[v\]](#)

Again, why is this important? Because, as we often see in our practice, a taxpayer can be assessed additional tax, or denied a refund, due to a federal, state or local taxing agency's enforcement of a policy or regulation, whether promulgated or not. And the taxpayer should be prepared to call foul on use of such authority if it fails to meet any or all of the strict requirements outlined above.

In Kentucky, this becomes even more critical because the Department has rolled out several new, amended or repealed administrative regulations over the past few months as it continues to interpret the substantial changes made to the Kentucky tax code in early 2018, along with any additional changes made by the General Assembly during the 2019 Regular Session.

One must pay close attention to the details of these regulations – not only for a general understanding of the new laws, but also to make sure new interpretations of old tax laws aren't thrown in, too, and become law before anyone notices or objects to same. Although the Department worked with representatives from our firm, and other Kentucky tax professionals and business organizations, to craft these proposed regulatory changes, the Department ultimately has the final say on the proposed language. Given its importance to the implementation of Kentucky's new tax code, we will take a deeper look at what has been proposed thus far in my next blog post.

View the follow up to this post: [Kentucky Issues New Tax Regulations – Part II: The Importance of Tax Regulations and its Critical Role After Kentucky's Recent Tax Reform](#)

In the meantime, if you have questions about any of the issues raised above, you can contact me ([Daniel Mudd](mailto:dmudd@fbtlaw.com); dmudd@fbtlaw.com) or any member of [Frost Brown Todd's State and Local Tax Group](#) – providing *Tax Law Defined*[™].

[i] KRS 13A.100.

[ii] See e.g., KRS 13A.100(1); KRS 13A.020–13A.350.

[iii] See e.g., [Flying J Travel Plaza v. Com.](#), 928 S.W.2d 344, 347 (Ky. 1996); [Ctr. Coll. v. Trzop](#), 127 S.W.3d 562, 566 (Ky. 2003).

[iv] See e.g., Revenue Cabinet v. Humana, Inc., 998 S.W.2d 494, 496 (Ky. Ct. App. 1998), *aff'g* No. 96-CI-00609 (Franklin Cir. Ct., Div. I 1997); Bowling v. Ky. Dep't of Corrections, 301 S.W.3d 478, 488-492 (Ky. 2010).

[v] See e.g., Charles C. Parks Co. v. Allphin et al., 295 S.W.2d 562, 565 (Ky. 1956); GTE v. Dep't of Revenue, 889 S.W.2d 788, 791 (Ky. 1994).

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