BEFORE THE
CALIFORNIA UNEMPLOYMENT INSURANCE APPEALS BOARD

In the Matter of:	PRECEDENT TAX DECISION
CALIFORNIA MARKET/ M S RHEE (Petitioner)	No. P-T-489 Case No. T-99-00071

EMPLOYMENT DEVELOPMENT DEPARTMENT

Office of Appeals No. C-T-05119

The petitioner appealed from the decision of the administrative law judge which denied its petition for reassessment. The petitioner did not appeal from that portion of the decision which concluded that the workers in question were petitioner's employees.[1]

STATEMENT OF FACTS

The petitioner filed a petition for reassessment pursuant to code section 1222 of the California Unemployment Insurance Code[2] on an assessment made by the Employment Development Department (hereinafter referred to as "EDD" or "the Department") on November 5, 1997, under code sections 1127 and 1128.

The assessment was for the period beginning October 1, 1987 and ending June 30, 1992, in the amount of $76,728.73 in contributions, $33,657.99 in California personal income tax, and $42,049.61 in penalties, plus interest. The assessment represented contributions and personal income tax, which the Department believed were due on unreported wages paid to grocery store workers employed by the petitioner. The assessment was

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[1] In its appeal, the petitioner explained that it did not contest the administrative law judge's conclusion that those individuals whose wages formed the basis of the assessment were "employees of the Western Avenue and Garden Grove locations of California Market." (Petitioner's Brief on Appeal, p. 1.)

[2] All references are to the Unemployment Insurance Code unless otherwise specified.

based on cash wages, which were paid to these workers but not reported to the Department.

The factual findings herein are based upon the testimony at the hearing, documentary evidence, testimony given at a preliminary hearing on the related criminal matter, and the declarations of employees. This evidence includes documentary and testimonial evidence concerning the petitioner's practices at both of its locations, in Los Angeles and Garden Grove.

The assessment resulted from a field audit and investigation conducted by EDD.

During the period in question, the petitioner, a sole proprietor, operated grocery stores in Los Angeles and Garden Grove, California. The petitioner hired grocery store workers whom it did not report as employees. It also paid unreported wages to certain workers whom it acknowledged were employees. The assessment included earnings of employees who worked at the petitioner's two grocery stores in Los Angeles and Garden Grove.

The petitioner paid wages by check and with cash. EDD determined that the wages paid by check were properly reported on the petitioner's contribution returns. The petitioner's records listed the amounts it paid to employees in cash and the amounts paid by check. The cash wages were not reported on the petitioner's contribution returns, the federal form W-2, Earnings Records, or on the federal form 1099, Miscellaneous Income. The petitioner withheld five percent of the workers' cash wages and did not pay over the withheld amounts to EDD.

EDD took into account the maximum taxable wage for unemployment insurance purposes for the year 1990, based on the petitioner's computation of the amount of remuneration paid to individual workers in excess of $7,000. EDD did not compute the maximum taxable wage for workers during other years, based upon the inadequacy and uncertain meaning of the petitioner's records.

Consequently, it was determined that the petitioner failed to report wages and that the petitioner intentionally evaded the payment of employment taxes. Although the petitioner filed returns for the period covered by the assessment, these returns were faulty because they failed to disclose the cash payments that the petitioner made to its employees.

The Department reached these conclusions after serving a search warrant on petitioner's premises and seizing its records.

The auditor who calculated the amount of the assessment looked through fifty boxes and reviewed, among other things, payroll records which had been prepared by the petitioner's accountant, W-2 forms, cash payment records, individual cash payment records and summaries and cancelled checks. Among the records seized were twenty-four bundles of time cards, which were designated "cash paid" for the period March 23, 1992 through August 16, l992.[3] The investigator also twice interviewed the owner and learned from him that he paid most employees by check, that he employed undocumented workers, and that he paid those workers in cash.

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[3] A document written in Korean was seized from the Garden Grove store. A purported translation of the document was introduced into the record. The document bears a heading "Payroll" and describes a number of procedures. Of note are the following comments:

"1. Semi-monthly

"...

"(2) Salaries are to be paid in check and cash ..."

"...

"(4) After computing, record only the check amounts in the Semi-Monthly Payroll Form ... and fax it to the CPA. Be careful. Do not send cash pay amounts.

"...

"(5) After faxing, record the cash paid amount and compute the total...

"(6) ... Record the total gross amount in the payroll journal, from the CPA on check coumn (sic)) . Put the total cash payments in (5) in cash (column) and get an initial from the senior president or his wife...

"(7) When receiving checks and cash from the Senior President or his wife, get their initial, and distribute them in envelopes with employee names.

"(8) When paying, put date of pay, check (gross) amount, cash amount, pay period individually...

"2. Bi-Weekly

"...

"(5) Since most people are paid in cash for overtime and weektime, only send regulars. If paid in cash, deduct 5% from the total amount."

The auditor noted that the records were similar for the approximately 250 employees of the petitioner. The auditor compared the amounts which the petitioner had paid by check and reported to EDD and the total actually paid (by check and cash). He also noted that the check stub given to the employee listed the hours for which compensation was paid by check but did not include the hours compensated with cash. The W-2's issued to these workers only reflected the wages paid by check, but did not include the amount of the additional cash wages. In addition, the forms (DE-3) submitted by the petitioner to EDD failed to report the cash wages it had given its employees.

The auditor examined a portion of the individual payroll records against summaries of wages paid and found the summaries to reflect accurately the contents of the payroll records. He used the summaries as a basis for calculating the amount of the assessment. He arrived at an annual wage for each employee and then prorated the amount over the four quarters of the calendar year. The amount assessed resulted from these estimates.

He determined that the petitioner had grossly underreported the wages paid and, consequently, had substantially underpaid payroll taxes. The total estimated unreported cash wages for the period beginning in 1987 and ending in 1992 was $2,444,882. The amounts of the annual unreported wages ranged from $124,000 in 1987 to $626,000 in 1988.

The auditor also concluded that the petitioner had engaged in fraud in this underreporting of wages. Several factors contributed to this conclusion. The petitioner kept two sets of records and only reported wages listed in one set. Furthermore, the owner, Mr. Richard Rhee, signed at least half of the DE3 forms upon which an employer must report wages paid to its employees. Also, the petitioner made deductions from the cash wages but never remitted the amounts deducted to EDD. Additionally, the petitioner withheld information concerning cash wages from its accountant and had written procedures which were designed to ensure that such wages would not be reported to taxing authorities.

The record supports these conclusions. Employees were paid both by check and in cash. The principal, Mr. Rhee, directed the bookkeeper concerning these pay arrangements. The bookkeeper did not tell the accountant about the cash wages. These wages were handled by Mr. Rhee.

The petitioner called no witnesses at the hearing. It offered no direct evidence to rebut the testimony and documentary evidence offered by the Department.

The following facts relate to the petitioner's contention that the assessment was time-barred.

On December 11, 1991, the United States Department of Labor advised an investigator in the criminal division of EDD that persons working for the petitioner had complained about its payment practices. The investigator gathered information and on or about August 20, 1992, EDD served a search warrant on the petitioner.

The investigator provided the information it gathered to criminal authorities and the petitioner's principal was criminally charged.

This investigator also shared the information gathered with the audit division of EDD. An auditor then reviewed the documents seized and ultimately used this information, together with information subsequently obtained through interviews, to prepare and serve the notice of assessment which is the subject of this appeal.

Witness interviews were conducted in September and October of 1994 and an audit report, which is undated in the body of the report, appears to have been prepared in December of 1994. According to the auditor, his investigation took approximately one year. However, the auditor did not file a notice of assessment when his investigation was complete because he was told by his colleagues in the criminal division of EDD to postpone the civil enforcement proceeding until the criminal case against the petitioner had been resolved.

The auditor was advised in 1997 that the criminal case had ended as a result of the death of the principal. The auditor understood that he could now make the notice of assessment. However, he waited four to five months after receiving this "go-ahead" before doing so.

The notice of assessment was made on November 5, 1997. It covered the period beginning October 1, 1987 and ending June 30, 1992. The notice of assessment was made approximately 5 years and 11 months after EDD first learned of complaints about the petitioner's practices and 5 years and 2 months after the petitioner's records were seized pursuant to a search warrant. The petitioner offered no evidence on the question whether the delay in the making of the notice of assessment was unreasonable or whether petitioner suffered prejudice from the delay.

We have concluded that the petitioner engaged in fraud and the intent to evade in the filing of its returns during the assessment period.

REASONS FOR DECISION

The petitioner has conceded that the wages that were the subject of the assessment were paid to acknowledged employees of the petitioner. Consequently, the petitioner was obligated to report accurately all wages paid to these workers, withhold taxes from these wages, and remit the taxed amounts to the Department.

The petitioner has contended in its appeal of the decision of the administrative law judge that the Department improperly estimated the amounts in the assessment and failed to substantiate a basis for the assessment of the fraud penalty. The remaining contentions of the petitioner concern the retroactive application of an amendment, which increased the fraud penalty to fifty percent, and the defenses of the statute of limitations and laches.

The Adequacy of the Assessment

Contributions are due the Department from employers with respect to wages paid in employment for unemployment insurance (*Unempl. Ins. Code*, sec. 976), disability insurance (*Unempl. Ins. Code*, sec. 984), employment training (*Unempl. Ins. Code*, sec. 976.6), and personal income taxes (*Unempl. Ins. Code*, sec. 13020).

If the Department is not satisfied with any return or report made by any employing unit of the amount of employer or wage earner contributions, it may compute the amount required to be paid upon the basis of facts contained in the return or reports or may make an estimate upon the basis of any information in its possession and make an assessment of the amount of the deficiency. If any part of the deficiency is due to negligence or intentional disregard of the law, a penalty of 10 percent of the amount of the deficiency shall be added to the assessment. (*Unempl. Ins. Code*, sec. 1127.)

Every employer must withhold taxes from wages paid to employees and pay the withheld taxes to the Department. (*Unempl. Ins. Code*, secs. 13020 & 13021.) The employer is liable for the payment of the tax that is required to be deducted and withheld under code section 13020. (*Unempl. Ins. Code*, sec. 13070.)

The Legislature bestowed on the Department the powers and duties necessary to administer the reporting, collection, and enforcement of taxes required to be withheld by employers. (*Unempl. Ins. Code*, sec. 13000.)

The petitioner has the burden of proof in a tax matter. (*Isenberg* v. *Calif. Employment Stabilization Comm.* (1947) 30 Cal.2d 34; *Aladdin Oil Company* v. *Perluss* (1964) 230 Cal.App.2d 603; *Smith* v. *Department of Employment* (1976) 62 Cal.App.3d 206.)

The amount of the assessment was based on estimates taken from summaries of wages paid. These estimates were made pursuant to the authority of code section 1127. Code section 1127 expressly permitted the use of estimates here because the Department was not satisfied with the returns made by the petitioner.

Precedent Tax Decision P-T-74 was decided before code section 1127 was amended. However, even prior to the amendment, the California Unemployment Insurance Appeals Board (hereinafter referred to as "Appeals Board") acknowledged that similar laws expressly gave "the tax administrators a rather broad power to resort to estimation in assessing a taxpayer who has been derelict in his duty to report information essential to the tax computation." (*Precedent Tax Decision* P-T-74.) When code section 1127 was subsequently amended, express authorization was granted to the Department in circumstances such as those arising in this case.

The auditor who calculated the amounts of the assessment made an extensive review of the petitioner's records and interviewed a number of people before reaching the conclusion that the petitioner grossly under-reported wages and underpaid taxes. His calculations were based upon payroll records and summaries. The evidence supports these conclusions and calculations. The petitioner failed to show that the Department's estimates and calculations were incorrect. We therefore find that the amounts assessed may not be reduced or stricken.

The Propriety of the Penalties Imposed

If the Department is not satisfied with any return or report made by any employing unit of the amount of employer or wage earner contributions, it may compute the amount required to be paid upon the basis of facts contained in the return or reports, or may make an estimate upon the basis of any information in its possession and make an assessment of the amount of the deficiency. If any part of the deficiency is due to negligence or intentional disregard of the law, a penalty of 10 percent of the amount of the deficiency shall be added to the assessment. (*Unempl. Ins. Code*, sec. 1127.)

Section 13020 of the code requires that employers withhold personal income taxes from the wages of employees. Under section 13050, an employer who has withheld such taxes must furnish each employee with a W2 Form and must file a duplicate of that form with the Department. Section 13052 provides that if an employer furnishes a false statement, or fails to furnish a statement in the manner, at the time and showing the information required, the employer is subject to a penalty of $50 for each such failure, unless the failure is due to reasonable cause.

If the failure of the employing unit to file a return or report within the time required or if any part of the deficiency for which an assessment is made is due to fraud or an intent to evade the law, a penalty of 50 percent of the amount of contributions assessed shall be added to the assessment. This penalty is in addition to penalties provided pursuant to sections 1126 and 1127. (*Unempl. Ins. Code*, sec. 1128(a).)

Penalties cannot be waived in the absence of a statutory good cause or other exculpatory provision. Where there is no exculpatory provision, liability for a penalty stands or falls with the liability for the contribution itself. (*Precedent Tax Decision* P-T-105.)

The amount of each assessment shall bear interest from the time that the contributions should have been paid until they are actually paid. (*Unempl. Ins. Code*, sec. 1129.)

The petitioner kept two sets of books, selectively disclosed portions of wages to its accountant and paid cash wages without providing the employee with written verification of the payment. Its own records revealed that the petitioner willfully underreported wages and, consequently, underpaid taxes. As the petitioner's conduct showed an intent to evade and willful misrepresentation, the deficiency assessed resulted from the petitioner's intentional disregard of the law. The ten percent penalty under code section 1127 was therefore properly imposed.

Furthermore, the Department offered ample evidence to support the penalty under code section 1128. The petitioner did little to rebut this evidence and waived its right to put on a case. We conclude from this evidence that the petitioner was aware of its obligation to pay taxes, and that its failure to do so evidenced fraudulent intent. The Department therefore met its burden of proof on the question whether the petitioner engaged in fraud or intended to evade its obligations under the statute. (See, e.g. *Marchica* v. *State Bd. of Equalization* (1951) 107 Cal.App.2d 501, 508-510.)

The Retroactive Application of the Amendment to Code Section 1128, Which Increased the Penalty to 50 Percent

The penalty under code section 1128 was increased by amendment in 1990. When code section 1128 was amended, effective January 1, 1991, it raised the penalty from 25 percent to 50 percent. The amendment to code section 1128 did not expressly provide retroactive application; it was silent on the question. The petitioner has argued that such amendment should not apply to any portion of the assessment occurring before 1991. We agree.

A portion of the deficiency in the assessment occurred before the 50 percent penalty in code section 1128 became effective. The administrative law judge concluded that the 50 percent penalty was appropriately applied to the entire assessment because the amendment to code section 1128, which increased the penalty to 50 percent, took effect before the assessment was made.

It is a "widely recognized legal principle ... that in the absence of a clear legislative intent to the contrary statutory enactments apply prospectively." (*Evangelatos* v. *Superior Court* (1988) 44 Cal.3d 1188, 1193-4.) This rule applies equally to an amendment of a statute. (*Cole* v. *Fair Oaks Fire Protection District* (1987) 43 Cal.3d 148, 153.)

If the enactment affected a substantive right, no retroactive application may be given. (*Coast Bank* v. *Holmes* (1971) 19 Cal.App.3d 581, 594; *Aetna Casualty & Surety Co.* v. *Industrial Accident Commission* (1947 30 Cal.2d 388, 392.)

The question here is whether the increased amount of the penalty affected a substantive right which existed prior to the enactment of the amendment.

The Appeals Board considered a similar question in Precedent Benefit Decision P-B-436. In that case, a claimant made a false statement before the enactment of code section 1375.1 (which imposed a 30 percent penalty on overpayments resulting from a false statement), but before the issuance of a determination and notice of overpayment by the Department. The Appeals Board set aside the penalty because the issuance of the Department determination was the only event which occurred after the effective date of the new statute.

The same reasoning is applied here. The increase in the penalty was a substantive amendment which affected the petitioner's obligations and the only event occurring after the effective date of the new penalty was the issuance of the notice of assessment. We therefore conclude that the amendment to code section 1128 may not be applied retrospectively. Consequently, the 25 percent penalty is imposed on the deficiency assessed for the period beginning October 1, 1987 and ending December 31, 1990. The 50 percent penalty was appropriately added to that portion of the assessment occurring after December 31, 1990.

The Time Within Which the Department Was Required to Act Under Code Section 1132

The petitioner has argued to the administrative law judge and in its appeal to the Appeals Board that the notice of assessment was time-barred. We disagree for the reasons set forth below.

Section 1132 of the Unemployment Insurance Code provides:

> "*Except in the case of failure without good cause to file a return or report, fraud or intent to evade any provision of this division or authorized regulations*, every notice of assessment shall be made within three years after the last day of the month following the close of the calendar quarter during which the contribution liability included in the assessment accrued or within three years after the deficient return or report is filed, or was due, whichever period expires the later. An employing unit may waive this limitation period or may consent to its extension.
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> In case of failure without good cause to file a return or report, every notice of assessment shall be made within eight years after the last day of the month following the close of the calendar quarter during which the contribution liability included in the assessment accrued. An employing unit may waive this limitation period or may consent to its extension." (Emphasis added.)

The question is whether the notice of assessment was made beyond the period provided in this statute of limitations.

The notice of assessment was made more than three years after the returns were filed or due. We must decide whether EDD was required to act within the three years described in the first paragraph of code section 1132.[4]

The statute created an exception to the three-year limitation "in the case of ... fraud or intent to evade any provision of this division or authorized regulations." (*Unempl. Ins. Code*, sec. 1132.) And we have concluded that the petitioner engaged in fraud or intentional evasion in the filing of its returns. The code section does not specify any time limitation which must be applied in such circumstances. What time limit existed, if any?

[4] Under the facts of this case, the eight-year statute of limitations in paragraph two of section 1132 does not apply, as the petitioner did not fail without good case to file a return.

The California Supreme Court has held that there is no time limit. In *Evelyn* v. *Calif. Employment Stabilization Commission* (1957) 48 Cal.2d 588, the court considered whether to apply an amendment to a former version of code section 1132 where a taxpayer had failed to file a return. It interpreted the following language: " 'Except in the case of failure without good cause to file a return, fraud or intent to evade this act or the authorized rules and regulations, every notice of assessment shall be made within three years.' " (*Id*. at p. 591.) In reaching its conclusion, the court stated that "there is no limitation on assessments for those delinquencies due, among other things, to a 'failure without good cause to file a return.' " (*Id*.)

In addition, the history of code section 1132 demonstrates a legislative understanding that no time limits whatsoever were to be imposed upon the Department under the circumstances referred to in each version of this code section.

When the Unemployment Insurance Act became law in 1935, it carried no time limitations. (*Calif. Employment Stabilization Commission* v. *Payne* (1947) 31 Cal.2d 210, 213.) In 1939, an amendment to the predecessor statute to code section 1132 provided that " 'no statute of this state shall limit the time within which the commissioner may enforce the payment of contributions...' " if no return had been filed. (*Id*.) By this amendment, "the three-year limitation contained in section 338 [of the Code of Civil Procedure] was rendered inapplicable, and the commission was given the right without limit as to time to enforce contributions where no return had been filed." (*Id*. at p. 215.) In 1943, the right of the Department to act without time limitation was narrowed. A three-year statute of limitations was created, with an exception where there was intent to evade the act. (*Id*. at p. 215.) Two years later, the provision was again amended. The version adopted in 1945 was very similar to the existing statute. ["Except in the case of failure without good cause to file a return, fraud or intent to evade this act or the authorized rules and regulations, every notice of assessment shall be made within three years."] (*Evelyn* v. *Calif. Employment Stabilization Commission*, *supra*, 48 Cal.2d at p. 591.) In that case, the 1945 version was held to allow the Department to act without time limitation where there was a failure without good cause to file a return. The same holding would clearly have been made where there was fraud or intent to evade the act.

The legislative history referred to above supports the conclusion that the Department was authorized to make an assessment without regard to statutory time limitations in circumstances such as those present here, where the taxpayer filed fraudulent returns and intended to evade its responsibilities under the code.[5]

This conclusion is buttressed by analogy to a similar state statute.

The Revenue and Taxation Code section 6487, which relates to sales and use taxes, uses language similar to that found in code section 1132. It provides, in part: "(a) For taxpayers filing returns on other than an annual basis, *except in the case of fraud, intent to evade this part or authorized rules and regulations*, or failure to make a return, every notice of deficiency determination shall be mailed within three years ..." (Emphasis added.) This code section is entitled "Notice of deficiency determination; statute of limitations; exceptions."

In *Marchica* v. *State Bd. of Equalization*, *supra*, 107 Cal.App.2d 501, the question was whether the notice of deficiency determination was barred by the statute of limitations in Revenue and Taxation Code section 6487. The court held that it was not. This decision stands for the proposition that Revenue and Taxation Code section 6487 requires the taxing agency to make its determination within the statutory time limits of the statute, " 'except in the case of fraud, intent to evade this part or authorized rules and regulations'; *for these cases, there is no limitation period*." (*Witkin, Summary of California Law, 9th Edition, Taxation, section 318, emphasis added.*)

The conclusion we have reached here is also strengthened by reference to federal law.

The federal courts have sanctioned lengthy delays in the collection of taxes under circumstances very similar to those present in this case. Internal Revenue Code section 6501 and the cases which have interpreted this federal statute articulate the longstanding principle under federal law that a governmental taxing agency may collect taxes from those who have filed fraudulent returns (or who have had the intent to evade the applicable taxing statutes) without regard to time limitations. Section 6501 contains exceptions

[5] Because we have decided that code section 1132 excepts from the statute of limitations assessments that are based upon the fraud or deceit of the taxpayer, we need not decide when the fraud was discovered.

to its statute of limitations. Subdivision (c)(1) provides that a tax may be assessed "at any time" in the case of a false or fraudulent return.[6] We recognize that this explicit language is absent in code section 1132. The federal statute is nevertheless a useful model and the federal case law interpreting this statute provides examples of delays in governmental action which have been countenanced by the courts.

In *Considine* v. *United States*, 683 F.2d 1285 (9th Cir. 1982), the Internal Revenue Service (hereinafter referred to as "IRS") issued notices of deficiency pursuant to Internal Revenue Code section 6501 almost ten years after the period covered by the taxpayer's returns. In that case, a related criminal case had been brought to conviction and the appeals of that conviction had become final before the IRS sent its deficiency notice. The court observed: "There is no statute of limitations 'in the case of a false or fraudulent return with intent to evade tax.' I.R.C. Sec. 6501(c)(1). Our conclusion that there was intent to evade tax for purposes of the civil fraud penalty also invokes this exception to the statute of limitations." (*Id*. at p. 1288.)

In the case of *Badaracco* v. *Commissioner of Internal Revenue*, 464 U.S. 386 (1984), more than ten years elapsed between the date of the returns and the issuance of a notice of deficiency by the IRS. The United States Supreme Court observed that where there is fraud or intent to evade, "the Commissioner is allowed an unlimited period within which to assess tax." (*Id*. at p. 392.) And, "[u]nder every general income tax statute since 1918, the filing of a false or fraudulent return has *indefinitely* extended the period of limitations for assessment of tax." (*Id*. at p. 393, emphasis added.)

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[6] Internal Revenue Code section 6501 proscribes limitations on tax assessment and collection. Subdivision (c) lists exceptions to these limitations, as follows:

> "(1) False return. In case of a false or fraudulent return with the intent to evade tax, the tax may be assessed, or a proceeding in court for collection of such tax may be begun without assessment, at any time.
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> (2) Willful attempt to evade tax. In case of a willful attempt in any manner to defeat or evade tax imposed by this title ... the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time."

The court observed that a taxpayer who had acted fraudulently was not in a position to complain about a delay ("A taxpayer who has been the subject of a tax fraud investigation is not likely to be surprised when a notice of deficiency arrives.") (*Id*. at p. 400.)[7]

Based upon the above, this Appeals Board is persuaded that there is no statutory time limit for the Employment Development Department's making of an assessment where the taxpayer is found to have engaged in fraud or the intent to evade its responsibilities under the code. As the petitioner has been found to have engaged in fraud and evasion, the exceptions to code section 1132 signify that the Department was not required to make the assessment within a statutory time limit.

While we recognize that this result may appear harsh to the taxpayer, we nevertheless find that it is dictated by law. A different result must come through legislative action.

In a recent precedent decision of the Appeals Board, a statute of limitations in the Code of Civil Procedure was applied to cut off notices of overpayment made by the Department. We conclude in this case, however, that the Code of Civil Procedure does not apply.

In the Precedent Disability Decision P-D-487, the notices issued by the Employment Development Department were based upon the allegedly fraudulent claims of persons seeking disability insurance benefits. The Appeals Board concluded that the notices, which were issued more than three years after the Department discovered the fraud, were barred by the three-year statute of limitations in section 338(d) of the Code of Civil Procedure. However, we are not bound by this prior decision because the statute of limitations in code section 1132 is governed by principles which are unique to tax law. (*See, e.g*. *People* v. *West* (1950) 35 Cal.2d 80, 87.) Also, we have reconsidered the rationale applied in Precedent Disability Decision P-D-487 and disapprove it.

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[7] A House Subcommittee report on a proposed version of I.R.C. section 6501 which was adopted in 1939 provided the opinion that " 'It is not believed that taxpayers who are so negligent as to leave out of their returns items of such magnitude should be accorded the privilege of pleading the bar of the statute." (*Colony, Inc*. v. *Commissioner of Internal Revenue* (1958) 357 U.S. 28, 34.)

The direct application of the Code of Civil Procedure to actions of administrative agencies has been viewed with disfavor. (Bold v. *Board of Med. Examiners* (1933) 133 C.A. 23, 25; *Bernd* v. *Eu* (1979) 100 Cal.App.3d 511, 516; *Lam* v. *Bureau of Sec. & Investigative Services* (1995) 34 C.A.4th 29, 37; *Little Co*. v. *Belshe* (1997) 53 Cal.App.4th 325, 329; *Robert F. Kennedy Medical Center* v. *Dept. of Health Services* (1998) 61 Cal.App.4th 1357, 1361; see also *Witkin, Cal.Proc., Actions, sec. 405, pp. 509-510*.) In light of the above authorities, we conclude that Code of Civil Procedure section 338(d) was the wrong yardstick to apply directly to the facts of this prior precedent decision.

We therefore disapprove that portion of P-D-487 which held that Code of Civil Procedure section 338(d) applied directly to the actions of the Employment Development Department.

However, we do not find that the result in P-D-487 should have been different. We hold that the actions of EDD in making such notices were not controlled by the provisions of section 338(d) of the Code of Civil Procedure.[8]

Finally, the petitioner has raised the argument in this case that the assessment is time-barred under the equitable principle of laches. This defense may not be asserted because the petitioner did not put on any evidence whatsoever on the issue of the delay in making the assessment or any resulting prejudice to the petitioner.

Laches is an affirmative defense. (*Green* v. *Bd. of Dental Examiners* (1996) 47 Cal.App.4tl 786, 792; *Miller* v. *Eisenhower Medical Center* (1980) 27 Cal.3d 614, 624.) Generally, the party complaining of the delay has a burden

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[8] We note that EDD did not argue that the statute of limitations in Code of Civil Procedure should not apply and that the defense of laches was not addressed by the parties. Therefore, the Department's delay in issuing the notices of overpayment may have been barred by laches.

Under the defense of laches, the three-year limitations period might have been borrowed from the Code of Civil Procedure "as a measure of the outer limit of reasonable delay." (*Brown* v. *State Personnel Bd*. (1985) 166 Cal.App.3d 1151, 1159-1160; see also *Fountain Valley* v. *Director* (1990) 75 Cal.App.4th 316; 11, *Witkin, Sum. Cal. Law, Equity*, sec. 14; but see *Fahmy* v. *Medical Board* (1995) 38 Cal.App.4th 810 and *Lam* v. *Bureau of Security and Investigative Services*, *supra*, 34 Cal.App.4th 29.)

of proof and must establish both that there was an unreasonable delay and prejudice to the party suffering from the delay. (*Id*.; *Robert F. Kennedy Medical Center* v. *Department of Health Services*, *supra*, at p. 1362.) In the present case, the petitioner did not produce evidence or prove that there was an unreasonable delay or that the delay resulted in prejudice. Also, those seeking this equitable defense cannot recover unless they have done equity themselves. (11 *Witkin, Summ. Cal. Law, Equity*, sec. 6; " '[H]e who comes into equity must come with clean hands.' " *Murillo* v. *Rite Stuff Foods, Inc*. (1998) 65 Cal.App.4th 833, 844.) It cannot be said that the petitioner, who submitted fraudulent returns, may avail itself of the equitable defense of laches. For the above-stated reasons, it is found that the petitioner's claim of laches cannot be sustained.

Accordingly, we conclude that the assessment was not time-barred.

DECISION

The decision of the administrative law judge is affirmed in part and modified in part. The decision is affirmed in all respects except for those portions of the decision applying the 50 percent penalty under code section 1128 to conduct of the petitioner occurring before January 1, 1991. The petition for reassessment is denied in part and granted in part. The penalty which is added to the assessment for the period beginning October 1, 1987 and ending December 31, 1990 is reduced to 25 percent. The petition is denied in all other respects.

Sacramento, California, January 18, 2001.

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