the dam, to be administered by the Secretary of Agricultural as a recreational river."

NATIONAL WILDLIFE FEDERATION,
Washington, DC, September 23, 1991.

Hon. Bill Bradley,
Chairman, Subcommittee on Water and Power, Committee on Energy and Natural Resources, U.S. Senate, Washington, DC.

DEAR SENATOR BRADLEY: With your permission, I would like to submit for the record the following information to supplement my testimony before the Subcommittee of Thursday, September 12, 1991, regarding Reclamation program reforms contained in H.R. 429.

In my testimony I called the Subcommittee's attention to the fact that there has been negative amortization of the repayment for irrigation features of the California Central Valley Project (CVP). According to the Bureau of Reclamation's Regional Office in Sacramento, the cumulative net repayment for CVP costs allocated to irrigation at the end of each fiscal year since 1985 has been as follows:

Fiscal year	*Annual (deficit)/gain*	*Net repayment (yr. end)*
1985	(8,863,000)	$38,060,000
1986	(11,987,000)	26,073,000
1987	3,743,000	29,816,000
1988	(8,541,000)	21,275,000
1989	(2,497,000)	18,778,000
1990	(7,388,000)	11,390,000

The reason given for this precipitous downward trend is that CVP irrigation operations and maintenance costs are now annually approaching $30-35 million, water deliveries are down, and most contracts are at a fixed rate that does not even recover the project's O&M costs, let alone any capital costs. Thus, for a project begun during the New Deal, with approximately $1.1 billion of Federal funds already spent on irrigation facilities, the total net capital repayment at the end of FY 1990 was $11,390,000. The Bureau's current plan does not envision recovery of CVP capital costs for irrigation until the year 2030—nearly another 40 years. As I noted in the testimony, because irrigation repayment is without interest, the present value of the scheduled repayment is only a penny or two on the dollar. The first appropriations for the project were made in FY 1936.

The Bureau told us they expected another deficit this year, but the final FY 1991 numbers have not yet been put together. So far 12 CVP contracts have been renewed and require cost of service rates that at least cover O&M, but these only represent a tiny fraction. Our understanding is that most CVP-served districts are incurring O&M deficits.

It is apparent that contract rates for most irrigation water in California—rates available to those who qualify under the acreage limitation rules of the RRA—severely disadvantage the Federal Government. We believe that the dismal financial condition of the CVP, against the general backdrop of the Federal budget deficit, underscores the need to narrowly target the irrigation subsidies to those farm operations where some demonstrable, legitimate social objective would be served by the continued availability of very low cost irrigation water.

Sincerely,

EDWARD R. OSANN,
Director, Water Resources Program.

Senator BRADLEY. Thank you very much, Mr. Osann.
Mr. Villarejo.

STATEMENT OF DON VILLAREJO, EXECUTIVE DIRECTOR, CALIFORNIA INSTITUTE FOR RURAL STUDIES, DAVIS, CA

Mr. VALLAREJO. My name is Don Villarejo, and I am executive director of the California Institute for Rural Studies, a private, nonprofit, research and education organization with offices in Davis, Modesto, and Berkeley, California.

The central issue before this committee is whether or not you are prepared to close the loopholes. The Federal reclamation program was intended to provide a limited amount of subsidized water to resident family farmers, and to ensure that the benefits of this program be as widely shared as possible. By setting firm limits on the amount of federally subsidized water that any one farm could receive, the program sought to prevent monopoly of a public resource and to prevent speculation in land values enhanced by that public resource.

The original 160-acre ownership limitation failed to meet this objective because it permitted unlimited leasing. The 1982 Reclamation Reform Act was designed to set a cap, finally, on the amount of land that could receive subsidized water. It is our view that neither S. 1501 nor H.R. 429 accomplishes that purpose.

The General Accounting Office, has found various instances in which large-scale farms have continued to operate, but for reclamation purposes have been permitted to divide up the landholdings into units of 960 acres or less. For example, nearly 3 years ago, GAO reported that:

> Our work identified one 12,000-acre farm that was divided into 15 separate landholdings, all but one of which was less than 960 acres.
>
> The 15 landholdings, however, continued to be operated as one large farm. This reorganization has allowed the farm to receive subsidized water on most of the 12,000 acres, and it reduced by $500,000 per year the cost of water that they had to pay.

Subsequent reports have found that abuses are even more widespread. A full accounting of the extent of the annual improper subsidies has, in my view, yet to be made.

Both bills, H.R. 429 and S. 1501, fail to recognize that the largest farm businesses have devised a relatively simple and clever scheme to retain control of very large tracts of land and continue receiving federally subsidized water. The heart of the scheme is the use of farm management or custom farming businesses to manage two or more legal entities who are each entitled to receive federally subsidized water, as we have documented in several of our publications.

And I will submit for the record a copy of *Missed Opportunities—Squandered Resources,*[1] coauthored by myself and Judith Redmond, who is a family farmer working right now this day in California where she lives.

In that document, on page 35, we outline a case of Perez Ranches that operates a total of 7,340 acres in the Westlands Water District, and does so through a number of entities, 10 in all, that have names such as FB.A, with 862 acres in the landholding; FB.B, with 923 acres in the landholding; FB.D, with 940 acres in the landholding; FB.E, with 898 acres in the landholding; FB.F, with 656 acres in the landholding, and I think you get the general idea, except the lack of imagination in naming the farms.

The 10 entities altogether, as I pointed out, have a total of 7,340 acres of irrigated land. But when they go to ASCS to qualify for program payments under USDA, they register the entire farm, including more land outside of the Westlands Water District, as a single entity. And when they go to get their pesticide permit from

---

[1] The document appears in the Appendix of this document.

the county agricultural commissioner, as all farms in California are now required to do, they again register as a single entity.

Clearly, what is going on is that they have used their original farm business, Perez Ranches, to manage the operation, and they have admitted this in interviews in public television. With respect to the landholding, however, they have complied with the regulations and rules promulgated by the Bureau. And in my view, those regulations and rules are, plainly speaking, inadequate.

In particular, the language suggested in both S. 1501 and H.R. 429 would embody in law the language used in the rules and regulations in 1987. And that is the direct risk of loss in the crop is the only test of the relationship of the custom farming or farm management business with respect to the landholding entities.

It is of interest to me, and I think to this committee, that the original language proposed in November of 1986, four of these proposed rules and regulations to implement the 1982 Reclamation Reform Act said, "person or entity performing the custom farming has no interest, directly or indirectly, in the crop on the farm." If that "indirect" wording had been retained, then the kinds of operations that we are talking about could not continue to receive unlimited water subsidies.

In closing, then, it seems to me that what we have to do is, following Phil Doe, adopt a very clear and simple test. In my view, that test is 960 acres for a single operation—you can continue to farm more land if you want to, you can even get water and pay full cost for it, if you want to. But with respect to subsidized water, let us set the line where it belongs, 960 acres. Thank you.

[The prepared statement of Mr. Villarejo follows:]

PREPARED STATEMENT OF DON VILLAREJO, EXECUTIVE DIRECTOR, CALIFORNIA INSTITUTE FOR RURAL STUDIES, DAVIS, CA

My name is Don Villarejo and I am Executive Director of the California Institute for Rural Studies, a non-profit research and education organization with offices in Davis, Modesto and Berkeley, California. We have conducted research on the issue of proper enforcement of the acreage limitation provisions of reclamation law for more than 15 years. Most recently, this work has been supported by major grants from the Ford Foundation and the Shalan Foundation. We are indebted to the J.R. Fund for providing travel funds to make it possible for me to speak here today.

The central issue before this committee is whether or not you are prepared to close the loopholes. The federal reclamation program was intended to provide subsidized water to resident family farmers and to insure that the benefits of this program be as widely shared as possible. By setting firm limits on the amount of federally supplied water that any one farm could receive, the program sought to prevent monopoly of a public resource and to prevent speculation in land values enhanced by that public resource.

There can be no doubt that Congress has always, from the inception of the reclamation program, sought to limit the benefits that a single user could receive from the delivery of federally subsidized water. There is also no question that large-scale farm businesses have successfully found ways to get around the law and to frustrate the intent of Congress. The recent GAO report ably documents the latest abuses of the largest farm businesses in the United States in capturing the benefits of the reclamation program.

GAO has found numerous instances in which large-scale farms have continued to operate but, for reclamations purposes, have been permitted to divide up the landholdings into units of 960 acres or less. For example, nearly three years ago GAO reported that

> . . . our work identified one 12,000-acre farm that was divided into 15 separate landholdings, all but 1 of less than 960 acres. The 15 landholdings, however, continue to be operated as one large farm. This reorganization has

> allowed the farm to receive subsidized water on most of the 12,00 acres, and it reduced by about $500,000 the cost of the water received in 1987.[1]

Subsequent reports have found that the abuses are even more widespread. A full accounting of the extent of the annual improper subsidies has yet to be made.

Neither S. 1501 and H.R. 429 make any significant progress in correcting these abuses. Both bills fail to recognize that the largest farm businesses have devised a relatively simple and clever scheme to retain control of very large tracts of land and continue receiving federally subsidized water. The heart of the scheme is the use of farm management or custom farming businesses to manage two or more legal entities who are each entitled to receive federally subsidized water, as we have documented in several of our publications.[2]

Both S. 1501 and H.R. 429 permit custom farming or farm management relationships for multiple entities whose combined holdings would otherwise not qualify them for fully subsidized water if

> . . . the custom farmer or farm manager does not bear a *direct risk* of loss in the crop.[3]

What we have found, however, is that indirect relationships are being used to mask the manner in which direct control of the land is being maintained.

Let me illustrate this use of "indirect" relationships to get around the law. Suppose that prior to 1985 ten individuals jointly owned a farming corporation, which I will call Farm A, and which placed its own capital at risk on 9,600 acres of federally irrigated land. After implementation of the Reclamation Reform Act, these same individuals continue to own shares of Farm A and, as well, became individual beneficiaries of ten trusts that each own 960 acres of land. By entering into a farm management agreement to "manage" all of the properties together, Farm A takes no direct risk in the crop production, thus complying with current federal law and with the proposed language of the two bills. Farm A has now become a farm management company and manages the ten "farms" owned by these same ten people. But Farm A no longer directly places its own capital at risk; the trusts now take the direct risk. But this new indirect relationship means that the same crops are being grown on the same land as before, and it is very likely that even the same equipment is being used.

Interior itself saw the possibility of this type of relationship. It originally proposed that custom farming would be considered a lease for reclamation purposes if the

> . . . person or entity performing the custom farming has no interest, directly or indirectly in the crop on the farm . . .[4]

Final regulations published by the Bureau deleted the crucial words ". . . or indirectly . . ." and opened the loophole.

This use of the terms "directly or indirectly" gets to the main point of this hearing. If indirect relationships are to be permitted then, in effect, you will be saying that anything goes, that you care little about correcting the abuses which GAO and others have found.

A final concern that I have is the use of trusts as a mechanism to attribute a portion of a large landholding to an individual beneficiary. The most notorious such case involves the Westhaven Trust, a 23,000 landholding formerly owned by the Boston Ranch Company, subsidiary of the J.G. Boswell Co. and located within the Westlands Water District in California's San Joaquin Valley. The beneficiaries of this newly created trust are certain employees of the J.G. Boswell Co. And guess who has been "selected" to "manage" this new trust's landholding: none other than the Boston Ranch Co., the original owner.

By allowing the attributed share of each beneficiary's holding to represent an independent interest, the Department of the Interior has done a great disservice to the very concept of acreage limitation. How is this any different than assigning to each stockholder of a giant corporation a portion of the corporate assets that is proportional to their stockholding? By this reasoning there are no giant corporations; we are instead a nation of mere small holders. The use of trusts as essentially private corporations to mask the reality of large holdings emasculates the law.

---

[1] United States General Accounting Office, *Interior Issues, GAO/OCG-89-24TR, November 1988.*

[2] For instance, see D. Villarejo and J. Redmond, *Missed Opportunities—Squandered Resources,* California Institute for Rural Studies, 1988, pp. 25ff.

[3] See S. 1501, Sec. 1702(B)(v).

[4] "Rules and Regulations for Projects Governed by Federal Reclamation Law," Sec. 426.7, *Federal Register* Vol. 51, No. 216, November 7, 1986, p. 40756

The proposed language of S. 1501 would permit up to 25 such individual attributions from a single trust holding, in other words, as much as 24,000 acres in a single landholding. As I have indicated, a single farm management company could then "manage" this property and thereby accrue more than $1,000,000 in annual water subsidies. This is not what Congress has intended.

Senator BRADLEY. Thank you very much, Mr. Villarejo.

Senator Burns, do you have any questions?

Senator BURNS. I have a couple. Correct me if I am wrong, Mr. Candee, but the lawsuit in California did not abrogate the reclamation law, did it?

Mr. CANDEE. Did not what?

Senator BURNS. It did not abrogate that law, or set that law aside? That lawsuit only said that you had to perform an EIS, is that correct?

Mr. CANDEE. That is correct.

Senator BURNS. So your statement in here is not correct.

Mr. CANDEE. No, it is correct. The court said that the rules are now hypothetical, because they were entered into without observance of the procedures required.

Senator BURNS. But not the acreage.

Mr. CANDEE. Not the limits.

Senator BURNS. Not the acreage——

Mr. CANDEE. No, the law is still intact. It is the regulations that were entered into illegally.

Senator BURNS. Okay, let us make—there is a distinction there. Do you farm, Mr. Villarejo?

Mr. VALLAREJO. Do I personally farm at this time?

Senator BURNS. Yes.

Mr. VALLAREJO. No.

Senator BURNS. What is your interest in this, then?

Mr. VALLAREJO. What is my interest in this? I represent a private, nonprofit, research, education and community organizing organization in California. Our board of directors include several family farmers. The co-author of the document I am submitting for the record is a family farmer herself in California, and is an advocate on the same issue.

Senator BURNS. When you say, when you say a manager of a farm or a farmer that goes in and he hires a manager, directly or indirectly participates in the money that is made on that farm, how do you distinguish the two whenever it does not make any difference, his income is going to be based primarily upon the production of the farm, is that correct?

Mr. VALLAREJO. Absolutely.

Senator BURNS. So directly or indirectly has nothing to do with it.

Mr. VALLAREJO. Not at all. As a matter of fact, the whole point of the Perez Ranches' scheme that I outlined to you is that Perez Ranches, as a farm manager, has no direct risk of loss in the crop. For a fee, they farm the ground, and the individual landholding entities are, for reclamation purposes, each qualifying with the 960-acre limit.

The point is that those landholding entities are separate, legal entities without any direct relationship.

Senator BURNS. Okay, that is—now, we go back to this, this drought in California is devastating. And we have been through droughts in Montana; we have all been through droughts. And I think in California, where you have a State with quite a few people, and I think there is an old saying that this old earth and this old land, given what it will produce, will only carry so much livestock, and man happens to be part of that livestock.

And it all starts in the soil. If you would have had no irrigation projects at all in California, Mr. Candee, if there had been no CVP, if there had been no irrigation farming in the San Joaquin Valley—and it was farmed dry land for many years, because it used to be one of the major wheat-producing areas in the country years ago—what would your environment be like now?

Mr. CANDEE. I do not know the exact answer to that, but my guess is that a 5-year drought would be pretty devastating. Of course, nobody is advocating shutting down any projects. I mean, that is not the idea. The idea here is to have some sort of balance. The San Joaquin River, you know, the Friant Dam, diverts 99 percent of the water out of the stream.

All we are talking is maybe putting 5 percent back, or 10 percent. You know, keep the rest in agriculture, give them the money it takes to improve their irrigation systems to the highest level of efficiency, do whatever it takes to protect those farming communities. But just put a little bit of the water back so the fish do not die.

I mean, right now there is a stretch of the San Joaquin that is dry, you know, has been dry for 5 years certain times of the year. So you cannot maintain any fish in that kind of situation. So you are absolutely right, you know, that you can manage the projects in a way that is better for the environment.

Senator BURNS. Okay, now, given that, and we know that the demand on the water, and nobody fishes more than I do, or hunts, or likes—I work in the sportsman's caucus here—sports more than I do. Given the situation, would you be supportive of some water storage projects in the mountains? To ensure stream flow and release at proper times? Would you be in favor of some new water projects in California?

Mr. CANDEE. You know, Senator, every time we talk about putting some sort of restoration project together, the first question is always, well, how about building some more dams. And, you know, I guess my answer is if you can do it in a way that improves the environment, that is better for the environment, we have no absolute prohibition in our view about building more storage.

In fact, right now I am involved in these negotiations in California where we are talking about, you know, off-stream storage and groundwater basins. There is lots of ways, using conjunctive use, a lot of farms are very interested in that idea of dry year leases, conjunctive use.

So storage is a big part of the solution. But the idea that you keep everything else static, do not make any improvements in conservation, just build another dam and then release a little bit of that water for fish, does not seem to be the smartest way to start.

Senator BURNS. Well, but your population continues to grow in California. Your municipal use is going to continue to grow.

Mr. CANDEE. That is a problem.

Senator BURNS. And you have got a demand on it. And I would say, I would say this. We are faced in Montana, we are going to talk about a grazing fee one of these days.

Now, once you bring a farm and it costs—we cannot lower the cost of a combine below $100,000; we cannot do that. So when you get a farm so small that it cannot afford even to hire custom cutters to cut it, then the only alternative that that farmer has is to subdivide his farm and try to get his money out of it, so more people can move in and the demands on water will be astronomical compared as to demands for irrigation.

What I am saying is, sometimes we do things for the environment under one guise, that basically we are destroying it. If you take the cattle off of public lands, which an increase in fees would do, and like these people will not be able to buy water, they are going to have to do something to retrieve their investment. So what are they going to do? They are going to build other things; it is going to attract more people, and people are really the polluters, are really the demand.

If it is not economical and viable, and until, if you keep these farmers in business, then you have got habitat, then you have got water. I am saying that I do not like these people who broke the laws here either, or tried to scurry it. I want to get to those people, I really do.

But sometimes we do things in the name of, to affect people, or an economic viability of a farmer ranch, because I can cite you cases in the state of Montana that we are going to lose winter elk range, we are going to lose fish habitat, we are going to devastate some environment in the state of Montana in the name of the environment. And we have got to be very cautious about that.

And I guess that is the point I am making now, that we cannot just go at it with a sledgehammer, because we have to make these farms economically viable.

Mr. VALLAREJO. On the subject of economic viability, I would propose to submit for the record the audited financial statements of the J.G. Boswell Company for 7 years in the 1980's, that shows that that company had net income after taxes in excess of $10 million a year in each of those 7 years.

Senator BRADLEY. Without objection, it will be submitted to the record.

[The information referred to is retained in subcommittee files.]

Senator BURNS. I have no objection against making money. Do you? Are you working for nothing?

Mr. VALLAREJO. I am not working for nothing, but I will tell you I have got something when I have to pay taxes to support them

Senator BURNS. Are you not a benefactor of them?

Mr. VALLAREJO. I do not see that I am.

Senator BURNS. Well, I will tell you what. You take all the water away from the west, and I want to see what you will pay for tomatoes.

Mr. CANDEE. Senator, I think even the Boswell Company is willing to pay full cost. That is all we are talking about. We are not talking about eliminating access to water, we are talking about paying, you know, reducing the subsidy.

Senator BURNS. The taxpayer is getting his money's worth, I will tell you that.

Mr. VALLAREJO. I do not agree with you on that, sir.

Senator BRADLEY. Okay, we are closing down here. I just want to ask one more question to Mr. Villarejo. We have had a lot of very good testimony today from farmers who are out there working, having legitimate problems, they are on the soil, or they are managing it for people who are in the immediate neighborhood.

What about the Pacific Agricultural Services? Could you explain what that is, and who it manages farms for?

Mr. VALLAREJO. The Pacific Agricultural Services Company operated in California for a number of years under that name. They have recently changed their name. They are a professional farm management company. Typically they manage land for people who are unable themselves, for whatever reason, to operate the farm directly, and do so for a fixed fee.

Approximately 25,000 acres, at the last point in time when I had an official report from them from Dun & Bradstreet, are currently under management by them. I do not know if that has changed recently or not.

However, I would like to add one comment with respect to this, and that is that there is a great variation in farming throughout the United States. As a matter of fact, I am sure Mr. Burns and I could agree wholeheartedly that it is very difficult to write a rule that equitably affects everyone in an equal way.

Senator BURNS. We do not have anything that big in Montana——

[Laughter.]

Mr. VALLAREJO. I know you do not.

Senator BURNS [continuing.] That is going to affect me in Montana.

Mr. VALLAREJO. I understand your problem. The issue in our view is that if you go out to the Westlands Water District, where Pacific Agricultural Services operates, and where the Boswell company operates, you have just in that water district, about 600,000 acres, 300 operations. They typically have 15 or 20 full-time employees, and dozens if not hundreds of seasonal employees.

If you go to the only incorporated city in the Westlands Water District, Huron, California, you find there are, 92 percent of the people do not have a high school diploma. The average family income is $6,000 a year. You are looking at a situation where people who are mostly Latino and who work on those farms and are doing the majority of the work on those farms are not deriving any benefit. We do not even have a junior high school or a high school in Huron.

So $700 million comes into the Westlands Water District, who is it helping? That is my question.

Senator BURNS. You build the schools.

Senator BRADLEY. So Mr. Villarejo, I take it then that your point is that $700 million in subsidies comes into the Westlands district, one operator out of that nets $10 million—did you say a year?

Mr. VALLAREJO. A year.

Senator BRADLEY. A year. And the people who live in the area do not have adequate schools and——

Mr. VALLAREJO. Do not even have an adequate school.

Senator BRADLEY [continuing]. Have an annual salary of $6,000.

Mr. VALLAREJO. That is right.

Senator BRADLEY. It sounds to me like you have found common ground with the previous panel.

Mr. VALLAREJO. I think we have.

Senator BRADLEY. And there is no absence of intent, I think, on the part of Senator Burns, based on his comments earlier, the previous panel, or you, to get at this problem. I assure you, we are going to get at this problem. Those who have tried to confuse the issue will be disappointed. This exchange, the previous panel, and both Senator Burns and my comments, have crystallized the issue.

I can assure you that the message should go out that this is not going to end until that loophole is closed, because I think of Ms. Brown, I think of Mr. Sack, I think of all those who have testified before here from reclamation projects in South Dakota, in Nebraska, in Montana, Wyoming, everywhere else, represented by senators on this committee. And I think they would be equally outraged, and I would say virtually everybody on this committee would be equally outraged.

So this is not going to end. I mean, we are going to pull back from this thing today, and we are going to take a look at this and go after it with a laser, because we are going to get it. Thank you very much.

Mr. VALLAREJO. I appreciate your commitment, sir.

Senator BRADLEY. Now, our last panel today is the GAO. Mr. James Duffus, Mr. George Senn, Mr. James Hampton. I know you gentlemen are used to testifying first or second at these hearings, but today you are testifying last, and I know that you are curious as to why. I will be quite candid with you, the reason is because I knew that if you were last, we would still have a crowd.

[Laughter.]

Senator BRADLEY. And that assumption has proven correct. And I also knew that, not a bad thing for you to sit and listen to some of the people who have testified today. So those are the two reasons, and in addition I wanted to accommodate Senator Burns' request that people who have come from far should actually be heard before people who are here every day.

But let the record note that you did get your testimony in before this morning, unlike the Bureau of Reclamation. So you are not in violation of that committee rule, but you are rather a victim of a kind of attempt to accommodate people who have come from distances. And I hope that, if this is the pattern of the committee in the future, then you will not have to sit here the whole time, we will tell you to come at such-and-such a time.

Thank you very much.

Mr. Duffus.