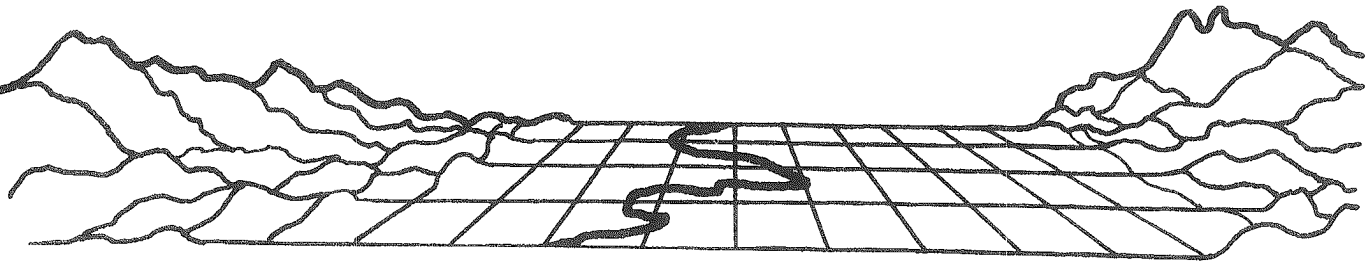

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Testimony of Dr. Don Villarejo
Subcommittee on Water and Power
Senate Energy and Natural Resources Committee
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My name is Don Villarejo and I am Executive Director of the California Institute for Rural 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

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[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).

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.

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.

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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.