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ABSTRACT

This series issue presents a description and assessment of the Agency for International Development (AID) funded endowment concept as conducted by a number of AID Missions and host governments in Latin American and the Caribbean. These endowments are being used to strengthen and sustain the financial base of existing or new non-governmental institutions, including foundations and educational institutions; or to help in transferring important development functions that are poorly performed by the public sector. Topics discussed include: the creation, funding, expansion, and management of endowments; their dissolution; and issues of concern that could hinder host governments and donors from establishing a successful endowment. These issues include institutional displacement, organizational performance, political interference, and the rapid devaluation of an endowment due to such things as currency instability, rampant inflation, and government policies. Also discussed are issues concerning financial accountability in order to protect endowment resources, and the point at which AID responsibility for monitoring and exercising control over the management and use of endowment earnings ends. Names and descriptions of eight AID-funded endowments in Costa Rica, Ecuador, Honduras, the Dominican Republic, and Portugal conclude the report. (GLR)

Innovative Development Approaches

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No. 3 ▼ December 1990

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## Summary

Since the mid-1980s, a number of A.I.D. Missions and host governments in Latin America and the Caribbean have collaborated in establishing and funding endowments. These endowments are being used to strengthen and sustain the financial base of existing or new institutions. In other instances, however, the endowment is being used to transfer important development functions, heretofore poorly performed by the public sector, to more entrepreneurial/nonbureaucratic organizational structures. These alternative structures are most typically nonprofit private foundations, or some other type of nongovernmental organization.

A.I.D.-endowed institutions and foundations are performing a range of development roles in agricultural research, natural resource management, and trade and investment promotion. As free-standing institutions with a stable financial base, these nongovernment organizations are presumed to be able to achieve greater continuity in programming, attract superior leadership and staff by offering competitive salaries, and demonstrate more creative problem-solving capacities than public sector organizations.

A.I.D. Missions have used local currency from Economic Support Funds (ESFs) and PL-480 food aid grants as the primary source for funding endowments. The new Debt-for-Development Initiative now allows dollar currency from development assistance (DA) funds and ESF to be used, through debt swaps, to fund endowments. Interest earned from these sources does not have to be returned to the U.S. Treasury and can be reinvested in the endowment or for funding development activities stipulated in the endowment agreement.

The agreements of many A.I.D. endowments stipulate that endowment funds be invested over a prescribed or indefinite period of time in host government bonds. In other instances, provisions have been negotiated for investing endowment funds in host country assets and for converting funds to foreign currencies for off shore investments. Some of the endowment agreements contain matching formulas to provide an incentive for the endowed organization to establish closer links with other funding sources.

Given the newness of A.I.D.-funded endowments it is still too early to evaluate their performance. However, based on an examination of A.I.D. design and review documents, it is apparent that Missions are cautious to avoid duplicating and displacing government institutions, to reduce the potential for organizations with guaranteed endowment income to succumb to organizational inertia, and to protect the endowment from political interference, devaluation as a consequence of economic instability, or financial improprieties in its management.


## Background

Since the mid-1980s a number of A.I.D. Missions and their host governments in the Latin American and Caribbean region have collaborated in establishing

*The purpose of Innovative Development Approaches is to identify, describe, and assess the progress of promising, experimental approaches being tried by A.I.D. and other agencies to achieve priority developmental objectives and new policy thrusts. This series communicates the key ideas behind each innovative approach to A.I.D. Missions interested in how some of their colleagues are addressing these objectives.*

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and funding endowments. The interest earned from these endowments is used to support and sustain important development activities that might not otherwise be adequately funded and supported under more conventional arrangements.

An A.I.D.-funded endowment is frequently associated with a private, nonprofit foundation or organization that uses funds earned from the endowment to carry out development projects and programs. The organization usually has a staff that plans and manages these development efforts. Some members of the staff may also be responsible for mobilizing additional funds from public and private sources to invest in expanding the endowment.

While endowments and foundations frequently go together, there are many instances in which this is not the case. In principle, any type of nonprofit, nongovernmental organization, whether it is a foundation or not, is eligible to receive A.I.D. endowment support. A.I.D. cannot endow public or private profit-making organizations; however, public-sector or profit-making organizations can initiate and benefit from the establishment of endowments. Thus, a public university could establish a private foundation with an endowment, the earnings of which could be used to support faculty research or student fellowships. Likewise, a nonprofit development corporation could use earnings from an endowment to provide venture capital or credit to private entrepreneurs.

As these examples suggest, endowments can be used with considerable imagination to support a wide variety of development activities. This fact is reflected in the emerging A.I.D. experience with endowments established to support agricultural universities in Honduras, Costa Rica, and the Dominican Republic; agricultural research in Ecuador and Honduras; trade and investment promotion in Costa Rica; and agricultural policy analysis in Ecuador. Some Missions are also contemplating using endowments to support microenterprise development. The following lists the eight A.I.D.-funded endowments currently in operation or about to begin operation. A brief summary of each of these cases can be found on pages 11-19.

1. *Costa Rica—Coalition for Development Initiatives (CINDE)*. Established in 1982, CINDE is a private, nonprofit foundation that actively engages in promoting foreign investments and agricultural exports for Costa Rica.

2. *Ecuador—Foundation for Agricultural Development (FUNDAGRO)*. Established in 1986, FUNDAGRO is designed to exercise a leadership role in agricultural research, education, and extension.

3. *Costa Rica—Cordillera Development Foundation (CDF)*. Established in 1989, CDF is intended to manage a major wildlife area and a surrounding buffer zone in the central region of Costa Rica.

4. *Honduras—Honduran Agricultural Research Foundation (FHIA)*. Negotiations for establishing an endowment to expand and to sustain the Foundation's programs are nearing completion.

5. *Ecuador—Institute for Agricultural Strategies (IDEA)*. Established in 1985, IDEA is designed to encourage greater private sector involvement in policy analysis and policymaking for the agricultural sector.

6. *Dominican Republic—Superior Institute of Agriculture (ISA)*. In 1989, ISA received an endowment to help finance its undergraduate operating and program expenses and faculty outreach and research activities.

7. *Honduras—Pan-American Agricultural School (EAP)*. In 1987, EAP (a 4-year undergraduate college) received an endowment to fund fellowships and to finance natural resource programs.

8. *Costa Rica—Agricultural College of the Humid Tropical Region (EARTH)*. In 1985, A.I.D. and the Government of Costa Rica agreed to establish EARTH and to provide it with a large endowment.

9. *Portugal—Luso-American Development Foundation*. Established in 1985, the Foundation is designed to promote scientific, educational, and cultural cooperation between Portugal and the United States.

## The Purpose of the Endowment

In some cases A.I.D. endowments are being used to strengthen and sustain the financial base of an existing or new institution. The three educational institutions listed above fall into this category: All are established private entities that must rely on their own fund raising, tuition fees, and other sources of income to support their programs. In other cases, however, endowments are much more than a financing device. They are in large measure institutional innovations used by A.I.D. and the host governments to improve, if not restructure, functions vital to the development process.

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Such a case is FUNDAGRO. Agricultural research, extension, and education in Ecuador were highly fragmented, chronically underfunded, and lacked strong leadership. A.I.D. and the Government of Ecuador believed that a new institution, unfettered by bureaucratic inertia and regulations, was needed to act as a catalyst to aggressively integrate the diverse elements of the national agricultural technology system around a well-planned, coherent research agenda. FUNDAGRO, as an autonomous entity, was established to undertake this task, and an endowment was set up with food aid funds to help ensure the foundation's institutional continuity.

CINDE also demonstrates the quest for a new institutional formula. In the past, trade- and investment-promotion programs sponsored by the Government of Costa Rica were relatively ineffective, largely because they were assigned to public agencies that operated within the confines of rigid bureaucratic norms and procedures. CINDE now performs these promotional functions, and as an independent foundation, has free rein to aggressively pursue clients and investors for trade and investment in Costa Rica.

IDEA in Ecuador is intended to mobilize greater private sector involvement to enable this sector to have a greater voice in agricultural policymaking. IDEA reaches out to the agricultural and agribusiness sectors, stimulating and facilitating the creation of coalitions that can actively and more effectively lobby for the interests of these sectors in public policy arenas. The goals of CDF in Costa Rica parallel the social mobilization role of IDEA: CDF staff, in addition to managing the wildlife areas, will be involved in organizing farm communities in agroforestry conservation practices in the surrounding buffer areas.

The common thread running through the rationale for establishing IDEA, FUNDAGRO, and similar endowments is an effort to support new kinds of organizational structures that can more effectively perform a distinctive set of development tasks. In particular, these foundations are being asked to perform tasks that require a high level of organizational entrepreneurship. For example, CINDE must aggressively seek new investors; CDF has to mobilize community forestry efforts; IDEA, FHIA, and FUNDAGRO have to exercise national leadership roles in forging public- and private-sector linkages.

Such entrepreneurial tasks require a highly motivated staff, strong leadership, and a parent organization that provides adequate resources, flexible procedures, and rapid problem-solving responses. Public sector organizations generally perform poorly in this area, largely because of the constraints inherent in their bureaucracy: low salary schedules, inadequate and erratic funding, political interference, discontinuous program priorities, and so on.

Indeed, in many of the endowment programs described above, the mandated function had originally been invested in a public sector organization, a solution that was soon demonstrated to be unworkable. The idea for a new institutional formula, the endowed nongovernmental organization, was in response to this failure. In effect, the institutional formula is to achieve a more appropriate fit between function and structure. Functions that require dynamic and innovative leadership in creating new coalitions, networks, and market responses, in turn, require the crafting of highly flexible organizational structures that can support such endeavors.

Endowed nongovernmental organizations and foundations enjoy a comparative advantage over public institutions because of their free-standing, independent status and relatively stable funding base, which should enable them to achieve greater long-term continuity in their programming. Presumably, they can also attract the most able leaders and staff because they are able to compensate them at their full market value. Finally, they have the advantage of creating an internal organizational system that allows their leadership and staff to maximize their contribution on behalf of the organization.

An endowed nongovernmental organization or foundation is a hybrid institution in that it is mandated to achieve a public purpose through quasi-private means. It falls into the category of organizations that generally stand at the interface between the public and private arena, for example, many types of nongovernment organizations, private voluntary associations, community development organizations, and public development corporations. Established by government or private initiatives, these organizations are vested with a level of autonomy and flexibility unlike any found in most public institutions, yet they are still dedicated to achieving larger public purposes. Their proliferation is an important barometer of development progress: They perform functions that neither the public nor private sector can effectively assume, thereby deepening the organizational capacity of a society to fulfill important developmental needs. In this context, the endowment should be viewed as a means of fostering organizational capacities of the host country that are important to development.

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## Establishing the Endowment

In most instances, the establishment of an A.I.D./host-government-funded endowment involves negotiating a Memorandum of Understanding (MOU) between these parties and the endowed organization, setting forth the purposes and conditions of the endowment. An MOU is a legal document to which the signatories are legally bound. Since most endowments are established for long periods, if not permanently, the conditions governing the endowment must be specified in an MOU, rather than in a project grant agreement, because the former applies to the life of the endowment, whereas, the latter expires at the end of the project.

MOUs usually stipulate the terms and purpose of the endowment, how the funds are to be managed, sources and amount of funds, conditions pursuant to the transfer of the funds to the endowed organization, the uses of the endowment income, requirements for reports and audits on the endowment and its income, and the conditions that would warrant dissolution of the endowment.

'stablishing an endowment requires detailed familiarity with host country laws and regulations. For example, the creation of an endowment may or may not require enactment of a law by the host country legislature, a process that could be quite cumbersome and time-consuming. In one country, A.I.D. and the host government were able to shorten this process by stipulating the establishment of the endowment in a project implementation letter based on the bilateral agreement between the United States and the host government, an agreement formerly approved by the legislature.

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## Funding the Endowment

Under current legislative acts and A.I.D. general counsel rulings, there are several sources that can be used to fund endowments. For purposes of this discussion, these sources are divided into three categories: development assistance (DA) funds; Economic Assistance Funds (ESF) funds; and PL-480 food aid funds. It should be mentioned that the legal basis for investing resources in an endowment is evolving in response to changes in Congressional acts, as well as in response to how creative A.I.D. and cooperating host governments are in interpreting existing rulings and guidelines.

### Development Assistance Funds

The use of DA funds to establish an endowment used to require a special legislative act by the U.S. Congress. However, under the Agency's debt-for-development initiative, as reflected in policy guidelines issued on February 15, 1989, and later updated on April 11, 1990, DA funds can be invested in endowments through debt-swap transactions without prior approval of Congress.

A second major legislative change, as reflected in the Global Environmental Protection Assistance Act of 1989 and the FY 1990 Appropriations Act, allows interest earned from debt-for-development endowments, instead of being returned to the U.S. Treasury to be reinvested in the endowment or used for funding activities authorized in the endowment agreement.

These policy and legislative changes indicate Agency support for debt-for-development initiatives and a corresponding interest in using endowments to support these initiatives. Indeed, in support of this effort, the Agency has provided a grant for the recent establishment of the Debt-for-Development Coalition, a consortium of nonprofit organizations representing U.S. universities, cooperatives, private voluntary organizations, and international agricultural research institutions. The Coalition, and its sister organization, the Debt-for-Development Foundation, assist the Coalition's member organizations in identifying and negotiating debt-swap transactions.

The debt-for-development initiative allows a nongovernmental organization to secure a DA grant from A.I.D., which in turn is used to purchase discounted debt currently owed by a developing country to a foreign creditor. This debt is then exchanged with the debtor government for local currency or other assets to finance development programs undertaken by the nongovernmental organization. Such activities can involve establishing an endowment.

Finally, it should be mentioned that, in cases where nonproject sector assistance programs have generated host-country-owned local currency, these funds can also be drawn upon indirectly to establish an endowment. In such cases, the use of DA funds must have the agreement of the host government.

### Economic Support Funds

As with DA funds, ESF dollars can also be used for debt-for-development initiatives. In addition, host-country-owned ESF-generated local currency can be used to invest in endowments. Indeed, most of the A.I.D. endowments recently established in Central America have used ESF-generated local currency as their primary source of funding. Again, the use of local currency for this purpose is dependent on securing agreement with the host government. Host governments have been inclined to support such initiatives because ESF local currency funding of endowments is usually invested in government bonds, which means the currency can remain nonmonetized, thereby reducing potential inflationary pressures within the economy.

### Food for Peace—PL 480

Another possible source of funding for endowments is local currency generated through sales from Title I and III food aid programs. The interest from these endowments can be reinvested in the endowment or used to finance development activities authorized in the endowment agreement. Current General Counsel rulings do not allow local currency generated from Title II sales to be used for endowments.

## Investing the Endowment

The major objective of an endowment is to provide a stable, if not expanding, source of interest earnings to finance the expenses of operations and programs for which the endowment was established. Building a stable and predictable source of endowment earnings obviously presents a challenge in many developing countries where volatile economic conditions can inject great uncertainty in financial markets. Thus, great care must be exercised to protect the endowment from being devalued by adverse changes and disturbances in the larger economic order.

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Most of the A.I.D. endowments listed above have included agreements among A.I.D., the host government, and the party receiving the endowment that the endowment funds would be invested in short-term government bonds. The interest yield is negotiated with the government, usually at a fixed rate several points above the inflation rate. Obviously, if the agreement required investment in longer term bonds, it would be important to obtain a variable interest yield indexed to the inflation rate. Even more imaginative formulas can be employed. For example, on long-term bonds it would be possible to secure a higher interest in compensation for allowing the bonds to mature and the principal returned in part or in full to the government.

Where large amounts of ESF or other types of A.I.D.-generated local currency are used to establish an endowment, the host government frequently insists, as mentioned earlier, that the currency be invested in government bonds rather than be monetized to reduce possible inflationary pressures on the domestic economy. In these instances, it is still possible to negotiate an agreement whereby some portion of the endowment could be monetized and thereby invested in other types of in-country assets or even converted to a foreign currency for investment abroad.

For example, in establishing the EARTH endowment, $50 million in U.S. dollar equivalent was invested in Central Bank of Costa Rica bonds, and $10 million was converted to U.S. dollars and placed in a U.S. trust account.

Where endowment transactions involve smaller investments, the host country government may allow a more diversified financial portfolio. This was the case for IDEA in Ecuador, where A.I.D. and the host government negotiated a $400,000 endowment, half of which was invested in the Ecuador branch of Citibank, which is providing a 43.5 percent annual interest on a 3-year CD, and the other half was converted to U.S. dollars and invested in U.S. Government Treasury notes.

Where endowment funds are not earmarked by any conditionality, the opportunity arises to build a more diversified portfolio, with funds invested in low-risk securities, real estate, and the like. FUNDAGRO, for example, used part of its endowment to purchase a commercial building to house its offices and rent the remaining space. ISA is investing a portion of its endowment in a housing development project, which upon completion will be sold and the proceeds reinvested in the endowment.

## Expanding the Endowment

A frequent objective in establishing A.I.D. endowments is to include provisions that ensure the growth of an endowment beyond its original value. This is done for two reasons. First, the earnings from the original endowment may not be sufficient to cover the expenses of the development organization that it is designed to support. Thus A.I.D. will insert a condition in the MOU indicating that interest earnings must be reinvested for a specified time in order to expand the endowment. During this interim period, A.I.D. and the host government will usually provide a grant to cover the operating and program costs of the endowed organization.

The second reason for expanding the endowment is to make the endowed organization more responsive to and identified with national and international sources of support. To do this, a provision can be employed requiring matching funds, thus compelling the recipient organization to mobilize specified amounts of donations (in cash or kind) from other in- and out-of-country sources, with the A.I.D./host government contributions provided in installments upon meeting the matching conditions. The EAP endowment agreement includes a matching provision whereby the A.I.D./host government endowment is provided in three installments. Each installment is released in sequence, once EAP has matched 25 percent of each installment, of which half must be in cash instead of in-kind contributions.

## Endowment Governance and Management

In most A.I.D. projects the legal and operational stewardship of the endowment is usually vested in a board of trustees or directors. Thus, in the case of EAP, responsibility for the endowment resides in the EAP Board of Trustees, for CINDE in the Board of Governors, and for EARTH in the Board of Trustees. The members of the board or the trustees serve in a fiduciary role and are thereby legally obligated to manage the endowment in accordance with conditions specified in the MOU.

In some cases an independent board of trustees, separate from the board of directors of the endowed organization, is established and vested with the management of the endowment. In the case of CINDE, this approach was used to produce greater distance between the authority to disburse the endowment earnings (vested with the trustees) and the organization (CINDE) expending the funds. It was assumed that the Board of Trustees, as a separate entity, would be more inclined to hold CINDE accountable for its performance than if both the disbursement and expenditure authority were vested solely with the Board of Directors.

In brief, establishing a separate board of trustees may be appropriate where the endowed organization is new and thereby without a sound track record of performance. Such a board may also be necessary with large endowments because of the possibility for conflict of interest or in cases where the inclination toward lax performance instilled by secure endowment earnings might adversely affect the intent of the endowment.

A range of additional provisions can be and usually is incorporated in the MOU or the A.I.D. project agreements that serves to strengthen the accountability and integrity of the management mechanism. A standard provision in the management of the endowment is the selection of a bank to establish a fiduciary account for the deposit and maintenance of endowment funds. As custodian of the funds the depository bank releases endowment funds and earnings for investment or expenditure as instructed by the board of trustees or directors of the endowed organization and in accordance with the conditions included in the MOU.

Another MOU provision for the management of endowments involves the selection of a securities trading company to manage the portfolio of endowment investments. Such a provision is not warranted when the endowment is invested in, for example, government bonds. However, once endowment funds are available for more diverse investments (securities, real estate, and so on) the financial expertise of a reliable trading firm is needed to ensure that funds are invested wisely.

The A.I.D. endowment agreement usually insists that both the depository bank and trading firm be bonded and that they be selected in an open bidding process, with A.I.D. frequently involved in the final selection process. In addition, the agreement usually stipulates that the endowment be periodically audited by a public accounting firm, selected through competitive bidding and frequently involving A.I.D. in the selection process.

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The management mechanisms mentioned above are all designed to provide a safeguard to protect the integrity of the endowment and to ensure that the endowment funds and earnings are invested and disbursed in accord with their intended purpose. These provisions are also designed to instill confidence in the host country public that endowments, partially funded as they are from formerly public monies and held as a public trust, are managed in a manner deserving of public trust.

## Dissolution of the Endowment

An MOU may or may not stipulate a time limit for the life of an endowment. In the case of CINDE, the MOU indicates that the endowment will be dissolved in 1996, after which it can be continued only if the host government, A.I.D., and other donors determine that such continuation is warranted. The duration of the endowment may also be governed by the statutes of the endowed organization, as in the case of FUNDAGRO, which is mandated to exist for 50 years.

The agreements of some of the A.I.D.-funded endowments explicitly stipulate that the provision of the endowment fund is "irrevocable and non-reimbursable, subject only to conditions contained in the Memorandum." This clause is intended to protect the endowment from unwarranted interference or termination by outside parties. The provision is important, largely because in many countries the concept of the endowment is new and may be viewed with skepticism in some quarters. Furthermore, what may be a friendly government today might, with a changeover, become an unfavorable force tomorrow.

An MOU may stipulate that the endowment agreement can be terminated if one or more of the signatories seek to substantiate, through judicial procedures, that the fiduciary role entrusted to the endowed organization is being mismanaged or abused, or that the endowed organization is not succeeding in its mission. There may also be a provision that the endowed organization may dissolve the endowment voluntarily for lack of success in meeting the conditions and objectives contained in the MOU, with further stipulations on whether the endowment funds will revert to A.I.D. and/or host government control or transferred to another organization.

## Issues of Concern

What are some of the issues that could hinder host governments and donors from establishing a successful endowment? Given the newness of A.I.D.-sponsored endowments, the record of experience from which to identify problems and pitfalls in these types of activities is still insufficient. However, based on a reading of A.I.D. design and review documents, it is clear that certain issues reappear in sufficient frequency to suggest some areas of potential concern. These concerns center on issues of institutional displacement, organizational performance, political interference, devaluation of the endowment, financial accountability, and termination of A.I.D. involvement.

## Institutional Displacement

Does the establishment of an endowed nongovernmental organization serve to duplicate if not displace existing government institutions? Does the creation of an endowed nongovernmental organization serve as an excuse for avoiding the larger issue of governmental reform? Finally, is support for endowed nongovernmental organizations simply a disguise for pursuing a traditional donor strategy of bypassing inefficient government institutions by establishing an independent project entity, which then arouses the resentment of old-line bureaucracies and consequently is frequently dismantled after the donor project is terminated?

These questions require considerable forethought by those contemplating using the endowment as a development strategy. In the case of CINDE and CDF, it was clear that the host government was convinced that the functions to be addressed by these two foundations needed to be transferred from the public to the private sector. In the cases of two of the universities (ISA and EAP), both were long-established private universities with a recognized track record of educational and research contributions. The third university, EARTH, received an endowment only after a careful review suggested that it would be too costly to add programs in the humid tropics to each of the many universities in Central America. Finally, IDEA, FUNDAGRO, and FHIA have identified a niche for themselves that complements rather than duplicates existing government facilities.

It is obvious that in the design and operation of an endowed organization, potential displacement effects have to be given careful consideration. For example, endowed nongovernment organizations always run the risk of prompting an internal brain drain when, with their superior working conditions and higher salaries, they attract talented officials away from government agencies. Not only would a brain drain serve to weaken, if not demoralize, government agencies, but it might arouse considerable resentment and perhaps a political backlash against endowed organizations as well.

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## Organizational Performance

Once an organization is endowed how can A.I.D. ensure that it remains responsive to its intended purpose and clientele? Does a secure financial base undermine organizational efficiency and effectiveness? Are there incentives and mechanisms that can be built into an endowment that can thwart the natural tendencies of financially secure organizations toward inertia?

One primary objective of an endowment is to provide the organization with a financial base that allows it, be it an agricultural research foundation, a university, or a trade and investment institute, to achieve greater program continuity by freeing it from the vagaries of irregular and inadequate sources of funding. In this regard, there is an important distinction between financial viability and security. Viability means that the endowed organization has sufficient resources to become an effective actor in the development arena, but it still must mobilize additional resources from its environment to fully support and sustain its activities over the long haul. In brief, it is less than financially secure.

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In order to keep an endowed organization responsive to its external environment, and closely linked with the needs of its clientele, some A.I.D.-sponsored endowments are designed only to achieve financial viability, not complete security. assumption is that a secure base might serve to .eate a more inward, rather than externally responsive, organization. Better to have an organization that always remains a little hungry, forcing it to secure some of its resources the old fashioned way, by earning it in the marketplace. In some cases, a matching grant formula can be used to further stimulate the endowed organization to mobilize a broader base of financial support.

Whether an endowment is utilized to create conditions of financial viability or security, organizational accountability can also be buttressed by designing strong governance mechanisms. In particular, the selection of a board of trustees or directors that is willing to exert a strong oversight role over the endowment and the endowed organization is one way of ensuring that performance is closely monitored and evaluated. In order to ensure a strong governance mechanism A.I.D. can exercise a role in selecting the board members.

Finally, the presumed comparative advantage of an endowed organization is that, by virtue of its independent status, the organization will be able to attract and financially reward the best available leadership and staff, thereby maintaining standards of excellence and performance that would be difficult to match under more conventional conditions. Indeed, because of higher salaries offered by FUNDAGRO in Ecuador, the foundation has been able to attract highly able Ecuadorean scientists who would otherwise have remained outside the country in more lucrative positions.

A.I.D. can employ a number of measures to strengthen performance standards of endowed organizations. In addition to taking a strong and active role in selecting board and staff members for the endowed organization, A.I.D. can also have an official or ex officio representation on the board. A.I.D. can also assign a tutelage or custodian role to an experienced outside contractor, who can assist a newly endowed organization in setting standards of performance and accountability in staffing and programming and in building constituency linkages. In the case of CDF, the A.I.D. project agreement includes the provision of grant funds to secure a contractor with wide experience in the management of natural resource programs to work with CDF over a 4-year period to establish and implement CDF programs.

## Political Interference

Once an organization is endowed how can A.I.D. ensure that the endowment remains inviolate, particularly from invasion and appropriation by the host government? How can A.I.D. ensure that the governance and management of the endowed organization are not subject to host government interference and manipulation?

There are no easy answers to these questions, although there are a number of measures that can be employed to reduce the risk of government meddling. One is to simply coopt important government agencies by including their representatives on the board of directors of the endowed organization, as is the case in several endowments mentioned in this paper. Such representation is warranted not only as a self-protective measure, but also because it may be appropriate for government agencies to have a legitimate voice in deliberations involving the endowed organization, particularly if the organization is working in cooperation with public sector, as well as private sector organizations.

Another method of shielding the endowed organization from outside influence is to enlist the participation of distinguished individuals, from within and outside the host-country, who can serve as members on the board of directors, or on various advisory councils for the endowed organization. This measure, coupled with a solid base of custodial agreements with banks and investment trading firms to properly manage the endowment, can further insulate the endowment from outside intruders.

The likelihood of indirect government intrusion would probably occur where there is default on interest or principal payments from endowment investment in government bonds, where firms with shares held by the endowment are nationalized, or where the government reneges on a previously agreed schedule of installment payments to the endowment. These conditions can arise either under extreme economic duress or where a changeover in government produces a leadership that is hostile to endowed organizations.

Government hostility, while it may not lead to interference, can greatly reduce the effectiveness of an endowed organization and its capacity to work with public and private agencies. The most effective strategy in averting or defusing government antipathy is by ensuring that the endowed organization has a leadership that is politically astute and sensitive to government concerns. In particular, the leadership should be skilled in building coalitions of support across a broad political spectrum, while at the same time firmly establishing the endowed organization as a nonpartisan entity.

## Devaluation

In many developing nations, particularly those with unstable political or economic structures, there is always the risk of rapid devaluation of endowments as a result of rampant inflation, currency devaluations, or sweeping and unexpected changes in government policies. An undiversified or illiquid endowment portfolio can be quickly eroded in value from such perturbations.

The risk factor may be particularly high in the early stages of the endowment, when most or all of the endowment resources are invested in government bonds. Some endowment agreements allow for the eventual movement of all or part of the original endowment, upon maturation of the government bonds, into other investments on the open market, including real estate and debt and equity investments. In some cases, the agreement also allows for the conversion of endowment resources into foreign currency for offshore investments. This allowance opens the door for endowment managers to diversify the portfolio and thereby shield the investments from undue erosion in value.

The ability of endowment managers to move the investment to a diversified, low-risk portfolio is partly conditioned by the flexibility and skill of A.I.D. and the host government in negotiating an imaginative yet financially sound MOU. Success in this area requires using experts who are highly knowledgeable of host country legal and financial regulations, as well as specialists who have international experience in designing endowments.

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## Financial Accountability

How can A.I.D. ensure that improprieties do not occur in the management of endowment resources? Are regular audits a sufficient means for ensuring that endowments are properly administered? How can A.I.D. protect endowment investment decisions from being biased by conflicts of interest?

These questions assume particular prominence in cases where the endowment corpus is large and the host country financial community relatively small, ingrown, and lightly regulated. These conditions can give rise to malfeasance or conflicts of interest involving members of the board, the bank custodian, or the investment management firm.

A.I.D. has sought to deal with these uncertainties by insisting on a range of protective measures, including annual audits by a reputable public accounting firm selected on a competitive basis, with A.I.D. as a voting member in the selection process, and the selection of the custodian bank and investment firm, again selected competitively with A.I.D. input. In addition, the contracts with auditors and custodian agents can be subject to periodic review, if not termination and rebidding. Finally, A.I.D. frequently insists that the board members and other custodian agents file financial disclosure statements.

## Termination of A.I.D. Involvement

At what point does A.I.D. responsibility for monitoring and exercising control over the management and use of the endowment earnings end? Can A.I.D. hold the endowment management and endowed organization accountable beyond the life of the project? Or does this responsibility cease when the project terminates?

In a few cases, these questions can be answered with ease; such is the case for CINDE, whose endowment will be up for review, if not termination, in 1996. However, for most of the other endowments, which are designed to last much longer, if not indefinitely, there are no definitive A.I.D. policy guidelines. The lack of established guidelines leaves A.I.D. with considerable latitude for incorporating conditions in the endowment MOU that can give the Agency a long-standing direct or indirect role in monitoring the governance of the endowment. These conditions include A.I.D. representation on the board of directors, periodic reporting to A.I.D., or periodic audit by an accounting firm approved by A.I.D.

Designing a longer term role for A.I.D. in the management of an endowment should be approached with some care and understanding of the political climate of the host country. For example, A.I.D. insistence on a longer term involvement might rouse a current or future host government to assume a more obtrusive role in the endowment management, a condition that could create an onerous burden for an endowed organization if not compromise the purpose of the endowment.

## Conclusion

In developing countries with weak institutional and legal structures, issues concerning organizational performance, political interference, devaluation, accountability, and A.I.D. termination assume greater salience. Under these conditions, the governance of an endowment can be more easily enfeebled or diverted from achieving its intended purpose. Such a situation presents a challenge to donors like A.I.D. in designing effective safeguards that can shield the endowment from a perilous environment. In some situations, the environment may be so turbulent as to negate this possibility.

The task of designing safeguards is much easier in developing countries where a stable political and economic order has allowed legal and institutional systems to assume a level of independence and integrity necessary for supporting the increasingly complex social and economic interactions of a modernizing country. These factors help provide some of the necessary preconditions for allowing an endowed organization to perform its designated purpose.

Necessary conditions must also be supplemented with sufficient conditions in order for an endowed organization to effectively perform its intended development role. Thus, having astute and politically sensitive leadership at the helm of an endowed organization is immensely important for garnering public support for and confidence in the organization's operations and programs. This fact is particularly important in developing countries where endowments and free-standing, nonprofit private organizations are still a relatively new concept.

In one sense, the emergence of the endowed, nongovernmental organization may be viewed as both the cause and effect of a more pluralistic social order. The establishment of endowments meets the need for expanding the organizational diversity of a society in order to address important public needs that might otherwise be inadequately met. Likewise, endowments can become a mechanism for animating and harnessing private resources and participation in addressing public needs.

# A.I.D.-Funded Endowments

## Coalition for Development Initiatives (CINDE), Costa Rica

In 1982, the Government of Costa Rica and the A.I.D. Mission agreed to establish the Coalition for Development Initiatives (CINDE), a nonprofit private foundation designed to promote foreign investment, agricultural exports, industrial reconversion for export, and export-oriented training.

CINDE was created in response to previously unsuccessful efforts by the Government of Costa Rica to promote trade and investment through public sector organizations. The performance of the public institutions had been less than optimal because salaries were too low to employ a high-level staff, management flexibility was constrained by bureaucratic regulations, and operational decisions were frequently subject to political interference. CINDE was established as a private foundation with sufficient latitude and autonomy to overcome many of the obstacles previously encountered by public sector trade and investment promotion organizations.

During CINDE's initial years of operation, its programs were funded primarily from annual Economic Support Fund (ESF) local currency grants. However, with a projected decline in ESF levels, in 1989 the Government of Costa Rica proposed to the international donor community at the Consultative Group meeting in Paris that an endowment of $110 to $120 million dollars be established, the income from which would be sufficient to fund most of CINDE's promotional activities. A.I.D. responded positively to this proposal; preliminary agreements between the Government of Costa Rica and the USAID Mission allocate an initial $27.15 million in ESF local currency to the endowment with additional ESF local currency grants of $45 million in subsequent years. In addition, the Costa Rican Central Bank is providing annual contributions to the endowment for a 20-year period. Additional operating expenses for CINDE will be covered through user fees and private contributions.

To avoid a potentially inflationary impact, the endowment will initially be placed in monetary stabilization bonds issued by the Central Bank of Costa Rica. Thereafter, the funds will be moved into private sector investments. The agreement with the Government also allows that a portion of interest earned from the income be converted into foreign currency to support CINDE overseas investment promotion.

Given the sizeable CINDE endowment and the need to hold CINDE accountable to specified performance targets, project designers created an elaborate set of checks for the management of the endowment. In particular, they vested the ownership, control, and programming of the endowment in a Board of Governors, established independently from CINDE. The Government of Costa Rica, A.I.D., and other donors will nominate and select the five-member Board in rough proportion to donor and Government contributions. The Board will be responsible for monitoring the performance of CINDE's programs, will have the authority to vary individual program funding by up to 20 percent, and will have the right to terminate funding of any of CINDE's programs, a decision that can be reversed only by agreement between the Government and participating donors. Changes in programming proposed by the Board, the Government of Costa Rica, or A.I.D. will be subject to approval by the Government and A.I.D.

These checks are further reinforced by a range of administrative and financial controls, including prior A.I.D. Mission approval over the design of the endowment's financial systems, its cash management and disbursement policies, and the financial controls of CINDE's program operations. Annual independent audits of the financial, administrative, and procurement systems of the fund and the programs it finances will be conducted by public accounting firms approved by the Government and A.I.D. In addition, A.I.D. can conduct its own audits or evaluations of the endowment and the CINDE programs.

The agreement stipulates that the endowment be dissolved in 1996. The endowment can be continued after this date, but only if there is a positive determination by the Government of Costa Rica and A.I.D. and other participating donors that continuation is warranted. Otherwise, the endowment will revert to the Government treasury or be reallocated to other development activities.

## Foundation for Agricultural Development (FUNDAGRO), Ecuador

In 1986, the Government of Ecuador established the Foundation for Agricultural Development (FUNDAGRO) as a private, not-for-profit institution. FUNDAGRO grew out of recommendations made by a high-level commission established by the Minister of Agriculture and composed of distinguished U.S. and Ecuadorean agricultural specialists.

FUNDAGRO is designed to revitalize a national research, extension, and education system that had failed to foster the innovation and transfer of technologies for improved productivity in the agricultural sector. The Government-operated agricultural research institute had been constrained by a range of political and administrative factors, including lack of public sector commitment to a strong research and outreach program, low budgets, political interference, lack of long-term program planning, inability to focus scarce resources on priority research problems, absence of linkages with farmers and the private commercial sector, and an inability to recruit and retain highly qualified agricultural professionals. Similar problems have plagued Government extension services and agricultural institutions of higher education in Ecuador.

FUNDAGRO is designed to achieve a more integrated research, extension, and education system, not by duplicating or displacing existing public and private sector programs, but rather by serving as a catalyst in enhancing the interaction between these activities and linking them more directly with farmer clientele. FUNDAGRO performs these tasks by employing a small, highly qualified staff to work with public and private sector institutions in the joint selection, planning, and funding of long-term applied commodity research and extension programs. As a participant and leader in this process, FUNDAGRO provides supplementary grants to support the work of the agencies working on these programs.

In its initial years of operation FUNDAGRO programs were partially supported by PL-480 local currency grants. In 1987, discussions were initiated among FUNDAGRO, the Government of Ecuador, and A.I.D. on establishing an endowment to provide the Foundation with greater independence, flexibility, and continuity. Thus, in 1988, an agreement was reached that awarded FUNDAGRO with a local-currency grant equivalent to $3 million drawn from the PL-480 local-currency account. The grant agreement forbids withdrawals from the endowment and its income for 5 years in order to expand the endowment principal. In the interim A.I.D. provided an operational grant to help defray operational and program expenses. A matching formula was also attached as a condition to the endowment grant, with the Government and A.I.D. agreeing to provide an initial installment of 80 percent of the total grant. The remaining 20 percent was to be allocated, as determined by the PL-480 advisory committee, after FUNDAGRO undertook a market survey of private funding sources and submitted a fund-raising strategy. FUNDAGRO has appointed to its staff a Development Officer responsible for cultivating alternative in- and out-of-country funding sources.

The management of the endowment is vested in a number of bodies within and without FUNDAGRO. A four-person oversight committee, appointed by the FUNDAGRO Board of Directors, is responsible for conducting an annual review of FUNDAGRO's obligations under the grant terms. The agreement stipulates that the oversight committee consist of high-level officials from international agricultural research centers, international private voluntary organizations, and third-country foundations or development agencies with experience in Latin American agriculture. Finally, the grant agreement stipulates that FUNDAGRO contract with an international financial services or accounting firm to assist the foundation in selecting a local bank and financial agent to manage the endowment investments. This firm will also assist in an annual performance review of the selected bank and financial agent.

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## Cordillera Development Foundation (CDF), Costa Rica

In 1989, the Government of Costa Rica established the Cordillera Development Foundation (CDF) to assume responsibility for managing a major national forestry reserve in the central Cordillera area of Costa Rica. The initiative reflects a recognition by the Government of Costa Rica that existing government structures are too fragmented, inefficient, and bureaucratic to effectively manage protected wildland areas and that a more unified, flexible, and responsive organizational model would be needed to perform this task. CDF was established as a private, nonprofit foundation to achieve this end.

CDF is the first of a number of foundations to be established for wildland management. The foundation will have its own management and technical cadre who will plan and manage a wide range of complex natural resource management tasks in the Cordillera area, including protecting the central forest reserve, introducing new agroforestry practices to farm communities in the buffer zone surrounding the reserve, supervising a private sector incentive system for sustainable harvesting of selected forests, and operating a range of tourist facilities in the protected wildland areas.

The USAID Mission has supported the Government of Costa Rica's policy of reorienting its forestry management approaches; in 1989, A.I.D. reached an agreement with the Government whereby A.I.D. would provide a $7.5 million grant to help fund the start-up costs of CDF. In addition, A.I.D. and the Government agreed to provide $8 million in ESF local-currency to establish an endowment for CDF. The intent of the endowment is to build a financial base for CDF, so that at the end of the 7-year A.I.D. project, earnings from the endowment would be sufficient to sustain CDF in perpetuity.

The A.I.D.-Government of Costa Rica agreement provided that the $8 million endowment grant be deposited in the Central Bank of Costa Rica where it will receive a rate of interest equal to the rate paid by the Bank's monetary stabilization bonds projected at 22.5 percent annually. With an inflation rate of 18.5 percent annually, the projected real rate of interest is

4 percent. The agreement stipulates that the endowment cannot be monetized until after the completion of the 7-year project. Finally, for the duration of the 7 years, all interest is to be added to the principal in order to expand the endowment to an amount sufficient to cover the operating costs of CDF after the termination of the initial A.I.D. project grant of $7.5 million. CDF will also be able to supplement its income from user fees, concessions operating in the protected area, and nominal admission fees to the national parks in the wildland areas.

CDF has a five-member Board of Directors, three of whom are appointed by the Ministry of Natural Resources, Energy, and Mines; one by the Municipality where the wildland areas are located; and one by the Executive Branch of the Government. Because CDF is new and lacks a track record of previous performance, the USAID Mission included a provision in the project agreement for an outside contractor with appropriate expertise to assist the Board during the initial 4 years in building the organization, recruiting and training staff, and implementing project activities.

The project agreement also provides for one A.I.D.-contracted adviser to serve as liaison between A.I.D. and the project, and to work closely with the support contractor; the Ministry of Natural Resources, Energy, and Mines; and CDF during the first 4 years of the project.

In addition to annual A.I.D. audits, CDF is required to have a public accounting firm to conduct periodic audits of its U.S. dollar and local-currency endowment accounts. The project agreement also requires that the CDF Board, A.I.D., and the Ministry of Natural Resources, just prior to the completion of the 7-year project, jointly select a financial institution to manage the endowment fund.

## Honduran Agricultural Research Foundation (FHIA), Honduras

In 1984, the Honduran Agricultural Research Foundation (FHIA) was established as a private, nonprofit foundation. The land, buildings, and other facilities for FHIA were inherited as a gift from the former agricultural research facilities of the United Brands Company. In order to provide an initial base of funding, A.I.D. awarded a 10-year grant to FHIA to help cover the Foundation's operating and program expenses.

The FHIA mandate is to engage in research and extension on agricultural crops. FHIA soon demonstrated a capacity to effectively conduct short- and medium-term applied research and to rapidly disseminate research results to farmers. These achievements were notable because they addressed the problem of the declining rate of growth in the agricultural sector.

FHIA's accomplishments prompted the Government of Honduras and A.I.D. to examine the prospect for further strengthening the Foundation's research and extension role. Thus, in 1989, A.I.D., the Government, and FHIA initiated negotiations, soon to be completed, to establish an endowment sufficient to meet FHIA's core operational and program expenses.

The Memorandum of Understanding (MOU) vests fiduciary responsibility for the endowment with the FHIA Administrative Council, a nine-member group operating under the guidance of the FHIA General Assembly, which consists of private citizens and government officials concerned with agricultural research and extension. The funding source for the endowment is ESF locally generated currency. The MOU requires that the endowment be invested in general government revenue bonds. Reinvestment of earnings on the endowment capital from ESF funds in other than government bonds can be done only in consultation with the Government to ensure that these reinvestments are consistent with the Government's economic stabilization policies.

The endowment will be provided in installments. A matching formula requires FHIA to match a percentage of the total A.I.D./Government of Honduras contribution to the endowment. This formula is designed to encourage FHIA to expand the endowment and to build a long-term support constituency for its research.

FHIA can meet its matching requirement through either cash or in-kind contributions. However, the MOU limits in-kind contributions (e.g., capital assets like buildings, land, equipment) to no more than half of the total contributions. The other half must be in the form of cash contributions to the FHIA endowment. Furthermore, FHIA will receive double credit on the match for contributions made in foreign currencies, such as U.S. dollars.

FHIA will be given a specified time to meet the matching requirements for each installment. During this period, interest earned for each installment must be reinvested in the endowment until the match contribution is fulfilled, at which time subsequent earnings can be used to meet core program and operating expenses. The Government has the right to reclaim the interest on those installments if FHIA does not provide matching funds in the specified time period.

Earnings from Government/A.I.D. contributions to the FHIA endowment must be spent on a range of core operational and program expenses, as specified in the MOU. FHIA must consult with the Government of Honduras and A.I.D. if it wishes to alter the agenda of core expenses. However, earnings from contributions generated by FHIA's matching contributions can be spent at FHIA's discretion. Similarly, matching contributions designated as an endowment donation can be invested by FHIA in government or nongovernment investments.

The roles of A.I.D. and the Government of Honduras in governing and managing FHIA are spelled out in the MOU. A.I.D. has official membership on the FHIA General Assembly and Administrative Council, whereas the Government of Honduras has ex officio membership on these bodies. FHIA must provide semiannual financial reports to the Government of Honduras, employ a certified public accounting firm acceptable to the Government, and submit annual audit reports to the Government.

## Institute for Agricultural Strategies (IDEA), Ecuador

In 1985, the U.S. Agency for International Development (USAID) Mission and the Government of Ecuador signed a grant agreement to fund an agricultural policy institute within the Science Foundation, a private nonprofit organization. The purpose of the institute was to conduct economic studies and sponsor public seminars and workshops on important agricultural policy issues. In 1988, the institute was established as an independent foundation and renamed the Institute for Agricultural Strategies (IDEA).

IDEA emerged as a result of a growing interest by leaders in the Government of Ecuador and A.I.D. to elicit private sector support for a more market-oriented approach to agricultural growth. To mobilize the private sector some kind of institutional mechanism was needed to build linkages where few existed between agriculture, producer and peasant associations, and input and product supplier organizations. IDEA was established to serve as such a mechanism.

IDEA's principal role is to stimulate agricultural policy analysis, discussion, and debate within the private sector, thereby building the private sector's capacity to demand sound policy decisions. IDEA has a board of directors and a small professional staff that manage and fund the contracting of important policy studies and seminars to the private sector. The focus of these efforts is primarily in macroeconomics, prices and marketing, and natural resource policy. IDEA carries out pilot or demonstration projects following the completion of some of these studies. It is also providing overseas scholarships to train a small cadre of policy analysts.

*IDEA's principal role is to stimulate agricultural policy analysis, discussion, and debate within the private sector, thereby building the private sector's capacity to demand sound policy decisions.*

Current IDEA expenses are funded from an A.I.D. grant. Once this grant expires IDEA funding will be drawn from several sources, including income from a $400,000 endowment established in 1989 by A.I.D. from PL-480 local currency. The endowment interest is to be reinvested and allowed to accumulate and compound until the expiration in 1993 of the A.I.D. project grant.

The major portion of the endowment ($300,000) has been deposited in a Citibank account, where it is provided a bank guaranteed rate of interest of 43.5 percent for a 3-year period. The remaining $100,000 has been converted to dollars to purchase U.S. Government Treasury notes. The finance committee of the IDEA Board of Directors manages the endowment.

## Superior Institute of Agriculture (ISA), Dominican Republic

In the Dominican Republic over the past decade, demand in the private sector has increased for trained agricultural technicians and researchers who can service a growing agribusiness sector in nontraditional export crops. However, in the Dominican Republic institutions of agricultural higher education have lacked sufficient financial resources to reorient their training and research to meet this new need.

To redress this problem, A.I.D. and the Government of the Dominican Republic agreed in 1989 to provide the Superior Institute of Agriculture (ISA), the nation's premier undergraduate agricultural college, with a large grant to substantially enhance ISA's educational and research capacities in nontraditional agricultural export. This agreement also includes a provision for a large local-currency endowment, the earnings from which will help sustain the new university programs after the termination of the A.I.D. project.

The A.I.D. grant was designed to refurbish and expand ISA's infrastructure (laboratories, equipment, supplies, library materials), fund new educational and research programs, expand the faculty, and, most important, substantially increase faculty salaries. In recent years, many of ISA's faculty have gone to the private sector, where they command much higher salaries.

While the grant provides a large infusion of capital to cover operating and program expenses, project designers were seriously concerned that ISA would be unable to sustain these improvements beyond the life of the project. As a private, nonprofit institution ISA cannot rely on Government funding; instead it must depend on diversified sources of self-generated income to maintain its financial viability. One source is tuition fees; however, because many of ISA's students come from poor rural households, their expenses need to be covered by ISA subsidies.

To build a larger, more self-sustaining income base for ISA, the A.I.D./Government of Dominican Republic agreement included the equivalent of a $2.4 million endowment from local currency generated from Economic Support Funds (ESFs). The A.I.D./Government agreement vests fiduciary responsibility for the endowment with the ISA Board of Directors. The Board is composed of leaders from business, civic, and religious organizations, as well as representatives from government agencies, including the Secretaries of Education and Agriculture and the Director of the Government of the Dominican Republic Agricultural Bank.

The endowment agreement includes a matching formula whereby for every peso that ISA secures as a donation, the Government and A.I.D. approve disbursements of three pesos. The prospect for organizing a successful fund-raising campaign appears very promising, largely because ISA is closely linked to business and civic leaders in the Dominican Republic. ISA has already surpassed the targeted amount of donations by 200 percent for the first phase of the endowment agreement.

ISA has been very imaginative in its efforts to enhance the value of its endowment. It has invested a portion of the endowment in a multidwelling home-construction project, which on completion will be sold and the proceeds reinvested in the endowment fund. In 9 months the value of the building lot has increased fourfold.

ISA has recently secured Government approval to undertake a substantial debt-for-development conversion by purchasing $2 million of commercial arrearage. The Central Bank will convert the debt at the official rate, generating approximately $14.7 million in local currency, of which $4.7 million will go into an interest-bearing ISA account to meet local project costs, $5 million will be deposited into the ISA endowment fund, and $5 million will be placed in dollar-denominated Government bonds in ISA's name, the interest from which will go into the Fund, as will the principal upon maturation.

## Pan-American Agricultural School (EAP), Honduras

The Pan-American Agricultural School (Escuela Agricola Pan-Americana [EAP]) located in Zamarano, Honduras, was established in 1942 as a private, post-secondary school to train agriculturalists throughout the Latin American region. From 1942 to 1957 the school was able to cover its finances from a trust fund established by the United Fruit Company, and thereafter from additional funds generated from student fees, private and public donations, and sales of products grown at the school.

Over the years the school has grown in prominence and has been asked to assume an increasing range of education and research responsibilities. To expand its financial base to meet these challenges, in 1987, EAP initiated discussions with the USAID Mission and the Government of Honduras on the possibility of securing an A.I.D. grant to expand its endowment and the income from the endowment. Negotiations were concluded that same year; the project agreement provided EAP with a local-currency equivalent of $15 million.

The funds for the endowment were drawn from ESF-generated local currency. Because the ESF account is the product of a stabilization and recovery program supported by an A.I.D. project already approved by the Honduran legislature, additional legislative action to ratify the endowment was unnecessary.

The conditions stipulated in a formal memorandum of understanding (MOU) among EAP, the Government of Honduras, and A.I.D. require that the grant funds be invested only in short-term (3-5 years) general revenue Government bonds of the Central Bank of Honduras. EAP is further obliged to keep the endowment capital intact, meaning that the capital can only be touched for reinvestment purposes. The MOU also contains a clause making the endowment irrevocable and nonreimbursable, with any proposal for its dissolution subject to proceedings and laws of the Honduran judicial system.

Finally, it is stipulated that during the term of the MOU, which is due to expire in 8 years, reinvestment of the Government grant into securities other than government bonds can be done only after consulttion with the Government in order to ensure that such reinvestments are consistent with the Government's economic stabilization and recovery program. After the 8-year period, EAP is free to convert the bonds to other local and/or foreign investments.

The MOU authorizes EAP to use up to 70 percent of the income to cover the cost of education for Honduran students and the remainder to fund natural resource management programs carried out by the school nearby. This condition holds beyond the 8year MOU.

The MOU also includes a 25-percent matching requirement intended to encourage the school to mobilize funds from other sources. As part of the matching formula the Government of Honduras/A.I.D. local-currency endowment is provided in three equal installments. The second and third installments are released only after EAP demonstrates that it has met the 25-percent matching requirement in each case. Furthermore, the income generated from the first installment cannot be used by the school until it has met the matching formula for the second installment. This rule also applies to the second and third installment.

The matching formula also requires that at least half of the 25-percent match be in cash (local currency or U.S. dollars), with the rest allowed in kind, including buildings, land, equipment, and vehicles (but not for operating costs). Finally, the restrictions on the nature of portfolio investments (the purchase of government bonds) and the use of income generated (for Honduran students and natural resource management programs) from the Government grant do not apply to funds or assets generated by the matching contributions.

***The matching formula also requires that at least half of the 25-percent match be in cash (local currency or U.S. dollars), with the rest allowed in kind, including buildings, land, equipment, and vehicles (but not for operating costs).***

The MOU stipulates that EAP's Board of Trustees also serve as trustees for the endowment; they in turn are required to select, after careful review and after consultation with the Government, a depository institution to assume custody of the funds and to disperse the income generated from the endowment. The Board meets twice a year and has 22 active members, 7 of whom are from Honduras and 15 from the United States.

## Agricultural College of the Humid Tropical Region (EARTH), Costa Rica

In 1985, A.I.D. and the Government of Costa Rica agreed to jointly fund the establishment of the Agricultural College of the Humid Tropical Region (EARTH). Construction of the campus began in 1989, and the first class of 60 undergraduate students from Central America were admitted to the college in March 1990. One hundred students will be admitted each year for a total student population of 400 by the fourth year. The agreement also provides a $60 million endowment for the college to cover its basic operating expenses.

The establishment of EARTH was in response to growing concern in Central America over declining or stagnant production levels in basic food and export crops, the lack of crop diversification, and the degradation of the natural resource base, particularly in the lowland humid tropic zones. These conditions reflect a lack of technology generation, inappropriate agricultural policies, and an inadequate supply of well-trained agricultural technicians and scientists.

EARTH was established to fill the demand in Central America for Bachelor-level agriculturalists trained under a learn-by-doing approach focused primarily on the humid tropics. Several options were considered in meeting this need, including the option of adding the capability to existing universities in the Central American region. However, the option was abandoned in view of the numerous countries and universities in the region that would have to be involved in the effort and the highly politicized atmosphere that permeated most of the campuses.

EARTH is chartered as a private, nonprofit institution; it therefore has the freedom to design its own programs and to hire, compensate, and dismiss its faculty in accordance with policies established by its Board of Directors. Its primary funding base will be tuition fees, income generated from the college farm, earnings from an endowment, and monies raised through its own fund-raising campaigns.

A.I.D. and the Government of Coasta Rica agreed that $60 million in ESF local-currency equivalent would be invested in the endowment. Most of the currency (US$50 million) has been invested in monetary stabilization bonds issued by the Central Bank of Costa Rica. The trust agreement also permitted that $10 million in local currency be converted to dollars and placed in a U.S. trust account. The interest from the U.S. dollar account will remain in the account for the first 10 years in order to expand the endowment. Dollar costs, which cover equipment purchases, salaries for foreign faculty, and so on during the 10-year period will be financed by a dollar grant provided through the A.I.D. project.

## Luso-American Development Foundation

The Portuguese Luso-American Development Foundation was established in 1985 as a nongovernment organization. Its goal is to promote economic and social development in Portugal by encouraging cooperation between Portugal and the United States in the fields of science, technology, culture, education, and commerce. The Foundation is funded through an endowment provided by the Government of Portugal from Economic Support Fund (ESF) grants provided by A.I.D.

The impetus for establishing the Luso Foundation arose in the early 1980s as Portugal adopted more democratic political structures and aligned itself with the more progressive economic changes underway in the European Common Market. In this context, negotiations were initiated between the governments of the United States and Portugal concerning the restructuring of the U.S. aid program and the closing of the A.I.D. office in Portugal.

The final agreement reached between the two governments in 1985 provided an initial endowment of $38 million for the establishment of the Luso Foundation. The endowment was funded indirectly, with the United States providing ESF funds to the Government of Portugal, which, in turn, provided a grant to establish the endowment.

The governing mechanisms for the endowment consist of a Directive Council, an Executive Council, and an Advisory Council. The Directive Council determines the basic policies of the Foundation, including the annual budget, and has seven to nine members, of whom two are appointed by the U.S. Ambassador and the others by the Government of Portugal. A three-member Executive Council assumes daily management of the Foundation. The Advisory Council consists of four Portuguese and four U.S. experts in business and science.

The Foundation is free to invest its endowment funds in stocks, bonds, and other financial instruments to increase its income and operating capital. As of 1988 it had $104 million in equity and outstanding interest obligations.

The Foundation's program activities are focused on providing grants, loans, and loan guarantees for projects in the following areas: private sector development, science and technology, education, public administration, regional development, language, and culture.

Because of its small staff, the Foundation does not develop project proposals itself, but rather solicits outside sources to develop them. It particularly favors project submissions that promote cooperation among Portuguese organizations or collaboration between Portuguese and U.S. institutions. The Foundation generally does not finance more than 50 percent of the costs of a project and does not provide support for projects involving partisan political activities.

A major priority of the Foundation is to support private sector projects, mostly by providing reimbursable loans to entrepreneurial companies. Other projects in private sector development have included an in-depth study of a potential technological park, export studies, and training and cooperative activities with national and foreign institutions.

In science and technology, the Foundation is seeking to hasten the process of technological advancement by building a stronger partnership between the industrial sector and independent research laboratories. Projects are being funded in agricultural production and marketing, new materials production and applied research, energy generation and application, and the health sciences.

In public administration and regional development, the Foundation is supporting the upgrading of public sector management capacities, including expansion of training capacities in information management and of automation of government services. In education, the Foundation is providing financial aid to support graduate and post-graduate work in the United States and is funding extended visits by U.S. professors to Portugal. Technical cooperation between the United States and Portugal in biotechnology is also receiving substantial Foundation funding, as is language and cultural exchange, particularly in the areas of dance, costume design, and sculpture.

*This report was prepared by senior social science analyst Gary Hansen of the Center for Development Information and Evaluation, Program and Policy Evaluation Division. The views and interpretations expressed herein are those of the author and should not be attributed to the Agency for International Development. Comments or inquiries about this summary may be sent to the Center for Devlopment Information and Evaluation, Bureau for Program and Policy Coordination, Agency for International Development, Washington, DC 20523-1802.*

## *Innovative Development Approaches* Reader Survey

The purpose of the Innovative Development Approaches series is to communicate to A.I.D. Missions the key ideas behind new, experimental approaches being tried by A.I.D. and other agencies that have shown promising results in achieving priority development objectives and new policy thrusts. To ensure that *Innovative Development Approaches* responds to your information needs, please take a few minutes to respond to the questions below. Return the survey by removing this page, folding it along the dotted lines and mailing it to the address given.

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