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PROJECT AGREEMENT



AGENCY FOR INTERNATIONAL DEVELOPMENT

UNITED STATES AID MISSION TO PERU

C/O AMERICAN EMBASSY

LIMA, 1 PERU

TELEPHONE 333200

CABLE: USAID/LIMA

March 2, 1989

Mr. Hernando De Soto  
President  
Instituto Libertad y Democracia  
Avenida Benavides 881  
Miraflores

Subject: Private Sector Institutional Reform Project (598-0772),  
Cooperative Agreement No. 598-0772-G-00-5910-00

Dear Mr. De Soto:

Pursuant to the authority contained in the Foreign Assistance Act of 1961, as amended, the Agency for International Development (hereinafter referred to as "AID" or "Grantor") hereby grants to the Instituto Libertad y Democracia, a Peruvian Private Voluntary Organization (hereinafter referred to as "ILD" or "Recipient") the sum of \$1,800,000 to assist in the implementation of ILD's program of applied research and reform activities related to the informal sector.

Subject to the availability of funds, AID plans to provide an additional \$8,085,000, for a total not to exceed \$9,885,000. This first increment of \$1,800,000 is effective and obligation is made as of the date of this letter and shall apply to commitments made by the recipient in furtherance of program objectives during the period March 1, 1989 to February 28, 1990.

This agreement is made to ILD on condition that the funds will be administered in accordance with the terms and conditions as set forth in:

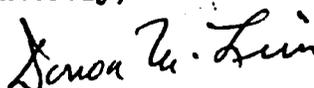
- Attachment 1, entitled "Schedule",
- Attachment 2, entitled "Program Description",
- Attachment 3, entitled "Optional Standard Provisions for Non-U.S. Non-Governmental Grantees", effective through December 31, 1989, and
- Attachment 4, entitled "Mandatory Standard Provisions for Non-U.S. Non-Governmental Grantees", effective through December 31, 1989.

Mr. Hernando De Soto  
Instituto Libertad y Democracia  
March 2, 1989

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Please sign the original and seven (7) copies of the letter to acknowledge your receipt of the Cooperative Agreement, and return the original and six (6) copies to this office.

Sincerely,



Donor M. Lion  
Director

**Attachments:**

1. Schedule
2. Program Description
3. Optional Standard Provisions for Non-U.S. Non-Governmental Grantees
4. Mandatory Standard Provisions for Non-U.S. Non-Governmental Grantees

**ACKNOWLEDGED:**

INSTITUTO LIBERTAD Y DEMOCRACIA



Hernando De Soto  
President

March 2, 1989

**FISCAL DATA**

Appropriation:	72-1191021.6
Budget Plan Code:	LDSA89-35598-KG12
PIO/T No.:	598-0772-3-9655910
Project No.:	598-0772
Total Estimated Amount:	\$9,885,000
Total Obligated Amount:	1,800,000

SCHEDULE

A. Purpose of Agreement.

The purpose of this five-year Cooperative Agreement is to assist the Institute for Liberty and Democracy (ILD) in the implementation of an international outreach, research dissemination, and training program; the expansion of these activities throughout Latin America and the Caribbean (LAC); and the strengthening of IID's policy development and implementation capacity. The main emphasis of IID to date has been on the working of the informal sector in Peru --- those economic activities carried on outside officially established laws, regulations, and taxes. Its programs have been directed toward making government and the general public aware of the size, functioning, and consequences of the informal economy in Peru through high quality research and publicity. It has developed proposals to promote changes in the legal, regulatory, and tax structures in order to integrate informal economic activities into the formal sector and to promote greater economic growth.

Under the terms and conditions of this Agreement, AID will provide funding for:

- budgetary support for IID's operations and institutional development in order to foster long-term self-sufficiency;
- implementation of development programs;
- design and implementation of training programs for the utilization of IID's research methodology by local research or public policy organizations throughout the Latin America and Caribbean (LAC) region; and
- development of an outreach program that will assist IID in expanding its international linkages to key public policy organizations and host governments in the LAC region; an important element in developing these linkages will be the selection of a U.S. coordinator to coordinate IID's activities in the United States.

B. Period of Agreement.

1. The effective date of this Agreement is the date of its signature. The expiration date of this Agreement is February 28, 1994.

2. Funds obligated hereunder are available for program expenditures for the estimated period March 1, 1989 to February 28, 1990, as shown in the Financial Plan, below.

C. Amount of Agreement and Payment.

1. The total estimated amount of this Agreement for the period shown in B.1., above, is \$9,885,000.

2. AID hereby obligates the amount of \$1,800,000 for the program expenditures during the period set forth in B.2., above, and as shown in the Financial Plan, below.

3. Payment shall be made to the recipient in accordance with procedures set forth in Attachment 3, Optional Standard Provision 1, entitled "Payment - Periodic Advance", until other payment procedures are established through issuance of project implementation letters.

4. Additional funds up to the total amount of the Agreement shown in C.1., above, may be obligated by AID subject to the availability of funds and to the requirements of Attachment 4, Mandatory Standard Provision 4, entitled "Revision of Agreement Budget".

5. The paying station for all activity under this Agreement will be USAID/Peru.

D. Financial Plan.

The following is the Agreement Budget, including local cost financed items, as authorized, and other contributions to the project. Revisions to the Budget shall be made in accordance with Mandatory Standard Provision 4 of this Agreement, entitled "Revision of Agreement Budget".

AGREEMENT BUDGET  
A. FINANCIAL PLAN, 1989-1994  
(in \$000)

<u>Source of Funding</u>	<u>Year 1 3/1/89- 2/28/90</u>	<u>Year 2 3/1/90- 2/28/91</u>	<u>Year 3 3/1/91- 2/29/92</u>	<u>Year 4 3/1/92- 2/28/93</u>	<u>Year 5 3/1/93- 2/28/94</u>	<u>Total</u>
AID	1,800	1,845	1,930	2,100	2,210	9,885
Other Donors and Sources	<u>325</u>	<u>795</u>	<u>1,265</u>	<u>1,735</u>	<u>2,210</u>	<u>6,330</u>
Total	<u>2,125</u> =====	<u>2,640</u> =====	<u>3,195</u> =====	<u>3,835</u> =====	<u>4,420</u> =====	<u>16,215</u> =====

AGREEMENT BUDGET  
 B. ESTIMATED BUDGET, YEAR 1  
 (March 1, 1989 - February 28, 1990)

<u>Expense Category</u>	<u>- - - AID Participation - - -</u>			<u>Other Donors and Sources</u>	<u>Total</u>
	<u>Foreign Exchange Costs</u>	<u>Local Currency Costs</u>	<u>AID Total</u>		
- Direct Labor	267,000	793,000	1,060,000	185,000	1,245,000
- Fringe Benefits	28,200	73,300	101,500	17,900	119,400
- Travel and Transportation	56,400	45,600	102,000	18,000	120,000
- National Advocacy and Dissemination	-0-	98,000	98,000	18,000	116,000
- International Training and Dissemination	55,200	84,800	140,000	25,600	165,600
- Evaluations, Systems Improvement and Audits	-0-	30,000	30,000	-0-	30,000
- Other Direct Costs	<u>43,200</u>	<u>225,300</u>	<u>268,500</u>	<u>60,500</u>	<u>329,000</u>
<b>TOTAL</b>	<b>450,000</b>	<b>1,350,000</b>	<b>1,800,000</b>	<b>325,000</b>	<b>2,125,000</b>

**E. Reporting and Evaluation.**

As more fully described in Section III.B. and C. of Attachment 2, IID agrees to provide annual implementation plans, reports, and financial statements, as well as any other reports which AID might consider necessary.

**F. Source and Origin of Procurement.**

Commodities financed by AID under this Agreement shall have their source and origin in Peru or the United States, except as AID may otherwise agree in writing. Except for ocean shipping, the suppliers of commodities or services shall have Peru or the countries included in AID Geographic Code 000 as their place of nationality, except as AID may otherwise agree in writing. Ocean shipping financed by AID under this Agreement shall, except as AID may otherwise agree in writing, be financed only on flag vessels of the United States.

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G. Standard Provisions.

1. All the Mandatory Standard Provisions for Non-U.S. Non-Governmental Grantees, provided in Attachment 4, and the following Optional Standard Provisions for Non-U.S. Non-Governmental Grantees, provided in Attachment 3, shall apply to this Agreement: 1, 3, 4, 5, 6, 7, 8, 10, 11, 12, 13, 14, 17, and 18.

2. To assist in the implementation of the project, AID from time to time will issue project implementation letters furnishing additional information on requirements about matters stated in this Agreement.

3. IILD and AID agree that the nature of the activities to be carried out under the Agreement require the substantial involvement of AID. IILD, therefore, agrees to:

- AID review and approval of Phase I activities (Years 1 and 2) prior to commencement of effort under Phase II;
- AID review and approval of programs and budgets for Phase II (Years 3 to 5); and
- AID decisions that conditions precedent and covenants have or have not been met.

PROGRAM DESCRIPTION

I. Introduction.

During the first two years of this grant (Phase I), IID will continue its ongoing development activities in Peru and develop an expanded international research and training program in conjunction with its conversion into an international organization. However, the specific activities, implementation, and budget of the second phase (Years 3 to 5) of the program will be based on the findings and recommendations of the Threshold Evaluation (see Section II.A., below) and those mid-course modifications agreed upon during Phase I.

This Agreement will support the following activities, all of which are aimed at the objective of effecting economic and institutional reform in Peru and the IAC region and to further the institutional strengthening of IID:

- implementation and dissemination of a major research program on the informal sector,
- development of an outreach program that will assist IID to expand its international linkages,
- a regional training program, and
- a U.S. coordinator.

For IID's detailed description of its activities, reference should be made to its proposal entitled "Institutional Reform with Popular Support for Private Sector Growth in Latin America", dated October 1988.

As part of its mandate, IID will conduct a multifaceted development program, the results of which will be used to formulate policy changes or reforms in Peru, especially in those sectors where the informal sector now plays a large role. It will disseminate its findings in Peru and abroad and make its proposed policy changes widely known, thus engendering broad public support for the changes.

Because the informal sector is an important component of the economies of most Latin American and Caribbean countries, IID will provide training for interested groups or individuals from Peru and from other governments and policy research groups organized to promote institutional change in a manner similar to that of IID. Participants will be selected only from countries eligible to receive direct AID assistance. The IID will also disseminate research abroad and institutional advances among these groups to stimulate additional research; it will provide them with technical assistance and opportunities for their staff members to engage in field work in Peru.

Innovative intellectual thinking and research are critical to IID's continued growth and effectiveness. To that end, IID will maintain a

coordinator in the U.S. to help to facilitate linkages with scholars, public policy institutions, and donor organizations in the U.S., Europe, Latin America, and the Caribbean.

II. Program.

A. Research and Dissemination Program.

ILD's involvement in particular fields (such as housing, manufacturing and transportation) is on-going and in advanced stages of study. These activities will be continued and new studies will be initiated with this funding. Some of the on-going work has already borne fruit in the form of policy and legal changes that are positively affecting economic development in Peru. Analysis is conducted by ILD staff and occasionally by consultants, who are organized in work circles or task force groups. These work circles concentrate on a particular field of study for a sustained period in order to maximize and follow through on the policy changes that may grow out of their efforts. The progress of each circle is monitored by the Research Committee which is comprised of the president, general manager, and the economic and institutional research directors.

The process employed by ILD is as follows:

1. Determine the nature of informality in whatever sector or activity being investigated by identifying and interviewing key formal and informal respondents in order to:
  - identify the factor markets and economic sectors in which informality occurs,
  - identify and study the reasons for the existence of that informal activity, and
  - quantify the extent to which it occurs.
2. Identify the laws and institutions that contribute to informality.
3. Refine and apply the methodology for measuring the costs of legal and institutional barriers to:
  - segregate some of the most significant costs, and analyze the interaction of these inefficiencies in the different markets and sector, thus clarifying the effects of one sector on the rest of the economy, and
  - develop a methodology generally applicable in developing countries.
4. Determine the existing cultural base on which new institutions should be based through:

- analysis of the extralegal norms developed by the informal sector to deal with the existing legal and economic institutions,
- acquisition of gender disaggregated data and analysis of social and economic impact of change on women as participants and beneficiaries, and
- conduct of comparative international research to identify similar problems and their solutions in other countries, and analyzing these solutions to determine whether they could be adapted to the situation in Latin America.

5. Develop alternative solutions, based on the above, that could remove or minimize the more disruptive structural barriers to economic and political participation, evaluating the effectiveness of the various alternative solutions relative to the existing situation.

6. Once the best solution is agreed upon, this is structured into a draft law or policy proposal for reform that is published and subjected to public scrutiny and debate. IID's experience in this matter shows that if the proposal is right it will be adopted by the authorities, and, if not, it will be enriched by the debate and returned to the drawing board for a comprehensive review and re-initiation of the process.

#### B. Outreach Program.

Outreach and dissemination activities will include promotion of the thesis and methodology of IID, dissemination of legislative proposals proceeding from the basic research, making available information on the informal sector outside of Peru, etc.

During Phase I, the IID program will focus on research, analysis, and policy formulation in the following areas related to the informal sector,

- legal and institutional costs in capital markets, the manufacturing sector, housing, agriculture, labor markets, and the transport sector,
- measurement of information sector activity,
- democratic decision making or rule making,
- institutional equilibrium through institutional checks and balances, and
- access and diffusion of information.

#### C. Regional Training Program.

Interest in the analytical process developed by IID has been widespread throughout the region, in part due to the publication of El Otro Sendero and many newspapers and magazine articles on the subject of the informal sector. An outcome of this interest has been requests for training by numerous groups in the region, IID will address these requests by undertaking training activities. The objective of this training is to

assist such groups to initiate efforts similar to those of IID in their respective countries. IID will make every effort to ensure that the number of female participants is optimized in all its training activities.

Depending on who is to be trained and what the objective of the training is, the training will take a number of forms:

1. Receipt of high level delegations who wish to familiarize themselves in a brief period of time with the IID program and to discuss the ramifications of IID's approaches within their national context.

2. Seminars for technicians who will be engaged in programs of economic institutional reform. These seminars will present theoretical underpinning and practical approaches to:

- measurement of informality and quantification of costs,
- identification of legal and institutional obstacles,
- formulation of proposals for reform, and
- public education.

3. In conjunction with these seminars, IID will develop manuals and other materials that could be used as texts and reference materials for persons interested in pursuing the IID approach.

4. Once programs are about to be initiated or are underway in other countries, IID staff will provide written or oral consultations or on site technical assistance.

5. Technicians from other countries will be selected to work with IID technicians in Peru to carry out field work to refine their understanding of the concepts.

**D. U.S. Coordinator.**

To maintain a continuous flow of intellectual and technical ideas to enhance its research, dissemination and implementation operations in Peru and to maximize its effects upon major donors operating within the region, IID will select a person or organization to coordinate its international activities in Washington, D.C. The IID U.S. coordinator will:

- facilitate IID's contact with the Inter-American Development Bank, the World Bank, the United Nations Development Program, and other institutions regarding projects and other opportunities to involve IID and its concepts in activities related to economic institutional reform,
- maintain a dialogue with U.S. and other academicians and scholars on the subject of economic institutional reform, this will complement an activity of the Bureau for Private Enterprise

to provide incentives for U.S. and other academicians to engage in research on informal sector topics,

- provide information to other groups engaged in informal sector studies and economic institutional reform in Third World countries,
- coordinate logistical arrangements for consultants who will work for ILD in Peru, the U.S., or other countries,
- coordinate the activities and flow of information to and from the Technical Review Committee, a panel of experts that will be established to review the research activities and outputs of the ILD, and
- liaise with USAID/Lima and AID/Washington on financial, informational, and logistic matters.

**E. Implementation Responsibilities.**

ILD will be the Recipient under the Cooperative Agreement. USAID/Peru is the authorized paying station, will serve as overall project manager, and will provide direct oversight to the program. Outside of Peru, AID/Washington will provide external coordination with other donors interested in the program and will participate in project reviews and evaluations.

1. Instituto Libertad y Democracia, Lima (Institute for Liberty and Democracy in Lima, or ILD). ILD is responsible for implementing the Cooperative Agreement.

- a. ILD will submit for USAID/Peru approval, at the beginning of the first year and in the eleventh month of each subsequent year, an Annual Implementation Plan of ILD's proposed duties for the coming calendar year. The Annual Implementation Plan will be a detailed description of the planned research and training programs, specific annual goals, objectives, outputs, planning timetables, reporting and evaluation schedule, procurement plan, staffing and hiring plan, detailed cash flow requirements, and other sources of financing. Such Plan will include gender disaggregated targets and strategies to achieve them, as appropriate, such that the percentage of women participants will be in approximate proportion to their traditional participation in the targeted activities or their proportion of the population, whichever is greater.
- b. ILD will develop a revenue diversification plan (see Covenants) within the first year of this Cooperative Agreement that enumerates goals, implementation plans,

financial targets, and likely sources of funds. This plan will reduce ILD's financial dependence on AID to less than fifty (50) percent of its annual budget by the fifth year of the project. The objective of this revenue diversification strategy will be to sustain a professional, credible organization that can attain the degree of financial self-sufficiency required to carry out core activities at the end of five years of AID financing.

- c. ILD will prepare semiannual reports (for the periods ending March 31 and September 30 of each year) or more often reports, if requested by USAID, in English on the specific activities given in the Annual Implementation Plan.
- d. ILD will participate in semiannual reviews with AID focusing on:
  - the status of activities being carried out under the program,
  - problems encountered that need resolution,
  - progress toward institutional development, financial self-reliance, etc.,
  - status of international program, and
  - other items of mutual interest and concern.
- e. ILD will participate in all Cooperative Agreement evaluations, financial reviews, audits, and incorporate appropriate recommendations and findings into ILD's organization and management.
- f. ILD will provide evidence that it has made progress towards developing significant international programs and an international institutional character.

2. USAID/Peru (USAD). The Mission will be the project manager and provide the day-to-day operational oversight. Among other functions, this will include the processing of all payment documents, conducting periodic program reviews and evaluation reviews, drafting appropriate correspondence and periodic reports on the Cooperative Agreement and the ILD's activities, approving budgets, operating plans, and financial reports, making decisions concerning conditions precedent and covenants, and maintaining effective liaison and contact with the ILD and AID/W.

3. AID/Washington (AID/W). The responsible office within AID in Washington shall be the Private Sector Office of the Bureau for Latin America and the Caribbean (LAC/PS). It shall maintain close contact with other U.S. Government agencies, international donor organizations, corporations, foundations, and other institutions concerning ILD's regional activities and related impact. AID/W shall participate in the semiannual project reviews and the threshold evaluation.

III. Evaluation, Conditions, Covenants, and Reports.

A. Threshold Evaluation and Last Three Years of the Cooperative Agreement.

Near the end of the first two years, AID --- acting through USAID/Peru and AID/W (IAC/PS) --- will conduct a joint evaluation with IID to assess the progress toward meeting the described purpose, goals, and objectives established in the Cooperative Agreement and the annual implementation plans. From that evaluation, and subject to the availability of funds, AID and IID will set forth mutually acceptable goals, timetables, and budgets for the activities and programs to be carried out during the three remaining years of the Cooperative Agreement.

The principal criteria that AID will utilize in assessing IID's program and related organizational growth will include, but not be limited to:

- the progress toward meeting the described purpose, goals, and objectives established in the Cooperative Agreement and the annual implementation plans,
- a diversified international financial base, and
- substantial involvement with public and private institutions outside of Peru.

The costs of independent participation in the Threshold Evaluation, if mutually agreed upon, are authorized as part of the activity's direct costs.

Based on the evaluation, IID will submit a revised implementation plan that will describe IID's activities and detailed budget requests for the last three years of the Cooperative Agreement and the Annual Implementation Plan for Year Three. Pending the approval of these plans, AID shall not obligate funds beyond Years One and Two.

B. Conditions and Covenants.

1. Conditions Precedent to Initial Disbursement. IID will submit in form and substance acceptable to AID:

- a. a copy of the first year Annual Implementation Plan with detailed budget,
- b. evidence that IID has developed and is utilizing, or has an acceptable phased plan for, financial and management improvements described in IID's proposal (Pages II-28 to II-30), and
- c. evidence that IID has made contractual arrangements for an independent audit of its calendar year 1988 financial statements. The audit shall be performed in accordance

with generally accepted auditing standards. The audit will be submitted to JSAID/Peru no later than September 30, 1989.

2. Conditions Precedent to Disbursement in Calendar Year Two. ILD will submit in form and substance acceptable to AID:

- a. a copy of the second year Annual Implementation Plan with detailed budget, and
- b. evidence that a Technical Review Committee has established and is reviewing the research activities and outputs of ILD.

3. Conditions Precedent to Subsequent Disbursement in Cooperative Agreement Years Three, Four, and Five. ILD will submit in form and substance acceptable to A.I.D.:

- a. evidence that ILD has made progress towards financial self-sufficiency, including compliance with Section II.E.1.b. (on revenue diversification), and
- b. a revised implementation plan, to document understandings reached during the first two years and in the Threshold Evaluation.

4. Covenants. IID agrees,

- a. to maintain funds received under this Cooperative Agreement in a bank account separate and apart from bank accounts and records of IID relating to any other funds made available to it,
- b. to maintain accounting records which classify and summarize clearly and separately and document fully all transactions relating to funds received under this Cooperative Agreement in such a manner as to permit the audit of all such transactions,
- c. to prepare annually a complete set of financial statements of ILD, prepared according to generally accepted accounting principles of the U.S. or Peru and provide for an independent auditor's opinion thereon based upon an audit performed by a U.S. or Peruvian firm of Certified Public Accountants acceptable to JSAID/Peru in accordance with generally accepted auditing standards. The auditor's report should also present the auditor's comments, findings, and recommendations as to:
  - (1) compliance by ILD with significant legal provisions and contractual stipulations, especially including those conditions and covenants prescribed by AID,
  - (2) adequacy of internal controls, financial management personnel, and the financial management system to reasonably provide accountability over resources owned or received from all sources and their custody or disposition, and

- (3) the appropriateness of management structure, procurement procedures, and personnel policies and practices, including remuneration of officers and employees;
- d. to implement within 30 days any and all recommendations for corrective actions or improvements made by ILD's independent auditor in his annual report or by the AID Inspector General in any report on ILD, or explain reasons for inability and alternative plan of action to solve the problem;
- e. that full-time employees covered under the Cooperative Agreement do not receive salaries from any other financial source, and
- f. that revenue diversification activities (Section II.E.1.b.) when financed by AID will conform to U.S. law and AD regulations concerning such activities.

C. Reports.

ILD shall provide USAID/Peru, these illustrative reports, and any others deemed necessary by AID:

- comprehensive semiannual program activity reports as part of the Annual Implementation Plan process. The form and content of the reports will be described in a letter from USAID/Peru,
- comprehensive and complete annual audited financial statements of ILD together with an independent auditor's opinion and report thereon as described in detail under Section III.B.4.c., to be furnished within forty-five (45) days after the end of ILD's fiscal year;
- a complete set of quarterly unaudited financial statements of ILD to be furnished within thirty (30) days after the end of each quarter.
- as needed, reports on problems, delays, or other adverse conditions that will delay, impede, or prevent ILD from carrying out the purposes and programs authorized in this Cooperative Agreement, and
- as part of the Annual Implementation Plan process, a report on fund raising and other revenue diversification activities aimed at broadening ILD's financial base.

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IV. Substantial Involvement Understandings.

The AID substantial involvement understandings of this Cooperative Agreement will entail the following activities by USAID/Peru,

- approving annual work plans, with particular reference to the research agenda and research work circles, progress toward developing a broad funding base, and developing and expanding the international program,
- approving advance/replenishment of funds,
- chairing the semiannual activity reviews in Lima in conjunction with the Annual Implementation Plan, involving AID/Washington, USAID/Peru, and ILD,
- deciding that conditions precedent have been met,
- monitoring the covenants,
- assessing the conclusions of the Threshold Evaluation and deciding how to proceed on programs and budgets for Years Three, Four, and Five, and
- USAID/Peru is the authorized paying office and all funds under this Agreement will be disbursed by JSAID/Peru.

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