



## Practice Standards for EFs: focus on Asset Management & Sustainability

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Project K: RedLAC – CAFÉ Knowledge for Action

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2

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The Latin American and the Caribbean Network of Environmental Funds - RedLAC was founded in 1999 and the Consortium of African Funds for the Environment – CAFÉ was established in 2011. The objective of the two networks is to strengthen EFs operation in their respective regions, by helping them to achieve excellence in their operations and practices, promoting innovative financing mechanisms and impact monitoring.

The “Knowledge for Action project – Project K” grew from the lessons learned after the final evaluation of the previous project, “RedLAC Capacity Building for EFs”, which was implemented by Funbio (the Brazilian Biodiversity Fund) on behalf of RedLAC, from 2010 to 2014, in close collaboration with the RedLAC secretariat. Project K is co-financed by the French Fund for the Global Environment (FFEM), Mava Foundation and the Global Environment Facility (GEF through UNEP).

The current proposed project aims at enlarging the EFs' portfolios of innovative financial mechanisms that take up the challenges of biodiversity conservation and climate change. In addition, it aims at strengthening capacities by providing support for EFs to adopt standards of excellence. The project is designed to provide the 40 RedLAC and CAFÉ EFs with an opportunity to test new financial mechanisms that they would otherwise be unable to test due to a lack of both resources and support for their ventures. In parallel, it is an opportunity to exchange and learn from the experience of other EFs and to document and disseminate their solutions.

This handbook was prepared for the 2nd workshop of Project K (Knowledge for Action project). It focuses on the development of evidenced-based norms, the Practice Standards, for use by EFs and those institutions and individuals who provide financial and technical support to them.

Chapter 1 of this Handbook will point out practical opportunities and approaches for how and when the Standards can be used.

Chapter 2 will be a summary of the workshop “Using the Practice Standards” that was held by Funbio in collaboration with CAFÉ, during CAFÉ Assembly which took place in Salima, Malawi, from October 10<sup>th</sup> to 12<sup>th</sup>, 2016.

As annexes of this handbook, we have the Executive Summary of the Practice Standards, followed by the agenda, list of workshop attendees and two case studies used in the workshop presented in Chapter 2.

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# Index

**05**

Chapter 1 – The Practice Standards and their Uses

**17**

Chapter 2 – Summary of the Workshop on Using the Practice Standards

**23**

Annex 1 – Executive Summary of the Practice Standards

**39**

Annex 2 – Agenda and List of Workshop Attendees

**41**

Annex 3 – Case Study on Financial Sustainability – Evaluating Two Different Project Opportunities

**47**

Annex 4 – Case Study on Financial Sustainability – Selecting an Investment Professional to Manage Endowment Capital

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## Chapter 1 – The Practice Standards and their Uses

The Practice Standards for Conservation Trust Funds were developed with very high hopes on the part of the community of practice – CTFs, donors, international conservation NGOs, foundations and other non-profit organizations, private supporters and committed individuals – that by codifying the way successful CTFs have evolved and the principles they followed, the entire community could benefit.

The Standards clearly state that:

- their use is voluntary and intended to serve as a tool for improving the design, management, and monitoring and evaluation of CTFs.
- they can be used, aspired to, or adapted to fit the particular needs of CTFs, donors and a variety of partners who support CTFs technically or financially.
- they can serve to achieve greater harmonization of international donor rules, standards and policies for CTFs, resulting in lower transaction costs for CTFs.

This Handbook will point out practical opportunities and approaches for how and when the Standards can be used.

“Conservation Trust Fund (CTF)” will be used throughout this Handbook to be consistent with the term used in the Practice Standards. However, the term “Environmental Fund” is also widely used, and use here of the term “CTF” can be understood to be the equivalent of “Environmental Fund”.

This Handbook uses the term “board” in a departure from the Standards which use the term “governing body”. The term “governing body” includes oversight committees and sub-boards that act in much the same way as a board. The preference for “board” in this Handbook is to clearly distinguish that body from another governing structure, the general assembly of members, which is part of the legal structure of many of the CTFs attending the workshop for which this Handbook is being prepared. “Board” therefore means the board of directors, management board or executive board that has overall management responsibility for the CTF.

## Who should Adopt the Standards?

The Standards are intended for use by a diverse group of stakeholders: CTF governing bodies and management; donors; technical partners and experts involved in design, in fundraising, in governance and management support activities and in performance evaluation; governments and others who just want to know more about what has proven to be a successful option for sustainable financing for conservation.

The Standards cover six fundamental areas of interest to CTFs:

- Governance (the composition, functions and responsibilities of a CTF governing body or bodies and the content and role of governing documents)
- Operations (strategic planning, grant making; interactions with government, and partnerships with other organizations)
- Administration (organizational roles and responsibilities, operations manuals, use of financial resources and auditing)
- Asset Management (the components of investment strategies, fiduciary responsibilities and relationships with various types of investment professionals.)
- Resource Mobilization (fundraising as well as managing payments for environmental services (PES), compensation funds, offset payments, etc; mobilization and management of additional funding sources to enhance overall financial sustainability of biodiversity conservation, particularly protected area (PA) systems.)
- Reporting, Monitoring & Evaluation (conservation impact monitoring; frequency, format and content of technical and financial reporting to donors; and dissemination of results.)

Taken together, these areas support both global management as exercised by a board and day-to-day management as carried out by a chief executive (whether a director, executive director or executive secretary) and his or her staff.

Boards should be familiar with the Standards because they not only provide insight into governance, but also offer the board an instrument to carry out its responsibility of overseeing day-to-day CTF management. Having the board formally recognize the Standards or validate them as the institution’s reference for assessing effectiveness and efficiency facilitates using them to plan and execute governance and management actions.

Finally, the Standards were not intended to be “set in stone” but to continue to evolve and be periodically updated by the CFA. Although it is possible that they could eventually evolve into a system of voluntary “certification” standards for CTFs, they are not designed to serve that purpose in their current form.

## The Practice Standards and the CTF Cycle

While the Standards have been neatly grouped into topic areas, each stage of a CTF’s cycle – creation, operation, evaluation - draws on key principles from several areas of the Standards. This section will show how to use the Standards when designing a CTF, as a reference when managing governance responsibility and day-to-day operations, and as a basis for evaluations of CTF performance. Annexes 1 and 2 of the Standards provide checklists for principles to consider when creating a CTF and when performing an evaluation.

### Creating a Conservation Trust Fund/ Environmental Fund

The process of designing, registering and putting in place the people and management tools to make a CTF operational is relatively complex, but it is probably the best understood of all parts of the cycle now that more than 50 CTFs have been created in Africa, Asia and Oceania, Europe and Latin American and the Caribbean.

## CTF Creation

### 1. Designing and Registering the CTF

Design begins with consideration of the legal framework that will regulate the way the CTF can do business in a clear and supportive way. Governance Standard 10 establishes the three elements that must be present in an acceptable legal framework. That framework:

- ensures the CTF’s independence from government;
- has clear and well enforced laws concerning private non-governmental organizations (including foundations or trusts); and
- does not subject the CTF to paying substantial taxes.

In cases where these elements are untested, not clearly present or clearly absent offshore registration,

i.e. registration outside the country where the CTF operates, has been chosen instead. Offshore registration is also an option for a CTF that brings together multiple countries.

Once a review of the legal framework gives a positive conclusion and the type of organization to be created is clear, design concentrates on the governing documents and the choice of individuals who will be involved in governance.

Governance Standards 1 and 2 address the fundamental elements included in governing documents. These are:

- a well-defined purpose or objective(s);
- definition of a board's composition to ensure that its members will have a high level of independence and stakeholder representation; and
- definition of the powers and responsibilities of the governing body (or bodies) that will permit them to carry out the purpose or objective(s) of the CTF in an effective and efficient manner.

A *well-defined purpose or objective(s)* will have sufficient focus for the CTF to achieve what is envisaged at the time of creation, and also allow some flexibility should future opportunities arise. *Independence* from government, or any dominant party, means the governing body members collectively will make and be accountable for decisions taken. The governing document defines the *powers and responsibilities of governing body members* that are required by law and support effective actions to achieve the stated purpose and objectives. More detailed governing rules, including processes and procedures for carrying out the obligations of a governing document, often appear in by-laws.

Governing body members exercise powers collectively and have responsibilities in an individual capacity. A variety of skills and experience are required, as well as commitment to participate fully. Governance Standards 3, 4, 5, 6 and 7 and Asset Management Standard 6 address important understandings and skills of members as well as the principle that changes in the members should be managed as an opportunity to bring in new thinking, but ensure some experienced members remain for continuity. A governing body should have:

- members willing to meet at least three times a year, or more if required;
- at least one individual with fundraising skills;
- members who understand fully their fiduciary responsibility;
- at least one individual with expertise or experience in investing in either local or global financial markets;
- training on key investment concepts for informed decisions when exercising investment management responsibilities; and
- terms of office that are staggered in time and limited in number.

## 2. Putting in Place the People and Tools for an Operational CTF

The second phase of the creation process focuses on making the CTF operational by putting the people and tools in place to carry out the CTF's business. Having a chief executive actively involved at the time management tools are developed can result in him or her acquiring a deeper understanding of and commitment to the business.

**“While the Standards have been neatly grouped into topic areas, each stage of a CTF’s cycle – creation, operation, evaluation - draws on key principles from several areas of the Standards.”**



The Chief Executive and Staff. Governance Standard 8 and Administrative Standard 1 provide for the board to recruit, using a competitive process based on clear and complete terms of reference, a full-time chief executive (or fund manager for sub-funds) to manage daily operations. The chief executive and staff should be supported with an appropriate organizational structure, adequate financial resources and a level and quality of human resources to allow efficient and effective performance. Administrative Standard 5 establishes that careful use of financial resources requires that appropriate quality goods, works and services needed for the CTF to conduct its everyday business be obtained through processes and practices that are efficient, cost-effective and transparent.

To support the work that will be carried out by the chief executive and his or her staff, Administrative Standard 4 indicates that one or more manuals will set out the internal regulations of the CTF in the form of policies, procedures and practices for administrative, financial and operational activities.

Core Business. For the purpose of the Practice Standards, the core business of a CTF is to use the resources it mobilizes for making grants. Operations Standards 4, 5, 6, 7 and 9 set out principles that are generally incorporated in the previously mentioned manual and, where relevant, legal agreements with the grantees. Key principles support:

- a well-defined and competitive grant award process be used to select high quality grant proposals in a timely manner;
- grantees are selected through evaluation of key written information and direct questions to ascertain their capacity for successful planning, execution, monitoring and reporting;
- the grant cycle concludes with the signature of a contract that sets out all important understandings and obligations regarding the financing the CTF will provide;
- grantees should contribute a portion of project or activity costs, with the CTF providing guidance on what types and percentage of contributions are acceptable; and
- in the interest of careful use of the CTF's financing, grantees should themselves apply effective, efficient and transparent acquisition processes and practices such that appropriate quality goods, works or services are obtained at the best value for price in the market. The grantees own practices should be ascertained at an early stage in the grant award cycle and any agreement on practices is recorded in the grant contract signed with the CTF.

CTF Management should be able to provide tangible evidence of impact to the board and help the board promote the CTF to donors, other partners and stakeholders. The CTF should put in place systems and ensure manuals provide for monitoring and evaluation processes, indicator development and analysis.

Reporting, Monitoring & Evaluation Standards 6 and 8 lay the groundwork for incorporating M & E in the CTF's business practices by

- Providing to grantees clear reporting templates, frameworks and information requirements for the purpose of monitoring and evaluating grant performance in achieving planned outputs and outcomes;
- CTF Staff monitoring of grants using indicators and measures agreed upon in contracts or their required monitoring plans.

With regard to the CTF's own reporting, RM&E Standard 2 establishes the principles that agreements between the CTF and its donor set out specific formats and information requirements, procedures and timing for technical reports and that donors work among themselves to harmonize reporting requirements in the interest of efficiency and cost reduction.

Strategic and Financial Planning. Prior to and during creation of the CTF, considerable thought is given to matching the institution's objectives to conservation needs and its initial resources to a stream of funding that will achieve financial sustainability. Early in its operational life, a board begin strategic and financial planning that looks

at future challenges and responses by the CTF and what resources the institution will need for its own development and to respond to those challenges. Operations Standard 1, Resource Mobilization Standard 1 and Reporting, Monitoring and Evaluation Standard 7 all help to define this important work by:

- setting the board on a path to translate the CTF's broad vision and mission statements into specific goals, objectives and activities;
- tying fundraising to the general strategy through a resource mobilization strategy or action plan; and
- providing for monitoring and evaluation of the strategic and financial plans themselves.

Preparing to Manage Assets. CTFs also have as their purpose the efficient management of financial assets in a variety of form as endowments, sinking funds or even revolving funds. A CTF is not truly operational until it has the financial assets needed to carry out its core business, and it should prepare for receiving them by ensuring there is a policy and guidelines that spell out how they will be managed and, when necessary, by obtaining professional services to assist with carrying out the policy and guidelines.

Asset Management Standards 1, 2, and 5 guide the preparation and approval of the investment policy and guidelines. They provide for:

- an investment policy that is clear and comprehensive when setting the core principles that will be applied in managing financial assets;
- management of the portfolio of assets in accordance with investment guidelines that set out the specific parameters to be applied by the chosen investment professional(s);
- the policy and guidelines, as well as the process for selecting an investment professionals and the reports and recommendations of those professionals, must be approved by the board;

Asset Management Standards 4, 7 and 8 support the choice of employing an investment professional. The choice is carried out by:

- the board delegating responsibilities related to investing the CTF's assets to a committee of the governing body and/or investment professionals;
- the board assessing its existing investment capacity, identifying what types of investment professionals it may require and selecting them through a competitive process and from among investment industry service providers of recognized quality; and
- contracts for services to be provided by investment professionals that state in a clear and

comprehensive manner the services to be provided, the objectives of the services, the costs of delivering the services and the responsibilities of both the service provider and the CTF.

## Managing with the Standards

Preparation of "high level" management tools - manuals, strategic and financial plans, an investment policy and guidelines - begins and is often completed at the time a CTF becomes operational, i.e. has its chief executive, staff and office in place and, in most cases, receives its capital. It is not enough, however, to just have those tools, CTF chief executives need to ensure that they are being applied and kept current. A second tier of management tools can be developed to manage in accordance with the Standards and enhance governance and daily effectiveness and efficiency. Some suggestions for these appear below:

## Managing Governance and Compliance

The following can help the board manage its own operations and the organization fulfill its legal obligations:

- Board by-laws may need to be prepared to set out governing rules that are too detailed to appear in the governing documents. By-laws can also include processes and procedures for carrying out the obligations of a governing document. *Definition of Governing Documents*
- Board appointed committees should have terms of reference, simple rules of procedure and a work plan that clearly state the responsibilities assigned by the board, how the committee operates and what will be accomplished. *Governance Standard 4*
- A conflict of interest policy covering not only the board, but staff also is developed and included in by-laws (for the board) and the operations manual (for staff) *Governanc Standard 7*. The policy can be supported by a Register of interests that records a real or potential conflict of interest that is generally known or of which the board or management has been informed.
- A compliance list covering all applicable laws and regulations, legal agreements between the CTF and donors, and with the CTF's own governing documents assists with monitoring obligations. The compliance list should include reports the CTF is required to submit to government agencies in the country where the CTF is legally registered and the countries where the CTF operates or has investments. *Governance Standard 9 and R, M & E Standard 3*

### Elements of a compliance list:

- The authority that has created the requirement or which must receive proof of compliance
  - The document to be provided or action that needs to be taken
  - The deadline or time limit of the obligation
  - The frequency with which the requirement must be met
  - If special forms are required, where these can be obtained
- 
- An audit by independent external auditors who apply standards that are consistent with internationally accepted accounting standards give assurances to the board and external parties that monies of the CTF are accounted for accurately and used for intended purposes. Board members fulfill their fiduciary duty by developing an understanding of the financial statements, discussing and approving the audit. *Administrative Standard 6*

### Making Strategic Planning Effective and Operational Processes Efficient

To guide day-to-day operations, the chief executive and his staff generally prepare and monitor an operating or business plan, annual work plan and budget that are all consistent with the Strategic and Financial Plan. *Operations Standard 1*

Web supported grant-making that, at a minimum, allows grant seekers to obtain all information on calls for grant proposals, grant proposal forms and award results but which can also accept proposals and queries can lower costs and make the process and communication more effective. *Operations Standard 5*

While it is a major investment on the part of a CTF to design them, using standardized forms for grantees to report on their use of the monies they receive and progress with activities and monitored outcomes can make review of the reports and their consolidation for reporting purposes a much more efficient task. Ensuring the forms request only necessary information and that there are clear instructions on what is expected in each section can contribute to better quality reports. Incorporating reporting into the web-supported grant system would realize further benefits. *Operations Standards 7 and 9 and R, M & E Standard 9*

### It's all about the Budget

The volume and allocation of a CTF's resources must be coherent with strategic and institutional objectives and allow the chief executive and his or her staff to carry out the many and diverse day-to-day tasks that serve the institution and its core business of achieving positive conservation impact. The budget becomes an effective management tool when it is presented transparently and in a way that facilitates analysis. A budget presentation showing spending categories (salaries, rent, utilities) as these relate to activities (support to the board, fundraising, programs under management) should enhance the board's understanding and aid decision-making. *Administrative Standards 2 and 3*

### Reporting, Monitoring & Evaluation

The work of the chief executive and his or her staff, as well as board meetings, will be carried out more efficiently if agreement can be reached on the format, content and timing of reports that the board wishes to receive. *R, M & E Standard 5*

Data produced by monitoring grants should be stored in a system that allows for analysis and reporting to the board, donors and external stakeholders and for use by evaluators. *R, M & E Standard. R, M & E Standard 9*

The committee responsible for overseeing investment management undertakes a review of investment management performance at least quarterly and, in many cases, monthly. The chief executive supports the committee and the board by producing reports generated by a monitoring system that records key elements of portfolio performance. *Asset Management Standard 9*

### Resource Mobilization

The initial strategic and financial plan written for a newly operational CTFs may include an early strategy for raising funds, but a separate and focused Resource Mobilization Strategy/Plan should be prepared as soon as time and resources can be devoted to the required financial planning and research. The RM Strategy/Plan can also include analysis of the opportunities for the CTF to serve as the mechanism for disbursing PES, user fees, REDD+, climate adaptation funding, biodiversity offset payments, environmental compensation and fines. *Resource Mobilization Standards 1, 2 and 5.*

A policy for screening and determining which donor contributions and conditions should be approved concurrently with the RM Strategy/Plan, unless the principles are already included in the governing documents or manuals. *Resource Mobilization Standard 3*

## Using the Standards for Assessments and Evaluations

Formal assessments or evaluations are often requested by donors at the time of a new capital contribution, when a CTF is selected to manage a new fund, program or project, in accordance with a specific agreement requiring periodic evaluations or at the close of a donor-funded program or project. Evaluations may look at compliance with donor agreements, achievement of program or project objectives and whether the governance and management of the CTF are effective and efficient. CTFs may also decide to carry out self-assessments either at the board or the management level in the interest of improving the effectiveness and efficiency of operations.

If a CTF was created in accordance with the Standards and efforts are made to manage using the Standards when appropriate, it is in the interest of a CTF to ensure the Standards are referred to in the terms of reference of an evaluation. This way, the CTF is prepared and the evaluator has a clear basis for concluding on the CTF's performance.

Based on the checklist of Annex 2 of the Practice Standards, the following are proposed to guide an evaluation. It should be kept in mind that an evaluation will need to make judgments about the qualitative application of the Standards. For example, it is not enough to have a well-written and complete investment policy and guidelines. An evaluator will need to determine whether it was followed, what results it produced and if it was adjusted when conditions required it. The sections below provide a fairly comprehensive list of questions that are typical of evaluations and internal or external assessments.

### Evaluating the Governing Framework and Governance Documents

Has the CTF been able to operate such that no one stakeholder exercises undue power in the outcome of decision-making and without interference or undue influence of any including the government? *Governance Standards 2 and 10*

Has the CTF used its assets only for the purposes stated in its governing documents? *Governance Standard 1*

Does the CTF have a "compliance list" including reports and schedules? Does it monitor those requirements on a regular basis and keep the list up-to-date? Does it (1) meet obligations of applicable laws and regulations; (2) comply with its own governing documents? (3) fulfill obligations of legal agreements between the CTF and donors? *Governance Standard 9 and Reporting, Monitoring & Evaluation Standard 3*

Does the CTF have a comprehensive conflict of interest policy that defines conflict of interest and allows it to identify, avoid and manage potential and actual conflicts of interest to reduce its exposure to reputational risk? Does



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the CTF have a register of interests? Have Directors or staff declared any conflicts of interest, and if so, were they handled in accordance with the conflict of interest policy? *Governance Standard 7*

#### Evaluating the Governing Body

Have board members been appointed in accordance with the rules set forth in the CTF’s governing document? *Governance Standard 1*

Does the governing body operate with a high level of autonomy, competency, stakeholder representation, and commitment to achieving the CTF’s mission? *Governance Standard 2*

Have the rules for selecting governing body members been followed when the body renews its members. Are terms staggered and have members been changed in accordance with the governing documents? *Governance Standard 3*

Have specialized committees been formally created? Is each committee’s mandate written? Does each committee keep records of its decisions? *Governance Standard 4*

Does the board meet at least three times per year and are accurate meeting minutes are kept to record all decisions? *Governance Standard 5*

Do board members understand their fiduciary responsibilities and either have or acquired the competence necessary to carry them out. Have board members received relevant short training including training by people with legal, financial and investment expertise. *Governance Standard 6*

#### Evaluating Strategic Planning and Partnering

Was a strategic and financial plan prepared with participation of the governing body and CTF staff, and did it incorporate the results of discussions with donors, government, partners (private and non-profit sectors, community leaders and academics) and potential grantees, as appropriate? Does it identify the specific actions and resources needed to achieve the goals that move the CTF’s mission forward? *Operations Standard 1*

Is the Strategic Plan reviewed periodically and adjusted in light of changing conditions? *Operations Standard 1*

Are performance indicators are used to link use of resources to achievement of strategic objectives. *Administrative Standard 2*

Does the CTF also have operating plans, annual work plans and budgets that are consistent with the approved strategic and financial plan and are they monitored and updated regularly? *Operations Standard 1*

Have opportunities for collaboration with different levels of national government on achieving conservation priorities have been identified and pursued? *Operations Standard 2*

Is local government informed and involved in the planning of sustainable development activities when grants are made in support of communities living adjacent to protected areas? *Operations Standard 2*

Are partnerships formed at the national or international levels with key actors in donor agencies, businesses, non-governmental organizations, communities and research and academic institutions have shown positive results for conservation? *Operations Standard 3*

Do strategic and financial plans include the development of collaborative relationships as a means of achieving the CTFs objectives? *Operations Standard 3*

### Evaluating Grant-making Practices

Is there a well-defined grant award process used to select high quality proposals in a timely manner through competitive means? Are the steps of the grant cycle, grantee eligibility criteria, guidance for submitting proposal documents and the criteria that will be used for evaluating proposals made public to ensure that all potential grantees have access to the same information? *Operations Standard 5*

Are timely notification provided to all applicants that do not receive funding? Is feedback made available on an equal-opportunity basis to all rejected applicants. *Operations Standard 5*

Are grantees selected through evaluation of key written information about the entity or individual seeking a grant and through direct questions that help to assess whether a grantee has the means required for successful planning, execution, monitoring and reporting of grant-financed activities? *Operations Standard 4*

Are cost-sharing arrangements encouraged through which grantees contribute a portion of the project or activity cost, or raise funding from others? If so, are grantee's own or solicited contributions monitored and taken into account when evaluating grantee performance? *Operations Standard 7*

Are grantees required to apply effective, efficient and transparent acquisition processes and practices such that appropriate quality goods, works or services are obtained at the best prices for value in a given market, and are the grantees practices determined at the earliest stage of the grant cycle? *Operations Standard 9*

Does any contract awarding the grant set out all important understandings and obligations related to the financing the CTF will provide? *Operations Standard 6*

Do instructions to grantees and grant contracts provide for clear reporting templates, frameworks and information requirements for monitoring and evaluation of grant performance to achieve planned outputs and outcomes? *Reporting, Monitoring & Evaluation Standard 8*

Do CTF staff and the grantee monitor grants using indicators and measures agreed upon in the grant agreement, or its required monitoring plan? Are the indicators used specific, measurable, attainable, relevant and time-bound (SMART)? *Reporting, Monitoring & Evaluation Standard 6*

*Reporting, Monitoring & Evaluation Standard 6*

Do grant contracts require grantees to use the CTF's reporting templates and frameworks and specify information requirements for monitoring and evaluation of the grant performance to achieve planned outputs and outcomes? *Reporting, Monitoring & Evaluation Standard 8*

Do CTF staff (and/or independent evaluators) perform due diligence and monitor grantees' progress towards achieving outputs and outcomes. *Reporting, Monitoring & Evaluation Standard 9*

### Evaluating Management and Administration

Is the performance of the Chief Executive reviewed by the board and evaluated annually? *Governance Standard 8*

Is the Chief Executive or a Fund manager responsible for hiring other staff based on written job descriptions and budgets that have been approved by the board? *Governance Standard 8*

Are the respective roles of the board and chief executive (or between a Fund's governing body and its Fund Manager) clearly specified in the governing documents and/or an operations manual, in order to minimize the likelihood of any conflicts between them or inefficiencies in managing the CTF? *Governance Standard 8*

Are the CTF's organization and resources adequate for the chief executive and staff allow them to perform effectively and efficiently, i.e. do they have (1) a clear mandate for the roles and responsibilities they carry out, (2) the skills needed to carry out their assigned responsibilities, and (3) an annual budget that is adequate for carrying out the annual work program? *Administrative Standard 1*

Are the Chief Executive and staff recruited on a competitive basis in accordance with clear and complete terms of reference/job description for their positions? Are TOR reviewed and updated periodically? *Administrative Standard 1*

Does Management create opportunities for professional growth of key staff, support reasonable remuneration that is competitive in the national marketplace and evaluates staff performance regularly? *Administrative Standard 1*

Does the Chief Executive or Fund Manager present a proposed and executed budget that transparently portrays management expenses in a way that allows the board to understand and analyze the full costs of delivering grant programs and any other strategic or institutional objectives? *Administrative Standard 2*

Have reporting, monitoring and evaluation been designed to support informed decision-making of the board about the performance and functioning of the CTF as an institution? *Reporting, Monitoring & Evaluation Standard 5*

Is an Annual Report prepared and distributed to donors and key stakeholders, and made available to the general public? *Reporting, Monitoring & Evaluation Standard 10*

Does the CTF comply with any agreed ratio that compares management expenses to spending on the grant program? Are the rationale for any such ratio and the basis for its calculation well defined? *Administrative Standard 3*

Do one or more operating manuals with up-to-date policies, procedures and practices guide the day-to-day management of the CTF or the Fund? *Administrative Standard 4*

Are guidelines on cost-sharing are spelled out in the manual covering grant-making? *Operations Standard 3*

Are goods, works and services needed to carry out everyday activities are obtained through processes and practices that are efficient, cost effective and transparent; assure the appropriate quality of goods, works and services, and aim to obtain the value for price in the market? *Administrative Standard 5*

If the CTF has execution responsibility for one of the programs or projects it also manages, does it apply the same standards to the service it provides for grantees as it applies to the service when it carries out that service for its own purposes? *Operations Standard 10*

Is an annual audit is performed by independent auditors who apply standards that are consistent with international audit standards? *Administrative Standard 6*

## Evaluating Reporting, Monitoring & Evaluation

Are the CTF's operating manual(s) is/are clear and explicit about the different types of reports that are prepared, as well as the specific audiences and purposes of the reporting? *Reporting, Monitoring & Evaluation Standard 1*

Does the CTF monitor and evaluate its programs in relation to the CTF's mission and its strategic plan, and in relation to national-level and international-level conservation indicators, targets and strategies? *Reporting, Monitoring & Evaluation Standard 4*

Is an independent evaluation carried out every 3-5 years and its results are reviewed by the CTF board which decides on how recommendations will be implemented? *Reporting, Monitoring & Evaluation Standard 4*

Do the CTF and the grantee monitor grants using agreed indicators and measures that are incorporated into the grant contract, or a required monitoring plan? *Reporting, Monitoring & Evaluation Standard 6*

Do monitoring and evaluation systems exist to support evidence-based reporting of conservation impacts? *Reporting, Monitoring & Evaluation Standard 7*

Do CTF staff (and/or independent evaluators) perform due diligence and monitor grantees' progress towards achieving outputs and outcomes? *Reporting, Monitoring & Evaluation Standard 9*

## Evaluating Management of Invested Assets

Is there a clear and comprehensive investment policy that sets out the core principles the CTF applies for managing its assets? Is it reviewed and updated regularly? *Asset Management Standard 1*

Is a CTF's investment portfolio managed in accordance with investment guidelines that set out the specific parameters to be applied by the investment management consultant, financial advisor and/or the investment manager(s)? *Asset Management Standard 2*

Are the investment guidelines reviewed with the investment management consultant or investment manager no less than once per year? *Asset Management Standard 2*

Does a CTF that selects and monitors its own investments, have a system in place to monitor purchases, sales, maturity dates, redemptions, etc. and provides quarterly performance reports to the governing body or its committee responsible for investing? *Asset Management Standard 2*

Do the investment policy and guidelines incorporate measures that serve to lower the risk that capital would need to be spent to meet distribution requirements? *Asset Management Standard 4*

Does the board review and approve the investment policy, investment guidelines, the process of selecting an investment management consultant and/or investment manager(s) and reports on investment and financial consultant and/or asset manager performance? *Asset Management Standard 5*

Do the governing body, investment committee and chief executive benefit from a transfer of knowledge by the CTF's investment management consultant or investment manager(s) as part of the review of the investment policy and guidelines and performance reports? *Asset Management Standard 5*

Did the CTF select its investment professionals through a competitive process and from among investment industry service providers of recognized quality? *Asset Management Standard 7*

Has the CTF has used a two-part process that initially qualifies a small number of firms and then requests the qualified firms to submit complete requests for proposals? *Asset Management Standard 7*

Do contracts for services to be provided by investment professionals state in a clear and comprehensive manner the services to be provided, the objectives of the services, the costs of delivering the services, and the responsibilities of both the service provider and the CTF? *Asset Management Standard 8*

Are regular reviews of investment management performance carried out by the investment committee? by the Board? *Asset Management Standard 9*

## Evaluating of Resource Mobilization Strategy and Practices

Is a resource mobilization strategy is in place to diversify and multiply the CTF's short-term and long-term sources of financing? Is it reviewed or updated every 2-3 years? *Resource Mobilization Standards 1 and 2*



Does a strategy or action plan exist for raising long-term capital as well as shorter-term funding for particular projects or programs? *Resource Mobilization Standard 2*

Does the CTF has a policy for screening and determining which donor contributions and conditions they will accept? *Resource Mobilization Standard 3*

Has the CTF pursued opportunities for using funds from particular donors or government sources as a way of leveraging additional resources? *Resource Mobilization Standard 4*

Have opportunities have been identified, analyzed and utilized that would allow the CTF to act as the financial and institutional mechanism for disbursing PES, user fees, REDD+, climate adaptation funding, biodiversity offset payments, environmental compensation and fines, in order to support activities that are aligned with the mission of the CTF? *Resource Mobilization Standard 5*

Do the board and chief executive coordinate with, and seek the support of, national government ministries and politicians in mobilizing additional financial resources for the CTF from national governments and international donors? *Resource Mobilization Standard 6*

Is the CTF able to show potential donors the role that the CTF it plays in providing long-term financial support for the national system of protected areas and/or for environmental action plans and programs? *Resource Mobilization Standard 7*

A photograph of two deer in a dry, wooded landscape. The deer are standing in a field of dry grass and brush, with trees in the background. The lighting is warm, suggesting late afternoon or early morning. The deer on the right is looking towards the camera, while the one on the left is looking slightly away.

## Chapter 2 – Summary of the Workshop on Using the Practice Standards

The workshop on Using the Practice Standards took place in Salima, Malawi from October 10 to 12, 2016. The workshop agenda and the list of workshop attendees are attached as Annex 2. Workshop documentation included PowerPoint presentations covering the main topics and two Case Studies.<sup>1</sup> A special presentation was also offered that was aimed at supplementing the Standards for Asset Management.<sup>2</sup>

Part 1 of this chapter summarizes general presentations made on the first day of the workshop and Part 2 will summarize the case studies and presentation, and highlight the questions raised by participants.

### Part 1 – Summary of Presentation

#### Presentation 1: Objectives, Approach and Subject Areas of the Practice Standards

Participants were introduced to the objectives, approach and subject areas of the Practice Standards to provide a general background and ensure they understood that the Standards were conceived, not as “best practice” or “how to” guidelines, but:

<sup>1</sup> Case Study 1 – Financial Sustainability, facilitated by Monica Ferreira of FUNBIO, examined how price, cost and value can be taken into account when a CTF considers various projects or programs it may wish to manage. Case Study 2 – the Dilemma of the Smiling Bonobo Foundation, facilitated by Kathy Mikitin, required a critical analysis of a problematic process for asset manager selection.

<sup>2</sup> Best Practices for Foundations and Endowments was presented by Jason Hamlin, UBS Arbor Group.

- as a tool for improving the design, management, and monitoring and evaluation of CTFs; and
- with the intent to increase the understanding of how CTFs function among members of the community of practice and a broader audience that might be interested in creating or providing financial and technical support to this group.

Adoption of all or part of the Standards is intended to be voluntary. There has been some discussion of certifying CTFs that do adopt them, but this is still under consideration.

Each Standard has four parts:

- The Standard itself – which is intended to convey a “universal principle”
- The Reason for the Standard – how the Standard relates to effective and efficient operation of a CTF
- Practical considerations – based on practices successfully used by a representative number of CTFs
- Evidenced by – what common usage documents establish whether and how a particular Standard is being applied.

Finally, the original Practice Standards cover six areas that are key to CTF operations: Governance; Operations; Administration; Reporting, Monitoring and Evaluation; Asset Management and Resource Mobilization. Not only are other areas to be taken up in the future, but it is hoped that feedback from users will be used to revise and improve the current Standards.

### Presentation 2: Adopting the Standards

While the Standards are intended for use by a broad group of stakeholders, it is particularly important that the following bodies incorporate their use:

- Boards – *formal adoption by the board allows a CTF to present the Standards as recognized by its governing body and to allocate resources to ensure they are incorporated into governance and management practices.*
- Management – *incorporating a reference to the Standards in an operations manual recognizes them as part of internal regulations. The chief executive is well-placed to encourage and educate the board in the use of the Standards.*
- Donors – *a policy or management directive in the donor organization can reduce uncertainty, guide staff and management and reduce transaction costs by establishing ex ante the principles and a design framework the donor can support.*

Furthermore, when the above parties subscribe to the Standards, there is a common and tested basis on which the board can base its global management activities, discussions with donors are facilitated and the definition and carrying out of internal and external assessments are made easier.

### Presentation 3:

#### The Practice Standards and the CTF Life Cycle

This presentation of this topic closely followed the section of Chapter 1 with the same title. Because that chapter treats in detail the use of the Standards at the time a CTF is created, as part of ongoing CTF management and for the purpose of assessments and evaluations, a summary of the presentation will not be provided here.

### Presentations 4 and 5:

#### Walk-thru of the Practice Standards

This topic was covered in two sessions:

- The initial session reviewed five subject areas (Governance; Operations; Administration; Reporting, Monitoring and Evaluation; and Resource Mobilization). In each subject area, emphasis was given to those Standards that were not covered by the Life Cycle presentation or which had been identified by the participants in their workshop application as topics of relevance and particular interest.
- The second session focused entirely on the Standards for Asset Management. Standard 7 which applies to the selection of investment professionals was reviewed to prepare participants for work on Case Study 2. Asset Management Standards 2, 3 and 4 which cover the principles embodied in an investment policy and guidelines were also reviewed as background for the presentation on Improving Portfolio Performance.

Discussions on the general presentations covered a variety of topics:

More information should be made available on the **impact of CTFs in Africa**. Most CTFs begin with limited resources and need to make their presence felt. Presenting a holistic operational plan, involving all donors, to the board helps to demonstrate for that body the role and importance of the CTF’s activities. Having the full picture of financial flows to PAs is important. FAPBM, for example, tracks its contribution for the PAs to which it contributes, and is aware that its financial participation varies from 12% to 80%.

With regard to Operations Standard 1, a question was asked on **the appropriate horizon for a strategic plan**. The first strategic plan of a CTF could have a relatively short horizon, possibly only three years, as the CTF in its early life is focused on putting its core business in place, building partnerships and searching for new fundraising opportunities. Following that, a five-year horizon is pretty standard, but after three years a review of progress and consideration of revisions is generally required.

An additional question in this area was **who is best placed to write the strategic plan** - a consultant or the CTF itself. Either way will work depending on whether the chief executive has the resources (staff and time) to undertake the work. In either case, the board should play an important role in defining the key areas the CTF will be pursuing and stakeholders should be consulted on challenges the CTF could address. Training for board members is useful before beginning the planning exercise, and if there is a consultant, that individual's role should be to facilitate the process of plan preparation.

Governance Standard 3 states that **board members are selected based on competencies and commitment to contribute**. How can this be ensured, especially if ministerial appointment is required. It is generally accepted that the board itself is responsible for renewing its members since it should have no other interest than having the best persons who will work well within the group. In the DRC, for those board members the Government has the right to name, the Government must propose three candidates, and the board chooses from among them.

Governance Standard 4 mentions two commonly seen committees, but **what other committees might be useful, what work can they do and can they be paid?** As stated in the Standards, a finance or investment committee and a scientific and technical committee often advise the board because those areas require specific expertise. In terms of permanent committees, the following are also common:

- An operations or grants committee often works with the chief executive to prepare the program that will be considered by Board.
- An audit committee reviews the audit report and may work with any internal audit unit to define areas of risk and an audit program.

Ad hoc committees may be named for a relatively short duration to carry out a specific task such as recruiting a chief executive, revising staff benefits and rules, preparing a special strategy to address a problem or new business area. Committee members are not paid, but if

there is a policy to reimburse board members for costs incurred, the board can extend that policy to committee members, even if they are external to the CTF.

A question was raised whether the **auditor selection** could not be carried out by the unit headed by the chief executive, since the board can become too involved in the process and some board members are located outside the country. It was explained that the financial audit is an audit of management and the audit reports to the board for reasons of independence. While the chief executive's staff may manage a competitive selection process agreed with the board, the board must be responsible for the final choice. Participants offered ways in which the process could be made more efficient. Virtual meetings offered flexibility. An audit committee could be named to take all but the final decision. Some boards have an "executive committee" that can facilitate processes and decision-making.

The Resource Mobilization Standards do not address how to engage board members and follow-up on fundraising efforts. CTFs need to develop knowledge of **fundraising best practice**. This is an issue for all CTFs and the need for additional work in this area and the identification of expertise is critical. However, the Standards are not intended to provide best practice advice, so this badly needed support will need to take another form.

**Asset Management Standard 6** states that a governing body "has at least one director/trustee who is a qualified professional with knowledge and experience in one or more of the fields of finance, business or economics", but what if there is no director who meets that description? It was generally agreed that the qualifications and experience of the investment committee is even more important in such a case. However, while investment committees often have external members, they should have at least one board member to help build competency within the board and transfer knowledge to peers.

**Investment training** is also key to building the knowledge a board needs to properly exercise its fiduciary duty. One participant indicated that the contract with its investment management consultant has a provision for delivery of two training sessions, but the firm seems to resist doing this. Another participant asked what to do in situations like that or when advice is bad. Performance reviews of investment professionals are foreseen in Asset Management Standard 9. Performance in line with any contract is a fundamental element of a review. "Bad advice" has to be clearly supported and documented, but a CTF should not be timid about questioning the advice it receives.



Much concern was expressed about **the high cost of investment professional services and monitoring of advisor performance**. A few CTFs have an advisor who is paid in addition to the investment manager, and sometimes as much. Satisfaction with the services varied. While there are benchmarks to monitor the performance of an investment manager, it is not clear how to monitor the advisor's performance. An easy answer was not obvious, but the additional cost should result in better performance. The CTIS gives participating CTFs the opportunity to share information among themselves on investment performance allowing a CTF to see how it is performing relative to other CTFs with similar characteristics.

Fundacion Natura, Panama, indicated that they have used both types of investment professionals. The committee that follows investments has an outside technical expert who helps with performance monitoring. This has proven to be effective and keep costs down.

Participants wanted to know what **the reasonable cost of portfolio management** by an investment professional should be and whether discretionary or non-discretionary management made a difference in costs. The relationship between the size of an endowment and the fees charged was explained, citing the trend for better fees (recently about 0.6%) when endowments reach \$20 million. If differences in fees exist, CTFs should be convinced they are getting better performance when there are higher portfolio management costs.

The possibility of using performance based remuneration for investment professionals was raised. It was explained that this is not a common practice because it can lead to taking on higher risk.

### Case Study 1 – Financial Sustainability (facilitated by Monica Ferreira)

FUNBIO's own experience in selecting projects/programs informed this case study, which was not intended to be seen as "best practice", rather to show the factors that need to be considered when making selections. The Case Study appears as Annex 3 to this Chapter.

A presentation on financial sustainability provided concepts and insights to prepare for the case studies. Concepts included:

- the "myth" that there is a standard percentage of a project/program's total costs that an organization should receive for project/program management;
- the "pitfalls" to avoid when calculating management costs;
- the relevance of price, cost and value when it comes to decisions on project/program management; and
- identifying direct and indirect costs and the tools that help do so

Two projects, one for reforestation in the headwater region of the Gold River and the other to support monitoring of manatees, were described in terms of their context, challenge, impacts/benefits and costs. Participants were divided into 4 working groups (2 anglophone and 2 francophone, with one group of each language analyzing one of the proposed projects). The objective was to determine whether the CTF should undertake either or both of the projects.

Each project was rejected by the two groups that reviewed it since the groups considered that the management costs were too high to be covered by the funding available. One suggestion was to look for partners who might be able to contribute additional funding or carry out services at lower cost.

In her follow-up, Monica Ferreira said that there was no right or wrong answer and that each CTF would need to work on a least cost solution, but also consider the value that the project would bring to achieving the objectives of the organization. In the case of the “Preparing for Monitoring Manatees Project”, the manatee is the most endangered aquatic animal in the country, so that allowing oil and gas exploration and production, known to have negative effects on manatees, to proceed without mitigating measures would worsen their critical situation. The CTF’s first effort should be aimed at trying to define a budget for project management that is within the envelope defined by the donors. If that is not possible, but the project or program is of very high value, then the CTF might accept a reasonable shortfall.

## Case Study 2 – Selecting an Investment Professional to manage Endowment Capital (facilitated by Kathy Mikitin)

The walk-through of the Standards for Asset Management preceded participants’ review of the case study to ensure that everyone had a good understanding of the terms used in the case study and the principles that needed to be applied. The case study which presents a dilemma faced by the Smiling Bonobo Foundation was based on an actual investment professional selection process of a CTF and appears as Annex 4 to this Chapter.

Participants were again divided into four groups. Each had to consider the following questions:

- Would your CTF have signed the contract with the selected investment bank? Why?
- Which Standards are most applicable to this Case Study?
- Can you suggest a new Standard or additions to the existing ones to avoid weaknesses in the process?

The four groups were unanimous in their conclusion that the contract should not have been signed giving the following reasons:

- The process was flawed by not defining selection criteria before the evaluation began; the contract should have been re-bid.
- There was a conflict of interest and possibly collusive action by the two firms.
- The donor’s refusal to consider an investment management consultant was not justified.

The groups were able to find relevance in Asset Management Standards 1,2,4,5,7,8, and 9, Governance Standards 6 and 7 and Resource Mobilization Standards 1 and 3. There was consensus that there should be a new Standard or an addition to existing Asset Management Standard 7 that would require due diligence on any firm assisting with selection of an investment professional.

In the follow-up, Kathy Mikitin explained that the contract had been signed. There was a very tight deadline for release of a large amount of endowment capital, and there was no time to rebid. Donors were uneasy, but had to recognize that the selected firm was highly qualified and may well have been selected had the process not been deficient. Donors indicated they would monitor performance closely and request a change in the investment professional if that was considered in the interest of the CTF.

## Special Presentation – Best Practices for Foundations and Endowments (Jason Hamlin, UBS Arbor Group)

A very thorough presentation was made with the objective of addressing expectations of participants to know more about portfolio management. As the Practice Standards were not intended to serve a “how to” function, this presentation was added. It addressed:

- The basics of investing
- Investment policy planning

**“ The CTIS gives participating CTFs the opportunity to share information among themselves on investment performance allowing a CTF to see how it is performing relative to other CTFs with similar characteristics. ”**

- Asset allocation strategy
- Investment manager review and evaluation
- The evolution of single manager to multi-manager consulting
- Quarterly reviews and monitoring

A very enthusiastic discussion followed with participants citing the experience of their CTF. Although not an exhaustive summary, explanations provided are highlighted below in a brief form:

- Asset allocation accounts for 91.5% of performance, so the allocation has to be right.
- Index funds generally do not do well when interest rates are rising. Interest rates have been low and increases are next. Active management, rather than passive funds, is currently recommended.
- High yield bonds signal likely credit defaults, so they are correlated with stocks and when there are disturbances in stocks, they do not protect by offsetting the stock behavior.
- If real estate is publicly traded, then it is a stock. Real estate is segregated in asset allocations because it behaves differently and pays a coupon value.
- Emerging markets are still attractive, as returns are good given the risk involved. There is general optimism about the offerings in markets such as the BRIC countries because population growth is much higher, creating opportunities for economic expansion.

The final session sought suggestions from participants in line with the Conservation Finance Alliance's expressed wish that users provide feedback to improve content and ease of use of the Standards. Several participants indicated that they were just beginning to use the Standards or intend to do so and will provide feedback once there is more experience. Nonetheless, many good proposals were put forward:

- The use of board self-evaluations as a tool to improve governance effectiveness and efficiency could be a good addition to the Standards for Governance.
- One important lesson from Case Study 2 shows the need for investment committees and boards to know which type of service – investment manager or investment management consultant – they prefer prior to launching a request for proposals. A statement to this effect could be incorporated in the “Practical Considerations” section of the appropriate Asset Management Standard.
- Participants felt that Standards for communication were very important. Those standards could add more on partnerships and the private sector.
- The Monitoring and Evaluation Standards could be expanded to include more on internal and external evaluations. Inclusion of “adaptive management” as a Standard for CTFs should also be considered.
- It was pointed out that in designing governing bodies, it should be kept in mind that there will be a higher cost for supporting the board when there are directors/trustees located outside the country of the CTF, or rotating locations for board meetings.
- The Standards could address the inherent conflict of interest created by NGOs that are directors/trustees and also beneficiaries. Identifying the issue and providing practical consideration on how to “manage” this type of Col would be a useful addition because the practice is fairly common.
- Some participants felt that there should be a separate area on grant-making to cover that topic with more depth. Other types of CTF-supported activities could then be grouped or have separate topics.
- It was also proposed to expand the Standards for Administration to “Management and Administration”.



Annex 1 –  
Executive Summary of the Practice Standards







## EXECUTIVE SUMMARY

# Practice Standards for CONSERVATION TRUST FUNDS

Prepared by: Barry Spergel & Kathleen Mikitin



Funded by:

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# Table of Contents

PAGE 1	<b>Background</b>
PAGE 3	<b>Objectives</b>
PAGE 4	<b>Using the Standards</b>
PAGE 5	<b>Governance</b>
PAGE 6	<b>Operations</b>
PAGE 7	<b>Administration</b>
PAGE 8	<b>Reporting, Monitoring &amp; Evaluation</b>
PAGE 9	<b>Asset Management</b>
PAGE 10	<b>Resource Mobilization</b>



# Background

**These Practice Standards for Conservation Trust Funds (CTFs) are the result of a nearly one-year collaborative initiative aimed at developing evidenced-based norms for use by CTFs and those institutions and individuals who provide financial and technical support to them.**

The initiative was developed through the Conservation Finance Alliance (CFA) - a global voluntary network established in 2002 to help address the challenges of sustainable financing for biodiversity conservation. The CFA includes almost all CTFs and major donors to CTFs, as well as many other conservation organizations, networks and individual experts.

Conservation Trust Funds are private, legally independent institutions that provide sustainable financing for biodiversity conservation. They may finance part of the long-term management costs of a country's protected area (PA) system as well as conservation activities and sustainable development initiatives outside PAs. The core business of CTFs has been to mobilize resources from diverse sources – including international donors, national governments and the private sector – and to direct them in the form of grants to multiple programs and projects on the ground through non-governmental organizations (NGOs), community based-organizations (CBOs) and governmental agencies (such as national parks agencies).

Over time, CTFs have proven to be institutions of innovation, leading some to develop new business areas outside of grant-making. Many CTFs now play roles in policy making, capacity building and strengthening of civil society as well as provide services to design financial mechanisms, ensure fiduciary management for the assets of indigenous communities or support corporate responsibility actions in the private sector.

CTFs are institutions with varied financial arrangements. Many begin by managing one single endowment or sinking fund, as is the case of CTFs that were created to support a given protected area or a network of protected areas. Over time, CTFs diversify their programs and their funding mechanisms, with the creation of "Funds" that are sums of money dedicated to conservation interventions that are distinct from the CTF's initial activities and which may even require a separate governing body. As CTFs evolve into multi-Fund entities, they may manage a combination of endowments, sinking funds, or revolving funds.

CTFs also have as their purpose the efficient management of financial assets as sinking funds or endowments. The CFA sponsors the publication of an annual Conservation Trust Fund Investment Survey (CTIS) that collects and analyzes information about the investment practices and performance of CTFs. The 2012 CTIS indicated that the 35 participating CTFs manage the equivalent of over USD 672 million in endowments and sinking funds that range from the equivalent of USD 1.3 million to over USD 120 million.

The Practice Standards have been designed for CTFs that are private independent legal entities. CTFs usually include government representatives on their governing bodies and explicitly try to promote and implement national biodiversity conservation policies and strategies, but CTFs are not themselves controlled by governments nor part of a government ministry. However, many aspects of these Practice Standards for CTFs as private independent legal entities and for the separate Funds managed by such entities can also be usefully applied to (or be adopted and adapted for) quasi-autonomous environmental funds that are hosted by (or are part of) government agencies or ministries.

The present Practice Standards concentrate on the core business of grant-making and do not attempt to develop norms in the newer business areas which are both diverse and offer limited experience on which to develop evidenced-based standards. Nonetheless, the majority of the Standards are still applicable to the CTFs as the institutions that “house” the new businesses or to the design, management and evaluation of the Fund that carries out the business.

Over the last two decades, CTFs derived valuable lessons from their experiences and have shared best practices among themselves, through CTF networks such as RedLAC – the Latin American and Caribbean Network of Environmental Funds and CAFE – The Consortium of African Funds for the Environment.

Select international donors and non-governmental organizations have also accompanied the development and strengthening of CTFs and have now come together to collectively develop these Practice Standards for CTFs.



# Objectives

**These voluntary Practice Standards for Conservation Trust Funds are intended to serve as a tool for improving the design, management, and monitoring and evaluation of CTFs. CTFs and their donors can decide to use, aspire to, or adapt the Practice Standards to fit their particular needs. It is hoped that they will also serve as a basis for greater harmonization of international donor rules, standards and policies for CTFs, resulting in lower transaction costs for CTFs.**

The Practice Standards are also intended to increase the understanding of how CTFs function, by current and potential donors, national governments, civil society organizations, and CTFs themselves. It is hoped that this increased understanding of CTFs will in turn lead to more effective and efficient management of CTFs, and to increased donor support for CTFs (including support by private companies and other non-traditional donors). To this end, the Standards cover six core areas that are considered essential to the development of CTFs as effective institutions:

**Governance** addresses the composition, functions and responsibilities of a CTF governing body or bodies and the content and role of governing documents.

**Operations** covers strategic planning, grant-making; interactions with government, and partnerships with other organizations.

**Administration** takes up organizational roles and responsibilities, operations manuals, use of financial resources and auditing.

**Asset Management** discusses the components of investment strategies, fiduciary responsibilities and relationships with various types of investment professionals.

**Reporting, Monitoring and Evaluation** reviews conservation impact monitoring; frequency, format and content of technical and financial reporting to donors; and dissemination of results.

**Resource Mobilization:** covers fundraising as well as managing payments for environmental services (PES), compensation funds, offset payments, etc; mobilization and management of additional funding sources to enhance overall financial sustainability of biodiversity conservation, particularly protected area (PA) systems.

This Executive Summary provides the text of each standard in the six core areas for easy reference.

Finally, the Standards are not “set in stone” but will continue to evolve and be periodically updated by the CFA. Although it is possible that they could eventually evolve into a system of voluntary “certification” standards for CTFs, they are not designed to serve that purpose in their current form.





# Standards for Governance

## **Governance Standard 1:**

Governing documents clearly define the purposes for which a Conservation Trust Fund's or a Fund's assets may be used.

## **Governance Standard 2:**

Governing documents clearly define the composition, powers and responsibilities of the governing body (or bodies). A governing body's composition is designed so that its members will have a high level of independence and stakeholder representation.

## **Governance Standard 3:**

Governing body members are selected or appointed based on their competencies and commitment to contribute meaningfully to the CTF's (or Fund's) overall mission and responsibilities.

## **Governance Standard 4:**

Specialized committees are established by governing bodies to provide advice and to perform certain functions of the CTF or Fund more effectively and efficiently.

## **Governance Standard 5:**

A governing body has at least two face-to-face meetings per year, and maintains accurate written records of all meetings and decisions.

## **Governance Standard 6:**

Governing body members understand their fiduciary responsibilities and ensure they have (or acquire) the competence necessary to carry them out.

## **Governance Standard 7:**

An effective conflict of interest policy is in place to identify, avoid and manage potential and actual conflicts of interest to reduce exposure of the CTF to favoritism and reputational risk.

## **Governance Standard 8:**

The governing body recruits a full-time chief executive or Fund manager to manage the CTF's or Fund's daily operations, and oversees his/her performance, which is evaluated annually.

## **Governance Standard 9:**

A CTF keeps a "compliance list" in order to monitor and ensure its full compliance with all applicable laws and regulations, with all legal agreements between the CTF and donors, and with the CTF's own governing documents.

## **Governance Standard 10:**

A CTF is established under the laws of a country that effectively ensures the CTF's independence from government, that has clear and well enforced laws concerning private non-governmental organizations (including foundations or trusts), and that does not subject the CTF to paying substantial taxes.



# Standards for Operations

## **Operations Standard 1:**

A CTF prepares a strategic and financial plan that translates its broad vision and mission statements into specific goals, objectives and activities.

## **Operations Standard 2:**

As public benefit organizations, CTFs actively pursue opportunities to collaborate with all relevant levels of national government(s) on achieving conservation priorities.

## **Operations Standard 3:**

CTFs actively seek partnerships at the national or international levels with key actors in donor agencies, businesses, non-governmental organizations, communities and research and academic institutions.

## **Operations Standard 4:**

When awarding grants, a CTF evaluates potential grantees by requiring them to submit key information and by making direct contact with them.

## **Operations Standard 5:**

CTFs follow a well-defined grant award process that aims at selecting high quality proposals in a timely manner through competitive means.

## **Operations Standard 6:**

The grant award cycle concludes with the signature of a contract between the CTF and the grantee; the contract sets out all important understandings and obligations related to the financing the CTF will provide.

## **Operations Standard 7:**

CTFs encourage cost-sharing arrangements through which grantees contribute a portion of the project or activity cost, or raise funding from others.

## **Operations Standard 8:**

Measures to strengthen grantee capacity are carried out which enable grantees to prepare responsive proposals and implement grant-funded activities.

## **Operations Standard 9:**

A CTF ensures that the entities to which it awards grant funding apply effective, efficient and transparent acquisition processes and practices such that appropriate quality goods, works or services are obtained at the best prices for value in a given market.

## **Operations Standard 10:**

A CTF that accepts execution responsibility applies the same standards to the service it provides for grantees as it applies to the service it carries out for its own administration.

# Standards for Administration

## **Administrative Standard 1:**

Clarity of roles and organization and adequate resources allow the chief executive, managers and CTF staff to perform effectively and efficiently.

## **Administrative Standard 2:**

When proposing a budget or reviewing budget implementation, transparent presentation of management expenses allows a governing body to understand and analyze the full costs of delivering grant programs and any other strategic objectives.

## **Administrative Standard 3:**

A reasonable allocation of the available budget between management expenses and a grant program seeks to maximize funding for the grant program, but also recognizes the importance of achieving the institutional strategic objectives of the CTF.

## **Administrative Standard 4:**

One or more operations manuals with up-to-date policies, procedures and practices guide the day-to-day management of a CTF or Fund.

## **Administrative Standard 5:**

A CTF acquires the goods, works and services; needed to carry out its own everyday activities through processes and practices which are efficient, cost-effective and transparent; assure the appropriate quality of goods, works and services; and aim to obtain the best price for value in the market.

## **Administrative Standard 6:**

A CTF undergoes an annual audit by independent external auditors who apply standards that are consistent with internationally accepted accounting standards.

# Standards for Reporting, Monitoring & Evaluation

## **R, M & E Standard 1:**

CTFs are intentional about reporting to different audiences for different purposes.

## **R, M & E Standard 2:**

Grant agreements between a CTF and its donor clearly set out the specific formats, information requirements, procedures and timing for technical and financial reports.

## **R, M & E Standard 3:**

CTFs maintain a regularly updated checklist and schedules for all of the reports that they are required to submit to government agencies in the country where the CTF is legally registered and the countries where the CTF operates or has investments.

## **R, M & E Standard 4:**

A CTF monitors and evaluates its programs in relation to the CTF's purpose and its strategic plan, and in relation to national-level and international-level conservation indicators, targets and strategies.

## **R, M & E Standard 5:**

A CTF designs internal reporting, monitoring and evaluation, including financial management<sup>1</sup> reporting, to support informed decision-making by its governing body about the functioning of the CTF as an institution.

## **R, M & E Standard 6:**

CTF staff, and often the grantee itself, monitor grants using indicators and measures agreed upon in the grant agreement, or its required monitoring plan.

## **R, M & E Standard 7:**

CTFs design monitoring and evaluation to support evidence-based reporting of conservation impacts.

## **R, M & E Standard 8:**

CTFs support their grantees by providing clear reporting templates, frameworks and information requirements for monitoring and evaluation of the grant performance in achieving planned outputs and outcomes.

## **R, M & E Standard 9:**

CTF staff (and/or independent evaluators) performs due diligence and monitor grantees' progress towards achieving outputs and outcomes.

## **R, M & E Standard 10:**

CTFs prepare an Annual Report each year, which is distributed to donors and key stakeholders, and is made available to the general public.

<sup>1</sup> "Financial management" in the context of this standard refers specifically to the transactions related to the institution's administration and operations (e.g. accounting, budgeting, grant-making).

# Standards for Asset Management

## **Asset Management Standard 1:**

A clear and comprehensive investment policy sets out the core principles the CTF applies for managing its assets.

## **Asset Management Standard 2:**

A CTF's investment portfolio is managed in accordance with investment guidelines that set out the specific parameters to be applied by the investment management consultant, financial advisor and/or the investment manager(s).

## **Asset Management Standard 3:**

The CTF governing body or its committee responsible for overseeing investment management, invests and manages as a prudent investor would invest his or her own funds.

## **Asset Management Standard 4:**

CTFs seek to preserve endowment capital in order to protect future earnings streams.

## **Asset Management Standard 5:**

The governing body may delegate responsibilities related to investing the CTF's assets to a committee of the governing body or investment professionals, but the governing body itself must review and approve the investment policy, investment guidelines, the process of selecting a financial consultant and/or investment manager(s), and reports on investment and financial consultant and/or asset manager performance.

## **Asset Management Standard 6:**

To appropriately carry out its own responsibilities with regard to investment management, a governing body (i) has at least one director who is a qualified professional with knowledge and experience in one or more of the fields of finance, business or economics and (ii) ensures that all its members receive targeted training on the key concepts required to make informed decisions when it carries out its responsibilities.

## **Asset Management Standard 7:**

The CTF assesses its existing investment capacity, identifies what types of investment professionals it may require, and selects these professionals through a competitive process and from among investment industry service providers of recognized quality.

## **Asset Management Standard 8:**

Contracts for services to be provided by investment professionals state in a clear and comprehensive manner the services to be provided, the objectives of the services, the costs of delivering the services, and the responsibilities of both the service provider and the CTF.

## **Asset Management Standard 9:**

A CTF engages in regular reviews of investment management performance.

# Standards for Resource Mobilization

## **Resource Mobilization Standard 1:**

CTFs have strategies to diversify and multiply their short-term and long-term sources of financing, rather than depending on a single source or a single funding mechanism.

## **Resource Mobilization Standard 2:**

CTFs develop resource mobilization strategies or action plans for raising long-term capital as well as shorter-term funding for particular projects or programs.

## **Resource Mobilization Standard 3:**

CTFs have policies for screening and determining which donor contributions and conditions they will accept.

## **Resource Mobilization Standard 4:**

CTFs analyze and pursue opportunities for using funds from particular donors or government sources as a way of leveraging additional resources.

## **Resource Mobilization Standard 5:**

CTF governing bodies and management try to identify, analyze and utilize opportunities for the CTF to be used as the financial and institutional mechanism for disbursing PES, user fees, REDD+, climate adaptation funding, biodiversity offset payments, environmental compensation and fines, in order to support activities that are aligned with the purpose of the CTF.

## **Resource Mobilization Standard 6:**

CTF governing body members and the chief executive coordinate with, and seek the support of, national government ministries and politicians in mobilizing additional financial resources for the CTF from national governments and international donors.

## **Resource Mobilization Standard 7:**

CTFs are able to show potential donors the role that the CTF plays in providing long-term financial support for the national system of protected areas and/or for national environmental action plans and programs.

## The Conservation Finance Alliance encourages readers and users to provide feedback aimed at improving the content and ease of use of these Practice Standards.

Comments and suggestions can be submitted using the electronic version that is accessible through the CFA website ([conservationfinance.org](http://conservationfinance.org)) or by sending an e-mail to the CFA Secretariat ([secretariat@conservationfinance.org](mailto:secretariat@conservationfinance.org)).

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A photograph of several quail birds in a dry, grassy field. The birds are grey with blue heads and necks. They are scattered across the field, some facing left and some facing right. The background is a blurred field of dry grass and some trees in the distance.

## Annex 2 – Agenda e Participantes

### Using the Practice Standards for Conservation Trust Funds

Salima, Malawi

October 10-12, 2016

#### October 10, 2016

- |               |  |
|---------------|--|
| 09:00 – 09:15 | Opening of the Workshop  |
| 09:15 – 09:45 | Introduction to the Practice Standards ( <i>Objectives, Approach, Subject Areas</i> )                    |
| 09:45 – 10:15 | Adopting the Standards ( <i>Who adopts, for What purpose, How</i> )                                      |
| 10:15 – 10:45 | Coffee Break   |
| 10:45 – 13:00 | Standards and the CTF Life Cycle ( <i>Creating, Managing, Evaluating</i> )                               |
| 13:00 – 14:15 | Lunch  |
| 14:15 – 15:45 | Managing with the Standards ( <i>Case Study I - Financial Sustainability - Monica Ferreira, FUNBIO</i> ) |
| 15:45 – 16:15 | Coffee Break   |
| 16:15 – 17:00 | Report back from working groups and discussion of Case Study I   |



## October 11, 2016

- 09:00 – 11:00 Walk-thru of the Standards for Governance, Operations, Administration Resource Mobilization and Reporting, Monitoring & Evaluation
- 11:00 – 11:15 Coffee Break
- 11:15 – 13:00 Walk-thru of the Standards for Asset Management
- 13:00 – 14:00 Lunch
- 14:00 – 16:00 Selecting an Investment Professional to Manage Endowment Capital  
*(Case Study 2 – Dilemma of the Smiling Bonobo Foundation)*
- 16:00 – 16:15 Coffee Break
- 16:15 – 17:00 Report back from working groups and epilogue of Case Study 2

## October 12, 2016

- 09:00 – 09:15 Summary of Tuesday's Discussion on Standards for Asset Management
- 09:15 – 11:15 Improving Portfolio Performance  
*(Presentation by Jason Hamlin, UBS Arbor Group)*
- 11:15 – 11:30 Coffee Break
- 11:00 – 12:30 Questions on Investment Management
- 12:30 – 13:00 New Standards *(including suggestions from participants)*
- 13:00 – 14:00 Lunch

## List of Workshop Attendees

Alfred Allogninouwa, Executive Director, FSOA  
Fenesoa Andriamahenina, Executive Secretary, BioGuinea  
Jorge Enrique Trejo Canelo, Regional Coordinator, FIAES El Salvador  
Aicha Sidi Bouna, Board President, BACoMaB, Mauritania  
Carl Bruessow, Executive Director, Mulanje Mountain Trust, Malawi  
Maria Celeste Chitará, Administration and Finance Director, Biofund, Mozambique  
Monica Ferreira, FUNBIO, Brazil  
Maria Alexandra Jorge, Program Director, Biofund, Mozambique  
Raymond R. Killenga, Program Officer, EAMCEF, Tanzania  
Kouakou Parfait Kouadio, Board Member, FPRCI, Côte d'Ivoire  
Katy Mathias, Conservation Trust Investment Survey Project Manager, WCS, USA  
Edoa Mengue, FEDEC, Cameroon  
Suelen Marostica, Project K Coordinator, FUNBIO, Brazil  
Lisa Meza, Environmental Specialist, Fondo de las Americas, Peru  
Joshua J. Moloji, Chief Executive Officer, Forest Conservation Botswana  
Rosa Montañez, RedLAC President, Fundación Natura, Panama  
Brendah N. Mpanga, Secretary, Board of Trustees, Uganda Biodiversity Fund  
Tuli Salum Msuya, Executive Secretary, Tanzania Forest Fund  
Wilson Mwetonde, Trust Administrator, Bwindi Mgahinga Conservation Trust, Uganda  
Aline Odje, Board President, FSOA, Benin  
Dr. Fanny N'golo, Executive Director, FPRCI, Côte d'Ivoire  
Gérard Rambeloarisoa, Executive Director, FAPBM, Madagascar  
Ravaka Ranaivoson, *Manager CEPF RIT MADIO, Tany Meva, Madagascar*  
Kempho Tsheko, Finance Manager, Forest Conservation Botswana  
Nestor Windevoxhel, Project K Committee Member, Guatemala  
Théophile Zognou, FTNS, Cameroon, CAR, Congo

## Annex 3 – Case Study on Financial Sustainability – Evaluating Two Different Project Opportunities

Author: Mônica Ferreira

### Facing the Financial Sustainability of the Smiling Bonobo Foundation

These case studies examine a key process that Conservation Trust Funds (Environmental Funds) generally follow when they evaluate a project opportunity from the point of view of financial sustainability of the CTF. Two hypothetical projects will be presented for the purpose of comparison.

The questions that appear at the end of the case study text can be answered by first estimating the costs of the SBF for each project to evaluate the opportunity from a financial point of view. However, like many day-to-day challenges faced by Environmental Funds, there is no simple or unique solution.

### Evaluating Two Different Project Opportunities

#### General Context

The Smiling Bonobo Foundation (SBF) was consulted about the possibility to manage two different environmental projects. Both are strictly linked to the SBF's mission and, if the success will not only have a great value for the environmental community, but also for society in general.

## Project A: Reforestation - Planting 2.5 million trees

### The Challenge:

Planting 2.5 million trees on approximately 1000 hectares in the headwater regions and sources of the Gold River.

### Impacts:

- i. Contribute to forest restoration,
- ii. Achieve recovery of water sources and forests on the shores of rivers feeding into the Gold River.
- iii. Generate income in a participatory and inclusive manner.

### Context:

The Gold River is one of the most extensive and important rivers in the region and has a great biological diversity. However, the river is subjected to strong pressure from the surrounding human occupants and has a high rate of deforestation.

A planting technique with costs that are 50% less than the traditional methods of planting seedlings will be used. This technique consists of mixing various seeds of native species in a substrate. Planting with this substrate results in the simultaneous germination plants with different behaviors, creating a diversity that attracts animals which, in turn, bring other plant species.

The main risks such as fire or errors in the use of technology are mitigated with specialized technical assistance and systematic monitoring. The major advantage of this initiative is a consistent effort of awareness and behavior change, stamped with the signing of contracts with the landowners that clearly define the responsibilities of each stakeholder.

The SBF should seek a partner in the project region. This partner will work with landowners to carry out the planting of trees. Due to previous experience, the cost per tree has been estimated. In addition, the SBF will be responsible for managing all financial resources, for resolving any legal issues between the parties, for monitoring the planting of trees and for preparing technical and financial reports quarterly.

### Target:

2.5 million trees, 1,000 hectares in five years

### Project cost:

The total cost including planting costs, technical assistance, monitoring and project management is \$ 10 million, to be disbursed over the five years of the project.

### Additional Information:

Cost of planting each tree: \$ 3,00

SBF – Total Staff: 32 persons

Job Title / Function	Number	Annual Base Salary without Benefits
Project Coordinator	2	\$ 200.000
Project Manager	6	\$ 120.000
Project Assistant	10	\$ 75.000
Legal Advisor	2	\$ 200.000
Financial Assistant	4	\$ 100.000
Procurement Assistant	3	\$ 100.000
Administrative Assistant	3	\$ 60.000
Technology Information Analyst	2	\$ 100.000

Annual Benefits: \$ 18.000/person

SBF Indirect Costs (Office support staff who are not directly working on this project; Utilities; Development/fundraising): 12% of direct costs

For simplification purposes, consider that there is no inflation in the project period

Based in the experience of the group, determine what functions are necessary for managing this project. After that, determine how many persons and the percentage time to be spent in this project (as the template below) to calculate the personnel costs. Ex: If you need one project manager allocated 50% of his time in the project, use 50% in template table. If you need two project managers allocated full time in the project, use 200% (or two lines with project manager with 100% each one).

The SBF Total Staff number must be used for calculating the office expenses proration.

### Discussion Questions:

**Should the Smiling Bonobo Foundation (SBF) accept to manage this challenging project? Why?**

## Project B: Preparing for Monitoring Manatees

### The Challenge:

Increase scientific knowledge about the population of manatees (*Trichechus manatus manatus*), which occurs in a specific region of the country, enabling a newly established *Aquatic Animal Research Center* to carry out future monitoring of the population through satellite telemetry and establish population estimates by overflight that relates data obtained in relation to the activities of *General Oil Corporation* in the region.

### Impacts:

Contribute to the preservation and increase of the population of manatees, which are the most endangered aquatic mammals in the country. With a current population of only 200-500 individuals and discontinuous territorial distribution along the north coast, the manatee is approaching extinction.

### Context:

This region has the highest incidence of strandings newborn individuals in the country and intense activity of exploration and production of oil and gas.

For *General Oil Corp* to obtain the environmental license to continue working in the region, it must provide a research center in the region with all the resources necessary for monitoring.

*General Oil Corp.* looks to the SBF to carry out the project to build the center and to acquire the infrastructure and equipment necessary for the start of monitoring.

The project will last one year, during which time the research center will be built and provided with all the necessary equipment to carry out aerial census and satellite monitoring. In addition to the infrastructure for the center, boats will be purchased to catch native manatees for introduction of electronic devices required for satellite monitoring.

Besides the procurement activities, SBF will be responsible for the financial management, including the preparation of quarterly financial reports.

### Target:

Set up a center of research all equipped for the start of the monitoring of manatees in one year.

### Project value:

The resources available to fund the research center are \$ 7 million and the amount to cover the SBF management expenses is limited to 10%. So the total cost of the project is \$ 7,7 million.

### Additional Information:

SBF – Total Staff: 32 persons

Job Title / Function	Number	Annual Base Salary without Benefits
Project Coordinator	2	\$ 200.000
Project Manager	6	\$ 120.000
Project Assistant	10	\$ 75.000
Legal Advisor	2	\$ 200.000
Financial Assistant	4	\$ 100.000
Procurement Assistant	3	\$ 100.000
Administrative Assistant	3	\$ 60.000
Technology Information Analyst	2	\$ 100.000

Annual Benefits: \$ 18.000/person

Payroll Taxes: 50%

Annual Office Operations & Maintenance Expenses (rental, phone, electricity bill, etc): \$900.000

SBF Indirect Costs (Office support staff who are not directly working on this project; Utilities; Development/fundraising): 12% of direct costs

For simplification purposes, consider that there is no inflation in the project period

Based in the experience of the group, determine what functions are necessary for managing this project. After that, determine how many persons and the percentage time to be spent in this project (as the template below) to calculate the personnel costs. Ex: If you need one project manager allocated 50% of his time in the project, use 50% in template table. If you need two project managers allocated full time in the project, use 200% (or two lines with project manager with 100% each one).

The SBF Total Staff number must be used for calculating the office expenses proration.

### Discussion Questions:

**Should the Smiling Bonobo Foundation (SBF) accept to manage this “lovable” project? Why?**

Suggested Templates For Exercise:

BUDGET DATE:

**Personnel**

Please complete the table below for project staff whose time can be tracked directly to the project. Be sure to include those positions that are to be hired.

Qty Hours/Year	2112
Project Time (years)	

Total \$\$ Benefit/Person/Year	
Payroll Taxes	

No.	Name (Optional)	Job Title / Function	Annual Base Salary w/o Benefits	Total % Time to be Spent on this Project
1		Project Coordinator		
2		Project Manager		
3		Project Assistant		
4		Legal Advisor		
5		Financial Assistant		
6		Procurement Assistant		
7		Administrative Assistant		
8		Technology Information Analyst		
9				
10				
11				
TOTAL				0.00%

Total Hours to be Spent on this Project	Total \$\$ Salaries to be Spent on this Project	Total \$\$ Benefits to be Spent on this Project	Total \$\$ Payroll Taxes to be Spent on this Project
0	\$ -	\$ -	\$ -
0	\$ -	\$ -	\$ -
0	\$ -	\$ -	\$ -
0	\$ -	\$ -	\$ -
0	\$ -	\$ -	\$ -
0	\$ -	\$ -	\$ -
0	\$ -	\$ -	\$ -
0	\$ -	\$ -	\$ -
0	\$ -	\$ -	\$ -
	\$ -	\$ -	\$ -

**Consultants and Contractors**

Please complete the table below for consultants and contractors who will participate in this project. Project participants who are or will be employed by your organization should be listed in the “Personnel” section above.

No.	Name / Organization	Service / Deliverable
1		
2		
3		
4		
5		

**Other Expenses**

Please include other expenses for this project: Travel (Transportation & Lodging); Communication & Publications (Travel expenses, Lodging, Supplies, Auditing expenses, etc)

Line Item	Amount	Description
Travel Transportation	= \$ 2100*48 = \$ 100,800	20 trips of 2 staff members 8 trips of third staff member Approximate cost per trip: R\$ 2100

**Office Operations & Maintenance Expenses (allocated pro rata)**

<b>SBF Total Staff (persons)</b>	
<b>Annual Office Operations &amp; Maintenance Expenses</b>	
Office Operations & Maintenance Expenses (allocated pro rata)	



<b>SBF COSTS - PROJECT</b>	<b>TOTAL</b>
<b>Detailed Budget Total</b>	
<b>Personnel</b>	
Salaries	
Benefits	
Payroll Taxes (50%)	
Subtotal Personnel Salaries	0
<b>Consultants and Contractors</b>	
Subtotal Consultant and Contractor Fees	0
<b>Other Expenses</b>	
Travel Transportation	
Travel Lodging	
Auditing Expenses	
Supplies	
Subtotal Other Expenses	0
<b>Office Operations &amp; Maintenance Expenses (allocated pro rata)</b>	
Subtotal Office Expenses	0
<b>Total Direct Costs</b>	<b>0</b>
<b>Indirect Costs</b>	<b>0</b>
<b>Total Costs</b>	<b>0</b>

## Annex 4 – Case Study on Financial Sustainability – Selecting an Investment Professional to Manage Endowment Capital

Author: Kathy Mikitin

### The Dilemma Facing the Smiling Bonobo Foundation

This case study examines a key process that Conservation Trust Funds (Environmental Funds) generally follow when they select an investment professional, whether it is an investment manager or investment management consultant, to assist the Board with investment of endowment capital. It is based on a true experience which took place in 2014.

The questions that appear at the end of the case study text are intended to provoke discussion and to encourage use of the Practice Standards for Conservation Trust Funds as a source of the principles that can be applied to achieve effective and efficient management. However, like many day-to-day challenges faced by Environmental Funds, there is no simple or unique solution.



## Context

The Smiling Bonobo Foundation (SBF) was fortunate to receive donor funding for the services of Bazaroff Inc. (BI) to assist with drafting of the investment policy and selection of a firm to manage the SBF's invested assets. Bazaroff Inc. was an *investment management consulting firm* headquartered in Syldavia. The donor accepted that its own rules for procuring services could be subordinated to investment industry practice for the selection process.

## Defining the Investment Policy and Guidelines for the SBF

BI provided the SBF with a questionnaire whose answers would help BI set key parameters of the SBF investment policy: these included the *investment horizon*, *risk tolerance*, the expected return and the pattern of disbursement of investment earnings. Investment in the US financial market was considered the best option for the SBF, because Europe was entering a financial downturn. Based on the answers from the SBF, BI performed return simulations<sup>3</sup> that helped define the percentage of different asset classes that would make up the "strategic asset allocation".

The "strategic asset allocation" is a key element of a request for proposals when selecting an investment professional. That particular allocation of assets will, according to the simulations, achieve the return a CTF is seeking over its chosen investment horizon and with a frequency and magnitude of losses in line with the CTF's stated risk tolerance. When bidding, each firm that submits a proposal to be the SBF's investment professional would have to indicate whether it could meet the target return by following the strategic asset allocation or whether it would change that allocation (which could mean taking on more risk).

Agreement was reached on the SBF investment policy and guidelines, including the strategic asset allocation and target return.

In addition, the policy and guidelines addressed the following topics:

- Principles of diversification
- Specific guidelines for types of assets
- Risk management strategies
- Allowable and prohibited asset class categories
- Percentage limitations for asset classes, industries or individual investments
- Liquidity of assets

- Benchmarks for measuring performance of the investment manager and portfolio performance
- An approach for taking environmental, social and governance factors into account
- Reporting requirements

A three-step selection process was also agreed in line with investment industry practice. The process would begin with expressions of interest based on a long-list of known, high quality international firms, be followed by a request for proposals from a short-list drawn from the interested firms and end with interviews of the three to four firms with the best proposals.

## Selecting the SBF Investment Professional

It is worth noting that the SBF had previously initiated an *investment professional* selection process that was never concluded. Proposals were received but, owing to delays in donor funding, no evaluation or decision was made. The proposals were more than a year old, and changes in financial market conditions and a major increase in the SBF's donor funding justified a re-bidding.

A long list of firms was proposed by Bazaroff Inc., comprised of European-based *investment managers* several of which were located in Syldavia. The list was questioned by the donor and the SBF because some firms that were known to be good performers and that were currently managing investments for other CTFs were not on the list. The SBF also questioned whether the list was biased, as all firms were *investment managers* and none were *investment management consultants*. Bazaroff Inc. attempted to justify the long list it proposed as being firms it "knew and worked with" and indicated that *investment management consultants* were not appropriate service providers, but it was overruled by the donor and the SBF. The long-list was modified to add known firms, including *investment management consultants*.

Five competent firms expressed interest in submitting proposals and became the short-list of candidates that would receive the RFP. One firm later dropped out, leaving four firms. One of the four firms was Dupont & Dupond, an *investment management consultant* from North America, while the remaining firms were *investment managers* headquartered in Syldavia.

Prior to the call for proposals, the SBF requested to review the full bidding documents prepared by Bazaroff Inc, including the invitation email and complete RFP (i.e. the RFP guidance plus the SBF's investment policy and guidelines). Based on the SBF's understanding of good procurement practice, it requested that each firm on the short list be notified of all other firms being asked to submit a proposal and it questioned whether it would not be better to also state the criteria that would be used to

<sup>3</sup> Monte Carlo Simulations can generate 10000 (or more) return paths over predefined horizons for different asset classes (equity, fixed income, alternative investments, etc.) simulating possible future market scenarios. This is the workhorse of strategic asset allocation and the basis for all portfolio calculations.

evaluate the firms' proposals. Bazaroff Inc. insisted that under "industry practice" this could not be done. The donor agreed to follow industry practice.

Four proposals were received in spite of a very short deadline for submitting proposals. All proposals were sent to Bazaroff Inc. which reviewed them and recommended that all four firms be invited for the interviews which were to be held in Syldavia.

Interviews of the four firms were held over two days with participants from Bazaroff Inc., the donor agency and the SBF. In addition to discussions of how each firm would achieve the target return, participants asked about fees, the willingness of firm representatives to meet in person at least once annually with the Board and Investment Committee of the SBF, tax exemption possibilities and reporting practices. Two strong firms emerged: the US branch of Ottokar Bank, a Syldavian investment manager and Dupont & Dupond, a North American firm offering investment management consulting services. Both firms indicated that they could accept to manage in accordance with the SBF investment policy and guidelines and that the target return could be achieved, with some modification of the strategic asset allocation. The modifications proposed were considered to be within an acceptable range.

To decide between the two firms, Bazaroff Inc. asked the SBF and donor participants to define evaluation criteria by which to choose the winning firm. The evaluation was carried out verbally. One rating was agreed through consensus for each criterion (quality of proposal, quality of supporting documents, client responsiveness, etc). During the evaluation, Bazaroff Inc. again raised the point that using an *investment management consultant* was not an appropriate arrangement for the SBF. The donor sympathized, indicating that a *discretionary arrangement* was needed and that a *non-discretionary arrangement* might be considered in several years when the SBF had more experience. The SBF questioned that judgment because the proposal and interview performance of Dupont & Dupond were very good. The SBF was worried, however, by the donor's statement that with a *non-discretionary arrangement* SBF would be faced with decision-making it was not ready to handle. Bazaroff Inc. nonetheless admitted that both firms were nearly equally rated and proposed instead that fees be the determining factor.



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Dupont & Dupond's proposal included its fee structure with an explanation of why its fees were generally higher than fees of an investment manager. When asked whether it could reduce those fees, the response was that it was not possible.

Ottokar Bank proposed a fee that was slightly less than the fee it stated during the interview (there was no fee in its written proposal). Since this fee was 0.2% less than that of Dupont & Dupond, it was decided to propose selection of the US branch of Ottokar Bank to the SBF Board.

## New Information

The proposal to retain Ottokar Bank was approved by the SBF Board of Directors. Prior to contract signature, SBF learned that Bazaroff Inc. was a wholly owned subsidiary of Ottokar Bank.

## Discussion Questions:

Would your Fund have signed the contract with Ottokar Bank? Why?

Which Standards are most applicable to this Case Study?

Can you suggest a new Standard or additions to the existing ones to avoid weaknesses in the process?

## Key to Terms Used:

**Investment Management Consultant:** A fee-based advisor operating under a non-discretionary arrangement who can provide guidance on portfolio theory, asset allocation, manager search and selection, investment policy and performance measurement. The role of the Investment Management Consultant is to provide independent advice, and the consultant's primary responsibility is to his/her client. Investment Management Consultants can help to review the performance of Investment Managers relative to the investment goals of the client, and may give the client advice on which investment managers to hire and fire.

**Investment Manager:** Specialists in managing a portfolio or investments in a specific type of asset, such

as medium quality corporate bonds; large cap value equities, or emerging market governments' debt. Mutual fund managers, portfolio managers and hedge fund managers are examples of this. Investment Managers act with their own discretion to buy and sell investments within the parameters specified by the investment guidelines.

**Investment Professionals:** For the purposes of the Practice Standards, a general term that refers to an investment management consultant, financial advisor or investment manager, either separately or jointly according to the CTF's arrangement.

**Investment Horizon:** The total length of time that an investor expects to hold a security or the portfolio that achieves the specified investment goal. The investment horizon is used to determine the investor's income needs and desired risk exposure, which are then used to identify the composition of the investment portfolio.

### **Risk tolerance:**

In the general context of investing, there are three broadly used definitions of risk: 1) The possibility that the return on an investment will vary from the expected return. 2) The possibility that an investor might lose part or all of his/her investment. 3) The "standard deviation" or variance of returns from a reference investment or a historic average return for an investment category. "Standard deviation" is the most commonly used measure of risk by investment professionals.

For CTFs, risk tolerance also refers to the CTF's willingness to accept, along with positive returns on its investments, that the stream of revenue expected from those investments could also potentially be reduced or even be zero for a given number of years during the period of the investment horizon.

**Discretionary:** Refers to an arrangement that gives an investment professional the authority to make decisions on behalf of the client using his or her own judgment, but within the guidelines provided by the client (i.e. the "investment guidelines" approved by a governing body or investment committee).

A **non-discretionary arrangement** requires the investment professional to seek approval of the client when making decisions.





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