

THE REPUBLIC OF UGANDA

PARLIAMENT OF UGANDA

REPORT OF THE ADHOC COMMITTEE ON ENERGY ON THE
PERFORMANCE OF THE ELECTRICITY SUB-SECTOR IN
UGANDA

SEPTEMBER 2011 – OCTOBER 2012

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ACCRONYMS/ABBREVIATIONS

ACE	Adhoc Committee on Energy
AfDB	African Development Bank
BHPP	Bujagali Hydro Electric Power Project
BOO	Build Operate and Own
BOT	Build Operate and Transfer
EAPP	East African Power Pool
ERA	Electricity Regulatory Authority
GOU	Government of Uganda
IDA	International Development Agency
IPP	Independent Power Producers
JICA	Japan International Co-operation Agency
MEMD	Ministry of Energy and Mineral Development
MFPED	Ministry of Finance, Planning and Economic Development
MoWE	Ministry of Water and Environment
MP	Member of Parliament
OTS	Open Tender Systems
PPDA	Public Procurement and Disposal of Public Assets Authority
PSDO	Power Sector Development Operation
PSRPS	Power Sector Restructuring and Privatization Strategy
RGN	Royal Government of Norway

TOR	Terms of Reference
UBC	Uganda Broadcasting Corporation
UEB	Uganda Electricity Board
UEDCL	Uganda Electricity Distribution Company Limited
UEGCL	Uganda Electricity Generation Company Limited
UETCL	Uganda Electricity Transmission Company Limited
UNDP	United Nations Development Programme
UNEP	United Nations Environment Programme
USD	United States Dollars
WB	World Bank

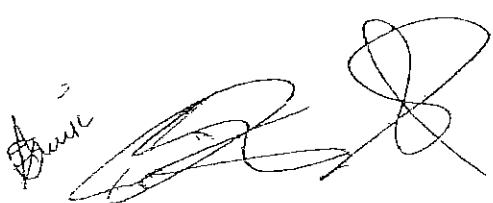
ACKNOWLEDGEMENT

The Adhoc Committee on Energy (ACE) in a special way extends thanks to the Rt. Honorable Speaker and Members of the 9th Parliament, the Office of the Clerk to Parliament for the financial and technical support rendered during the investigation. The Committee also recognizes the contribution of the support staff during the investigation.

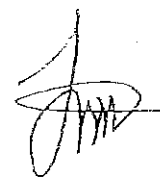
The Committee would like to express its most sincere appreciation and gratitude to the various witnesses inter-alia; Ministers, Heads of Government Institutions and individuals and private entities who appeared before the Committee to give evidence and valuable information.

The Committee also appreciates the role played by the Press and Media in publicizing the Committee's work for appreciation and participation of the wider population.

The Committee is indebted to the Government of Kenya, Ministry of Energy of the Republic of Kenya, Kenya Power Lighting Company (KPLC), Kenya Electricity Generation Company Limited (KENGEN), the Government of Republic of Ghana, Energy Commission of Ghana (ECG) and the Volta River Authority (VRA) for hosting and sharing vital information in the Energy sector and the reforms.

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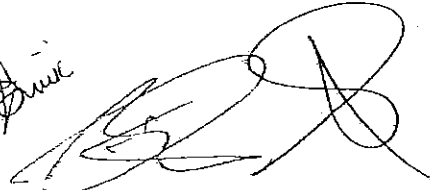

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EXECUTIVE SUMMARY

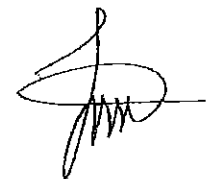
On the 24th August 2011 the Rt. Honourable Speaker of Parliament of Uganda, appointed an eight member Adhoc Committee on Energy (ACE), to investigate the electricity crisis in the country which was characterized by among others, persistent power outages and load shedding. This came at the time when stakeholders had raised concerns about high electricity tariffs, faulty billing systems, astronomical subsidies by the Government towards thermal power generation, as well as, poor quality of service by Umeme Limited.

In order to effectively understand the irregularities in the electricity sub-sector and to comprehensively address its Terms of Reference, the Committee as a matter of necessity had, to review the restructuring and reform process in the sector that dates as far back as 1999. The Committee established that the reform process in the power sector that led to the unbundling of UEB into successor companies (UEGCL, UETCL and UEDCL) had good and well intended objectives which included:

- i) Securing sustained, efficient and affordable electric power for domestic, commercial, industrial and other uses
- ii) Attracting significant private sector participation or investment in the sector
- iii) Removing real or perceived monopolistic structures in the sector and thereby create market conditions that would make for competition for services
- iv) Achieving transparency in the regulation of power utilities.

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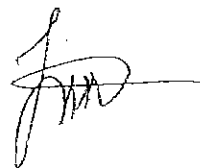
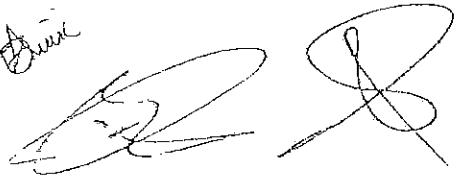
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The Committee noted that the power sector restructuring process which involved the unbundling UEB into successor companies was marred by irregularities. The Power distribution concession agreements signed between GoU and Umeme Ltd have number of unfavorable clauses to Government and the citizenry. The role played by Paul Mare in the unbundling of UEB was highly suspect given his employment record with Eskom Enterprises South Africa (a share holder of UMEME Ltd, 2004) and later Eskom Uganda and UMEME. It's no doubt that Paul Mare came as a forerunner for his parent company, Eskom Enterprises South Africa (Eskom Uganda), which together with Umeme Ltd are running the key segments in the electricity chain ie generation and distribution respectively. Unfortunately, it was on the strength of the biased/doctored information provided by Paul Mare (as a billing expert with UEB) about the level of losses and dilapidation of electricity network that the Government based to privatize and sign the power distribution concession with Umeme Ltd in 2004.

More than ten years after the reforms in the power sector were carried out, the generation capacity output at the main Kiira-Nalubaale hydropower dropped from high 270MW (when Eskom took over) to a low generation output of 140MW, while the power distribution segment is still characterized by dilapidated infrastructure in most areas (despite a claim by UMEME Ltd to have invested \$130million in the network), high energy losses, high levels of government subsidies (until Feb 2012), poor quality of supply and energy utilization inefficiencies.

Uganda continues to charge one of the highest electricity end-user tariffs in the region and globally despite the high Government subsidy. Notwithstanding Government efforts to expand power connectivity through the Rural Electrification Agency (REA), only 10-12% of the country's total population has

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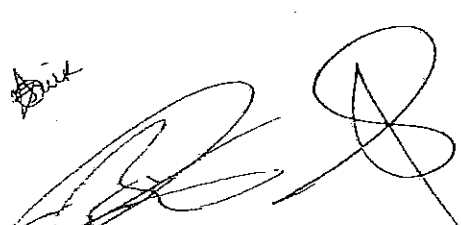




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access to the power. The coming on board of 250MW from the Bujagaali Hydropower Plant has done little in boosting the national electricity coverage, save for temporarily stabilizing the power supply. Admittedly, this is, according President Museveni likely to tame power outages and load shedding for only two years. Unless the intention to develop Karuma and other hydro-power stations is implemented per plan, the demand for power in Uganda will increasingly outstrip supply, undermining targeted socio-economic growth rates and exacerbating environmental degradation.

In addition to the reforms in the power sector, Government through the Energy Ministry has demonstrated some efforts aimed at addressing the challenges in the sector, particularly the high power tariffs, power distribution losses and poor service delivery. In 2009, the then Minister of Energy and Mineral Development, Hon. Hillary Onek constituted a Committee for Interim Review of Electricity Tariff chaired by Gen. Salim Saleh. The committee made key findings and recommendations as contained in its Report on Electricity Tariff Reduction. While initially efforts were made to have this report considered by Cabinet, the Minister of Energy realized that since this was a tariff matter and therefore under the purview of the sector regulator, he sent the report to the ERA Board for scrutiny and eventual implementation. However, save for the basic implementation done by ERA, the critical recommendations in this report such a forensic audit into the Umeme investments and level of losses have not been addressed.

The inherently poor performance of the power generation and distribution segments of Uganda's electricity sector is attributable to mismanagement of the reform process by PU-MFPED, the inefficiency of ERA, the ineffectiveness of UEDCL and the failure by both Eskom and UMEME Ltd to manage those assets as was intended. For the electricity sector to succeed it is mandatory to have a technically astute and experienced regulator, asset owner and asset manager.

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Of great concern to the committee was the manner in which the power distribution concessionaire was procured and the outrageous terms and conditions of the agreements signed between GoU and Umeme Ltd. The soft targets set for UMEME Ltd notwithstanding, the committee found out that because of the peripheral role played by the Attorney in the drafting of the power concession agreements, their terms and conditions were skewed to favour Umeme at the expense of Government and the people of Uganda as evidenced by scandalous provisions like loss of sovereign immunity over national assets, termination, abnormal buy-out amounts, working capital allowances/days lag and compensation of Umeme for making losses.

The Committee also identified critical institutional and policy deficiencies, whose correction is fundamental to the smooth running of the sub-sector. For instance, the Ministry of Finance Planning and Economic Development (MFPED) continues to direct, control and superintend over the management of UETCL, UEDCL and UEGCL yet the operations and functions of these agencies fall within the purview of the Energy Ministry. This overlap in political supervision affects the performance of the sector institutions and must be urgently addressed. The MFPED should immediately relinquish its control of the UEB successor Companies to the MEMD.

Considering the central role electricity plays in the industrialization and socio-economic development of a country, it is therefore apparent that Government takes the necessary deliberate action to resolve the sector structural, institutional and legal challenges, whose long-term impact will continue undermine country's long term development goals as outlined in the National Development Plan and the Vision 2040.

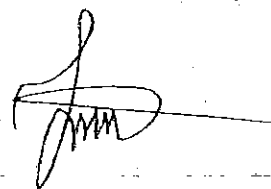
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To strengthen the sub-sector further, the current structural arrangement should be modified by introduction of an overarching corporate body, the Energy Regulatory Commission to replace the current Electricity Regulatory Authority (ERA)(with UEGCL UETCL and UEDL under it) while the Rural Electrification Agency is elevated to an Authority given its paramount role of extending electricity upcountry to the country.

The power distribution segment should be managed under a Public-Private Partnership framework with Government having atleast a 51% shareholding. It should be further broken up into various zonal areas that will attract competitive participation and the involvement of mainly home grown solutions just as is the case countries like Kenya and Ghana. These changes should be aimed at responding to the strategic and operational interests of Uganda.



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CHAPTER ONE

BACKGROUND TO THE INVESTIGATION

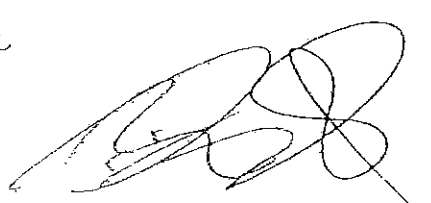
1.1 Background

This chapter states the Terms of Reference for the investigation, composition of the Adhoc Committee, scope of investigation and the methodology used during the investigation.

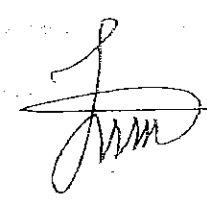
On the 21st of July 2011, Hon. Muhammad Nsereko, Member of Parliament (MP) Kampala Central, moved a motion for the creation of an Adhoc Committee on Energy (ACE) to investigate the Energy sector. This arose during the consideration of the Report of the Standing Committee on the Budget on the request by Government for Parliament of Uganda to grant authority to spend UGX 61 billion (Sixty one billion shillings) toward thermal power subsidy.

This was also precipitated by the numerous concerns raised by stakeholders about the persistent load shedding, high electricity tariffs, faulty billing systems, huge government subsidies towards thermal power generation and poor quality of service by Umeme Limited.

There was general concern by the House that substantial amounts of money had been sunk in the electricity sub-sector without corresponding improvement in service delivery. It was believed that the inefficient operations of the sector must be a precursor to the high level of electricity tariffs and hence the need for the unsustainable level of subsidy requirements from Government.

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Arising out of those concerns, there was resolution by the August House that the Rt. Hon. Speaker constitutes the Adhoc Committee on Energy and provides it with the requisite Terms of Reference. Consequently, Rt. Hon. Speaker appointed the Adhoc Committee on Energy under rule 164 of the Rules of the Procedure of Parliament of Uganda with specific Terms of Reference (ToR) to investigate the energy sub-sector.

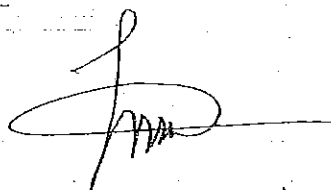
1.2 The Composition of the Committee

An eight member Adhoc Committee on Energy (ACE) of Parliament of Uganda, hereafter referred to as The Committee, was constituted by the Rt. Honourable Speaker on the 24th August 2011 and comprised the following:

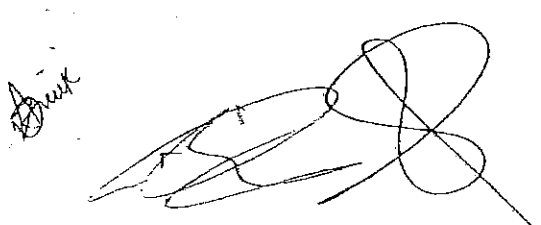
Hon. Oboth M. Jacob	Chairperson
Hon. Mulongo Simon	Member
Hon. Dr. Eng. Ajedra Aridru	Member
Hon. Lubega Ssegona Medard	Member
Hon. Nankabirwa Ann Maria	Member
Hon. Okupa Elijah	Member
Hon. Baryayanga Andrew Aja	Member
Hon. Amongi Betty Ongom	Member

1.3 Terms of Reference

In a letter dated 16th September 2011, reference AB 199/199/01 (Appendix I), the Rt. Hon Speaker issued the Terms of Reference to the Chairperson and Members of the Adhoc Committee on Energy. The Committee commenced investigation on 21st September 2011 and was tasked to assess the performance of the Energy Sector and in particular:-



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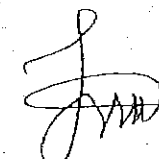



1. Investigate matters related to power losses, Tariffs, subsidies and power generation;
2. Scrutinize agreements between Government and Independent Power Suppliers with the view of determining whether the terms are favourable to Government and consumers;
3. Establish the extent to which the recommendations of the report of General Salim Saleh Committee on Tariff Review instituted in 2009, to investigate the energy sector have been implemented;
4. Investigate whether the management of Open Tender System on the purchase of oil products from Kenya has a bearing on production costs of generation of thermal electricity by the various power suppliers; and
5. Make such recommendations as the committee may consider appropriate and report back to the House within sixty (60) days.

1.4 Scope of the Investigation

The scope of investigation covered the period between 1999 to May 2012 in the following key areas of the electricity sub-sector:

- i. The performance of the energy sector.
- ii. The Power sector restructuring and reform process.
- iii. Agreements between the Government of Uganda and Electricity Producers/Suppliers.
- iv. Power losses, tariffs, subsidies/rebates, investments and power generation in general.
- v. Procurement and construction of hydro and thermal power generators.
- vi. The policy, legal and institutional framework.


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1.5 Method of Work

The Committee designed and agreed on a systematic method of work that enabled it collect, collate, triangulate and analyze information collected from diverse sources on the performance of the electricity sub-sector.

The Committee reviewed pertinent literature and generated specific questions that steered the investigation.

The Committee held a series of meetings with Government officials, the private sector operators, consultants and experts in the electricity sub-sector (Appendix II).

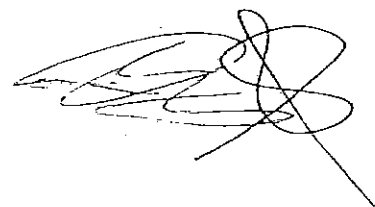
The committee carried out field or site visits to the electricity infrastructure projects; and undertook benchmarking visits to the Republic of Kenya and the Republic of Ghana to acquaint itself with the developments and performance of the electricity sector in these jurisdictions.

1.6 Challenges encountered during the investigation

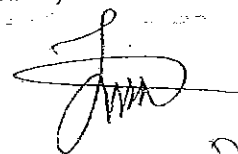
The Adhoc Committee encountered some challenges that need to be taken into account. The key challenges that bogged down the Committee's work included:

- i) **Complexity of matters under investigation:** The electricity sub-sector is not only wide but also technically complex. The committee found out that the scope and volume of work to be handled during the investigation was quite enormous. The matters the Committee was tasked to investigate are broad and complex, and therefore the necessity

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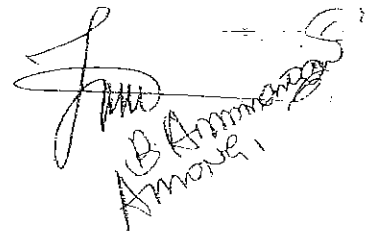
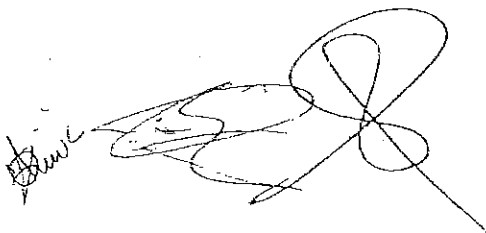
for ample time in which the Committee had to do and complete its work was overlooked. The number of documents reviewed, the diverse reference materials and cross section of witnesses examined and fact finding visits undertaken by the committee among others, explain why the assignment was bigger than anticipated.

ii) **None co-operative witnesses:** Considerable delays were also caused by reluctant or unwilling witnesses who were invited to appear before the committee but deliberately refused or failed to appear on the day(s) they were invited. In other cases some witnesses withheld key information asked of them. Ultimately, the Committee had to reschedule its program with the inevitable consequence of prolonging the time it was expected to complete its work.

iii) **Threats to members of Committee:** There were external forces especially those believed to be working for individuals and companies in the electricity sector who occasionally and vehemently threatened the members and technical staff on the Committee. Some of these threats were brought to the attention of the Police and other security agencies.

iv) **Competing Responsibilities:** Whereas members of the Ad hoc Committee on Energy demonstrated devotion and unquestionable commitment to the assignment given to them, it must be noted that they at the same time remained duty-bound to perform their Constitutional duties of legislation and representation. It therefore became apparent that members had to take time off to attend plenary and committee meetings, as well as their respective party programs.

v) **Counter/parallel government programmes:** Following the commencement of this investigation (possibly as a result of the



momentum generated by the inquiry) the electricity subsector witnessed several attempts by the Ministry of Energy to carry out abrupt reforms/programmes some of which were in direct reverberation of the Committee's Terms of Reference. For example, the commissioning of a review of the performance of the electricity sub-sector, a review and announcement of a new electricity tariff structure by ERA effective January 2012, closure of most thermal energy plants while Umeme Ltd hastily reduce energy loss rates and significant reduction in power outages at the time of submitting this report.

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CHAPTER TWO

THE ELECTRICITY SECTOR RESTRUCTURING AND REFORM PROCESS

2.1 Introduction

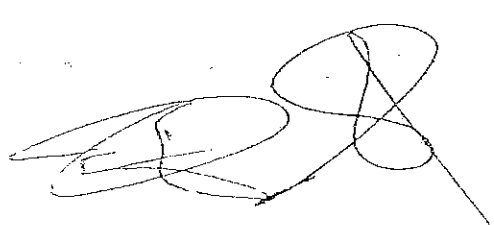
This chapter gives the background to the state of the electricity sector that led Government to institute a restructuring and reform process in the sector. It also states the key objectives of the reform process and its failures.

In order to contextualize the investigation, it was necessary to get a fair understanding of the background to the restructuring and reform of the electricity sector to discern the need for the ensuing agreements that would be under scrutiny in the next chapter. The chapter therefore, seeks to achieve that insight to build the case for subsequent analysis.

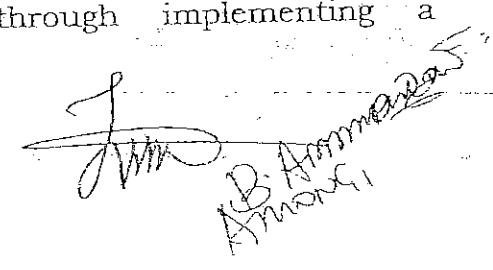
2.2 Background to the Restructuring and Reform Process

The electricity sector in Uganda underwent various reforms over the last two decades, associated with general liberalization of the economy and privatization of state enterprises. The reforms involved a rapid range of structural and institutional changes in which the Uganda Electricity Board (UEB), a state owned vertically integrated company, was unbundled into successor companies. Initially, UEB established in 1948, was responsible for all the aspects of power supply chain operations in Uganda.

Like many Government owned parastatals, UEB was overtime grossly mismanaged. By the late 1990's the Government of Uganda (GOU) had recognized that major efficiency improvements and expansion of access to electricity — could — be better accomplished through implementing a

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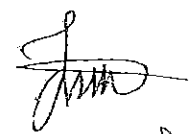
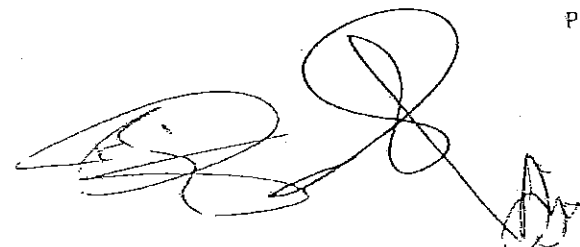
comprehensive power sector reform program which would place the electricity sector under private management, operated on prudent commercial principles.

Against the backdrop of a worsening state of the power sector, characterized by the dilapidated infrastructure, low levels of efficiency, high energy losses, low rates of revenue collection, limited investments, frequent power outages and load shedding, Government of Uganda with the assistance of the World Bank undertook comprehensive reforms in the electricity sector in 1999. The key objectives of the electricity sector reform included the following:

- i. Securing sustained, efficient and affordable electricity power supply for domestic, commercial, industrial and other uses;
- ii. Attracting significant private sector participation or investment in the power sector;
- iii. Increasing access to electricity through additional customer connections with the existing infrastructure and through the Rural Electrification Programme;
- iv. Removing real or perceived monopolistic structures in the sector and thereby create market conditions that would make for competition for services;
- v. Achieving transparency in the regulation of power utilities;
- vi. Improving the reliability and quality of electricity supply through improved monitoring and supervision of the sector and improved quality of services;
- vii. Making the power sector financially viable and able to perform without subsidies from Government budget;
- viii. Meeting growing demand for electricity and increasing coverage; and
- ix. Taking advantage of export opportunities after satisfying local demand.

The above gave rise to the formulation and enactment of the new electricity Act of 1999, Cap 145, as part of the reform process, which among other outcomes

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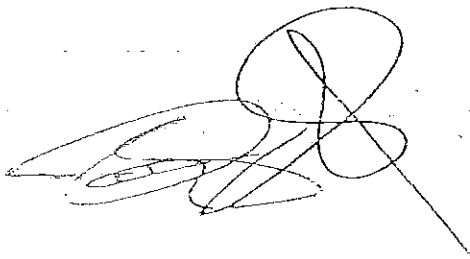


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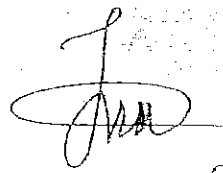
led to the unbundling of UEB in 2001. The unbundling of the Uganda Electricity Board led to the creation of three successor companies namely: Uganda Electricity Generation Company Limited (UEGCL) responsible for power generation; Uganda Electricity Transmission Company Limited (UETCL) responsible for power transmission; and Uganda Electricity Distribution Company Limited (UEDCL) responsible for distribution of power to consumers.

A new legal and regulatory framework that would now oversee the newly disintegrated utility with the separate Generation, Transmission and Distribution segments was formed with the Electricity Regulatory Authority (ERA) established in 2001 to provide the desired regulatory oversight. ERA, the independent regulator was to oversee the operations of the sector, setting the electricity tariffs, issuing Licences to generation, transmission and distribution companies and setting technical standards among others. Key among the expectations in the new arrangement was that the generation segment would be enhanced through private sector investments; distribution segment would be leased to the private sector and that the transmission segment owing to its strategic importance would be retained as a public entity.

In order to attract foreign director investment (FDI) in to the electricity sector, the Government of Uganda engaged UMEME Ltd as a private sector concessionaire to restore, rehabilitate, expand, operate and maintain the Uganda distribution network owned by UEDCL. The electricity generation segment was leased to M/s Eskom Limited while the electricity transmission segment was retained by UETCL to be managed as a Public entity. While the reforms resulted in some FDI in flows, the Government has over the years (until 2012) continued to subsidise the electricity sector due to the high cost of power generation especially the diesel fired thermal power plants.

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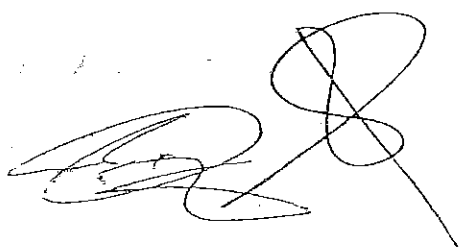
The hydrology on Lake Victoria is reported to have deteriorated in 2005, which reduced hydro power generation at the Nalubaale and Kiira dams in Jinja from installed capacity of 270mw to about 140mw in 2011. In order to minimise the impact of reduced hydropower generation, the Government of Uganda was compelled to engage Aggreko, Jacobsen and later Electromaxx to supply emergency power using light fuel oil, known as automotive gas oil (AGO) and heavy fuel oil (HFO) or diesel between 2005 - 2008.

More than ten years after the reforms into the power sector were carried out, the generation capacity output at the main Kiira-Nalubale hydropower dropped from a high 270MW (when Eskom took over) to a low generation output of 140MW, while the distribution segment is still characterized by dilapidated infrastructure in most areas (despite a claim by UMEME Ltd to have invested \$130million in the network), high energy losses, high levels of government subsidies (until Feb 2012), poor quality of supply and energy utilization inefficiencies.

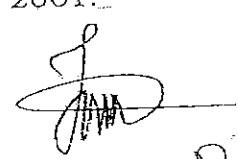
The poor performance of the electricity sub-sector is mainly attributed to a long span of limited capital investment, over hedging by the private sector and increased power demand.

The committee was informed that Government has made efforts to improve the performance of the sector by putting in place among others, the following:

- i) The Hydropower Development Master Plan.
- ii) The Plan to Supply Power to the country in the short, medium and long term 2005/06.
- iii) The Rural Electrification Strategy and Plan 2001.

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- iv) The Energy Policy 2001.
- v) The Renewable Energy Policy 2007.
- vi) The Power Sector Investment Plan 2011.
- vii) The Hydropower Development Master Plan 2011.

2.3 Challenges to the Electricity sub-sector

Notwithstanding the efforts above, the electricity sub-sector is still registering poor performance and is characterized by a lot of irregularities. This poor performance can be explained by the following:

i. Inadequate and unreliable power supply

By 1999, power generated in Uganda stood at 180MW. From 2005, the energy demand in Uganda has grown at an average rate of about 10% per year. This has been largely driven by increased economic growth. However, the energy supply has not increased correspondingly to meet the demand. This was also exacerbated by drought in 2005/06 which is said to have led to a drop in water levels in L. Victoria resulting into reduced discharge of water from Nalubaale and Kiira Hydropower Plants. This created an energy deficit which led to the electricity crisis in the country leading to severe load shedding. Government was then compelled to engage Aggreko, Jacobsen and Electromaxx to supply emergency thermal power. Later on, some small hydro and cogeneration power plants were also brought online.

Additionally, delays in the completion of Bujagali and other Mini-Hydropower plants compounded the problem of energy crisis. Consequently, the Government was compelled to continue using thermal generation plants longer than earlier anticipated.

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ii. Weak Governance structures and overlap in supervisory role

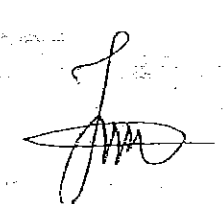
The reforms in the energy sector in the late 1990s and the entire process of unbundling UEB were largely driven, controlled and dominated by the Ministry of Finance, Planning and Economic Development (MFPED); particularly the Privatization Unit (PU). The sector ministry i.e Ministry of Energy and the Electricity Regulatory Authority (ERA) instead played a peripheral role. At times they were just co-opted to the extent that their expert views were ignored. The MFPED, Privatization Unit in particular, dominated the procurement and negotiation of the power generation and distribution concessions with minimum or no input from the relevant line Ministry and ERA.

As much as the MFPED was mandated under the PERD Act to spearhead the privatization process of UEB, this did not entail the retention of ownership, control and management of the successor companies which undermined the role of the line Ministry of Energy and Mineral Development. The MFPED does not have the requisite technical capacity to supervise, monitor and guide the UEB successor companies whose functions and duties fall within the mandate of the Ministry of Energy and Mineral Development.

To-date the Minister of Finance still appoints and disbands the Boards and Management of UEGCL, UETCL and UEDCL, which makes these key players in the energy sector pay greater allegiance to the MFPED other than the sector Ministry of Energy and Mineral Development.

Given that the Ministry of Finance owns the shares of the successor companies and controls the boards, the role of the line Ministry of Energy is undermined.

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iii. Inadequate Sector financing

The development of electricity infrastructure (generation, transmission and distribution infrastructure) requires huge capital investments. The Committee established that the industry/global average financial requirements each Megawatt of hydro electricity generation stands at US\$2.9Mmillion while the same amount of thermal power generation costs ten times. Whereas Government has over the years made commendable investments in the sector, the increasing demand for electricity due to population growth and economic growth calls for a lot more capital investment in the sector to meet the growing demand.

iv. Weakness of the Sector Regulatory Body

The Electricity Act, 1999 provides for the creation and functioning of the Electricity Regulatory Authority (ERA) as an "independent" organization to regulate the affairs of the electricity sector. Apparently, it is evident that the Authority has failed to effectively regulate, provide the necessary technical guidance and ensure compliance with the sector regulations as envisaged in the Act. On several accessions ERA has acted under the direction, manipulation and control of the sector Minister or other sector players. The Auditor General's report on Electricity Sub-Sector (2012) Volume II shows that the composition of the ERA Board was not done in accordance with the Act with respect to qualifications, expertise and conflict of interest issues.

A review of ERA's financial and human resources shows that ERA is not well resourced to execute her mandate. The revenue sources for ERA are limited and therefore, the Authority is incapable of generating enough resources to facilitate execution of its mandate. The secretariat is not well staffed with several positions vacant in the key departments as well

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as some being occupied in acting capacities. The Chief Executive Officer who had acted in the post for more than one and a half years was just recently substantively appointed.

Over seven years into the power distribution concession, ERA has failed to ensure the development of the Restoration and Rehabilitation Plan, the Investment Determination and Verification Guidelines and also failed to establish a clear mechanism for determining technical and commercial losses.

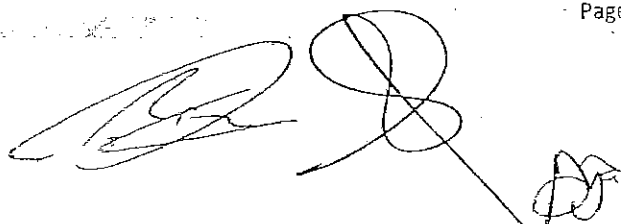
v. External control of the reform process in UEB

The Committee found out that the reform process in UEB was from the onset managed, directed and controlled by Eskom of South Africa, a government controlled company that had business interest in Uganda's power sector. It was this same company that subsequently took over the power distribution concession in a consortium comprising of itself, Eskom (44%) and Globeq(56%) under a special purpose vehicle known as UMEME Ltd in 2004.

Between 1999-2001, the Ministry of Energy and Mineral Development (MEMD) contracted the services of Mr. Paul Mare, a South African national as "a billing expert" after being seconded by his employer Eskom South Africa. Mr. Mare oversaw the unbundling of UEB into the successor companies and the subsequent concessioning of the power generation and distribution to Eskom(his employer back home in South Africa). After the unbundling of UEB, Mr. Paul Mare served as MD of Eskom (U) Ltd between 2001-2005, and UMEME Ltd between 2005-2009.

Given the employment record of Mr. Paul Mare who held senior positions in UEB, Eskom and UMEME Ltd, it is clearly evident that he covertly worked for and served the interests of Eskom and UMEME Ltd

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and therefore, the information he provided on energy losses before the unbundling of UEB did not reflect the actual status at the time and it debased the values of the successor companies.

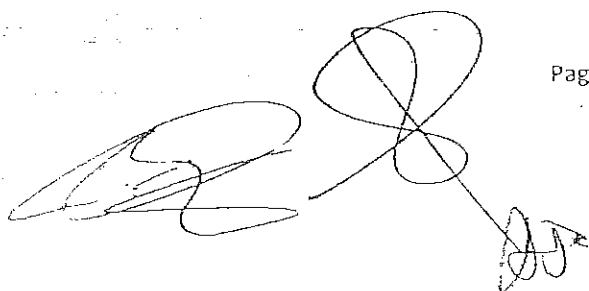
Regrettably, Government did not carry out a prudent and independent study on the baseline of critical factors like power losses before UMEME Ltd took over the power distribution concession in 2004, but instead relied on the information provided by this "billing expert" called Paul Marell. A more measured rate of engagement and independent verification by Government would have mitigated the current discordance in the energy sector arising from the distorted level of losses.

vi. High Oil prices and fluctuating exchange rates

The thermal power generation plants in Uganda have been running on AGO (diesel) and Heavy Fuel Oil (HFO) which fuel commodities have witnessed a sharp increase in prices reaching a record high in recent times. This increase in fuel prices (by about 87% per litre) has had far reaching effect on the end-user tariff since fuel is used as a pass through cost. As a result, Government has been intervening by financing the shortfalls to subsidize the electricity tariff to consumers. Between 2006 and June 2011, Government of Uganda paid UGX 1.1trillion as subsidies to thermal power plants.

The Committee also noted that since the introduction of emergency thermal power generation in 2005, the USD to UGX exchange rate has significantly increased from 1700 to 2500 Shillings to the Dollar. It is imperative to note that whereas the electricity tariff is denominated in Shillings, most of the costs of power generation (hydro and thermal) are denominated in USD. To recover these costs, which are most times

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exaggerated by the investors and the bureaucrats in the sector, Government has had to adjust the tariff upwards.

The tariff structure therefore, responds to the foreign exchange fluctuations and in a bid to have a fairly affordable tariff, Government has always moved in to heavily subsidise the sub-sector.

vii. Exaggerated distribution Losses

Uganda continues to post the highest power distribution losses in Eastern and Southern Africa and one of the highest in the world¹. The power loss factors have for a long time hovered between 38% and 40%, until 2009 (following the Gen. Saleh Inquiry), when UMEME Ltd drastically reduced the losses to 28%. The exaggerated level of losses significantly impacts on the end-user tariff.

viii. Existence of Subsidies in the Sector

The reform process was meant to make the electricity sector financially viable and able to perform without subsidies from Government. However, it was found that since 2005 Government has been subsidising for electricity in order to keep the end user tariffs to affordable levels. The subsidy contributions by Government were stopped in May 2012 after it was realised that a total of Shs.1.99 trillion had been spent on subsidies 36% of which was compensation for declared losses by Umeme Limited and 24% for profit on declared but unverified investments and the balance for electricity generated by emergency diesel thermal power generators from 2005 to 2012. This money could have been used for construction and expansion of the electricity infrastructure.

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ix. Existence of Monopolistic Structures in the Electricity Sector

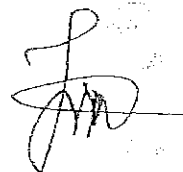
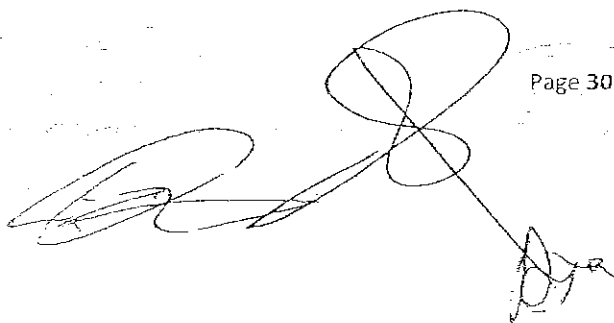
One of the key objectives of reforming the power sector was to remove monopolistic structures and thereby create market conditions that would make for competition and provision of quality services for the customers. However, to-date monopolistic structures in the sector still exist. For example, in the electricity distribution segment, Umeme Limited controls 99% of the market share whereas the new companies in this segment only have 1% of the market share and are based in rural areas. The nature of the agreements that were entered into with Umeme Limited, gave the company monopolistic advantages. Given the territorial advantage of Umeme Ltd no electricity distributor can effectively compete with it in a way that would compel Umeme make improvements on the distribution network, efficiency in service delivery and reduction of distribution losses.

x. x. High Electricity Tariffs

It had been expected by Government, the electricity consumers and the general public that the coming in of a private Company to manage the distribution network would result into expansion of the network, efficiency and lower tariffs, but this has not been the case. The Committee found that since the taking over of power distribution by the private company, electricity tariffs have continued to rise and Uganda's domestic tariff ranks the highest in Africa, and second highest in the world.

The privatization of the electricity distribution segment has therefore, not resulted into affordable electricity for domestic, commercial or industrial users who have continuously complained about the high electricity tariffs. Suffice to note, high electricity tariffs adversely affects industrialization and the competitiveness of Ugandan products on the international market.

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xi. Low Access Levels to Electricity

Since 2005, the demand for energy in Uganda has been growing at an average rate of 10% per annum. However, electricity generation and supply has not increased correspondingly to satisfy the demand. Currently only 12% of the country has access to electricity supply with only about 450,000 customers connected due to limited investment in the expansion of the electricity transmission and distribution networks. Much as the Rural Electrification Agency (REA) receives reasonable funding from various Development Partners, there is no adequate mechanism to ensure value for money. According to information accessed by the committee, a total of US\$145 million has been injected by the Development Partners and GOU towards expansion of the power network in the rural areas in the period 2004 - August 2012 with no value for money audit available.

Conclusion

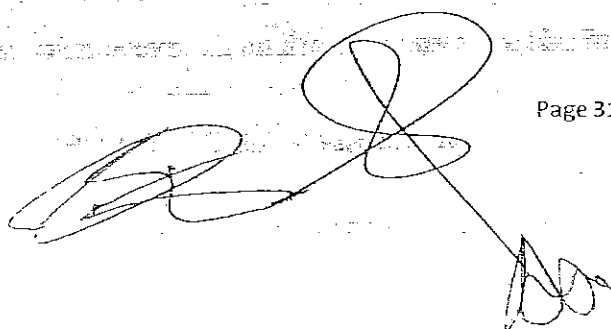
Whereas Government has made commendable efforts especially since the late 1990s through initiating among others, structural, institutional and legal reforms in the electricity sub-sector, it is apparent that the objectives of these reforms have not been substantially realized. For example, the sector still faces inadequate funding, limited connectivity while the power distribution system is still characterized by dilapidated infrastructure in most areas (despite a claim by UMEME Ltd to have invested \$130million in the network), high energy losses, high levels of government subsidies (until Feb 2012), poor quality of supply and energy utilization inefficiencies.

The Committee recommends that:

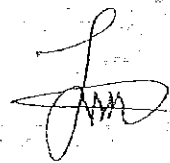
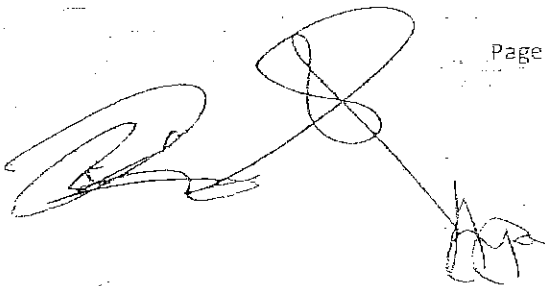


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- i. The Ministry of Energy and Mineral Development should develop a comprehensive and dynamic energy resource plan to guide and ensure effective coordination and execution of energy projects in the country.
- ii. Government should prioritise and explore other options of increasing funding and investment in the development of power infrastructure and develop alternative sources of energy.
- iii. The Auditor General conducts a comprehensive value for money audit of all the Rural Electrification projects undertaken by REA since 2004 to-date, where about US\$145million has been injected towards expansion of the power network in the rural areas and no value for money audit has been carried out. The audit should cover the technical, financial, project tendering and award processes.
- iv. There is urgent need to rehabilitate the power distribution network in order to reduce on energy losses.
- v. In a bid to improve/streamline the governance of the electricity sub-sector, the MFPED should immediately relinquish the supervision, control and management of the UEB successor companies to the sector ministry MEMD, which has the technical competence for oversight.
- vi. There is need for restructuring the ERA to provide for critical positions and skills to effectively execute its regulatory mandate.
- vii. ERA must rise to challenge to oversee, control and regulate the sub-sector without fear or favour in accordance with the Electricity Act.



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CHAPTER THREE

REVIEW OF MECHANISMS FOR DETERMINING TARIFFS, POWER LOSSES, SUBSIDIES AND POWER GENERATION

3.1 Introduction

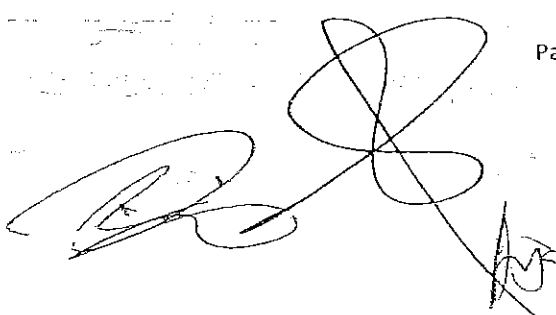
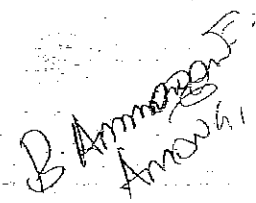
This chapter specifically addresses the Term of Reference requiring investigation on matters related to tariffs, power losses, subsidies and power generation. The chapter is structured into four sub-sections in which the above mentioned issues are discussed separately.

3.2 Objectives

- i. To review the determination of bulk supply tariffs (BST) and end user tariffs and analyze their trend since 2005.
- ii. To review the mechanism for determining power losses and analyze their trend since 2005.
- iii. To review and ascertain the level of Government expenditure on subsidies since 2005.
- iv. To review the modes of power generation in Uganda and ascertain the investment and construction costs of the ongoing power projects.

3.3 Tariffs

A tariff is a price a customer has to pay to a provider to obtain services or supply of a product. In the case of this investigation, a tariff is a unit price for supply of electricity. In Uganda the mandate to determine electricity tariffs is vested with the Electricity Regulatory Authority which has issued the Electricity (Tariff Code) Regulations, 2003 under section 120 of the Electricity



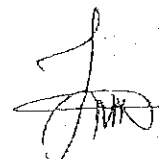
Act, 1999. According to these regulations a tariff is computed for every license issued by ERA for operators in the supply chain.

For the power supplied through the grid, electricity prices are set at three points in the industry:

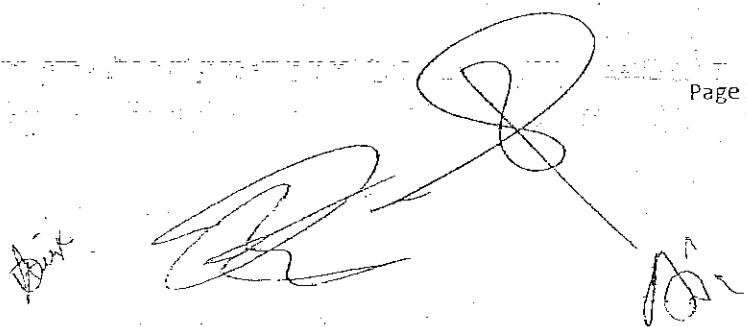
- i. At the interface between generation and transmission (Generation tariff);
- ii. At the interface between transmission and distribution (Bulk Supply Tariff); and
- iii. At the interface between distribution and end user consumers (Retail Tariff).

The Uganda Transmission Company Limited (UETCL) is the single buyer of electricity supplied to the transmission network in Uganda and the sole exporter and importer of electricity. The prices charged by the generation company (Eskom Uganda Ltd.) for power supplied to UETCL are negotiated between the two companies in a form of a Power Purchase Agreement (PPA), which is subject to oversight and approval by ERA. The transmission company, UETCL, then sells power to any electricity distribution company, like Umeme Limited, that is connected to the transmission network at a Bulk Supply Tariff (price). The Bulk Supply Tariff (BST) reflects the costs of power generation and transmission. UETCL can export power at specially negotiated prices, but not below either the average or marginal cost of power purchase.

The electricity distribution company purchases power at the Bulk Supply Tariff and sells it to end users following an approved tariff schedule by ERA. The end user tariffs reflect the cost of power purchase as well as the cost of distribution and retail.



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3.3.1 Tariff Setting Model

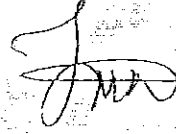
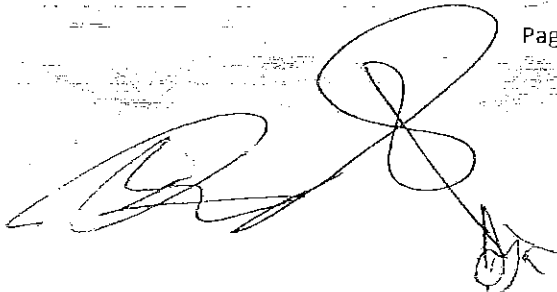
Tariff setting for Eskom (U) Ltd., UETCL and Umeme Limited is done by ERA using a tariff model. An in-depth review of the tariff methodology in order to get an insight in the determination of end user tariffs, bulk supply tariff (BST) and power losses and also compute the level of Government expenditure could not be done by the Committee. This is due to the technical and mathematical nature of the tariff model. And also the level of effort and expertise required understanding the tariff model in order to address this objective significantly exceeded that was envisioned. A simpler approach to investigate the determination of tariffs was therefore, considered.

The tariff levels are estimated in accordance with the total revenue requirements of the regulated and licenced entities. Revenue requirements of the regulated businesses are meant to compensate the companies with respect to the following:

- Allowed expenses that include cost of sales, operation and maintenance costs, concession or lease payments and regulatory fees,
- Investment component that includes capital recovery for investments undertaken and to be undertaken in future, a return on investment (ROI) and applicable taxes, and
- Other expenses not covered by the above such as any allowed adjustments, performance incentives, etc.

The end user tariff structure is then designed taking into account the tariff levels and the costs of supplying the various consumer categories (i.e. domestic, commercial, medium industrial, large industrial, very large customers and street lights).

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The tariff applicable to power generation companies (except for Eskom Uganda) is negotiated between UETCL as the single authorized and licenced buyer and developer and is spelt out in a Power Purchase Agreement approved by ERA.

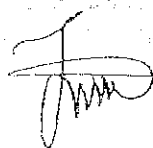
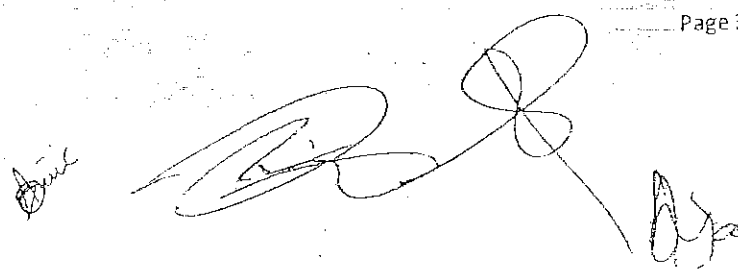
Renewable energy feed-in tariffs for Independent Power Providers are determined by ERA and published on the ERA website. They provide an indication of what developers expect to receive from technology applied for renewable energy projects.

The end user tariff generally includes the following cost categories:

- i. Power acquisition related costs,
- ii. Operations and maintenance costs,
- iii. Investment related costs,
- iv. Return on investment,
- v. Adjustment factors, for system losses (commercial and distribution), inflation and exchange rate fluctuations, and
- vi. Tax assumptions
- vii. Uncollected debt parameters
- viii. Other costs as approved by ERA

In setting the end user tariff, the following objectives are put into consideration:

- i. To provide consumers with fair and reasonable price structures consistent with maintenance of a financially and operationally secure electricity supply system;
- ii. Encourage consumers to make efficient use of energy based on price signal;
- iii. Encourage operators to make efficient use of plant (assets) and operational efficiency based on financial benefits and penalties;



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- iv. Provide operating companies reasonable return/ profit to give confidence to current investors and attract new investors;
- v. Provide a tariff structure for cost reflective tariff for each customer group; and
- vi. Provide for future progress towards a commercially competitive system.

Simplified Approach to Tariff Determination

In this approach, high inefficiencies in electricity distribution segment impacts on the end user tariffs. While high electricity distribution losses also lead to high end user tariffs because of the revenue requirement.

The simplified formula used to determine the tariffs is as follows:

$$\text{Tariff} = \frac{\text{Total Revenue Requirement (TRR)}}{\text{Number of Units of energy sold}}$$

Where,

$$\text{TRR} = \text{Costs of Generation} + \text{Costs of Transmission} + \text{Costs of Distribution}$$

And,

$$\text{Number of units of energy Sold} = \text{Number of units Generated} - \text{Number units of energy Lost}$$

Therefore,

$$\text{Tariff} = \frac{\text{Total Costs of Generation} + \text{Transmission} + \text{Distribution}}{\text{No of Units of Energy Generated} - \text{Number Units of Energy Lost}}$$

For example:

Suppose the Total Revenue Requirement (Cost, C) = 100

Total units of energy generated (G) = 100 and

Units of energy lost (L) are 32% of total units of energy generated = 32 (where 5 units are lost in transmission and 27 units lost in distribution)

Therefore,

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$$\text{Tariff} = \frac{C}{G - L}$$

$$\text{Tariff } T_1 = \frac{100}{100 - 32} = \frac{100}{68} = 1.47$$

Now assume that units of energy lost come down to 16% (i.e. reduced from 27% to 11% in the distribution segment) of total units generated.

$$\text{Tariff } T_2 = \frac{100}{100 - 16} = \frac{100}{84} = 1.19$$

In percentage terms, a reduction in tariff from 1.47 to 1.19 would be 19%.

The Committee was informed that a 1% reduction in the tariff leads to an approximate saving of US\$3 million per annum. Therefore, in the above example, 19% reduction in the tariff would lead to a saving of US\$57 million per annum.

Other cost drivers include the high costs of generation that were occasioned by a substantial component of Emergency Diesel thermal generation in the energy mix at the time of the investigation. In particular the cost drivers are attributable to high fuel prices (for Emergency Diesel thermal generators), high supply logistical cost (freight, insurance) and the depreciation of the shilling have an impact on the tariff.

3.3.2 Structure and Trend of Electricity Tariffs

The trend of electricity tariffs between 2005 and up to August 2012 for various categories of consumers are shown in Table 3.1 below.

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Table 3.1: Trend of End-User Retail Electricity Tariffs (Shs /kWh) 2005-2012

	Domestic Consumers	% Change	Commercial Consumers	% Change	Medium Industrial	% Change	Large Industrial	% Change	Street Lights	% Change
1st January 2005	171.4		164.8		150.3		60.4		162.6	
1st April 2005	212.5	24	204.4	24	178.9	19	71.9	19	201.5	24
1st January 2006	216.9	2	208.6	2	190.2	6	76.4	6	205.6	2
1st June 2006	298.2	37	286.8	37	261.5	37	120.8	58	282.8	38
1st November 2006	426.1	43	398.8	39	369.7	41	187.2	55	403	43
1st January 2010	385.6	-10	358.6	-10	333.2	-10	184.8	-1	364.3	-1
15th January 2012	524.5	36	487.6	36	458.9	38	312.8	69	488.7	33
Cumulative % Increase		133%		129%		132%		206%		131%
Source: Electricity Regulatory Authority										

The end user tariffs have generally been on the rise since 2005 when Umeme Limited got the electricity distribution concession. The cumulative percentage increase in the end user tariffs for domestic consumers since 2005 to date is 133% while that for commercial consumers rose by 129%. The cumulative percentage increases in end user tariffs for medium industrial and large industrial consumers were 132% and 206% respectively. And the cumulative percentage increase in tariff for street lights is 131% since 2005.

According to ERA, end user tariffs in Uganda remained fixed over a period of time from November 2006 to January 2010 and were not adjusted to reflect the then prevailing circumstances. As a result, the end user tariffs were not reflecting the true cost of providing the service, with the shortfall of the sector revenue costs being met by GOU in form of subsidies.

3.3.3 The Move to Automatic Tariff Adjustment

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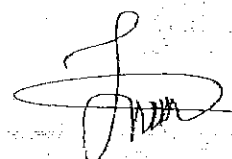
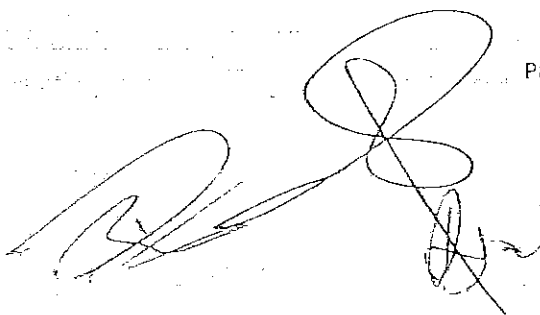
According to ERA, the energy sector will begin to operate a mechanism called 'Automatic Tariff Adjustments' as communicated earlier in January 2012 during the tariff review. Automatic Tariff Adjustments is a process by which the current tariff (BASE Tariff) is adjusted for changes in Inflation, Exchange Rates and Fuel Prices in proportion to the contribution of each in the energy mix. The costs of these inputs are already factored in the BASE Tariff. It is the changes to the price/cost of these inputs that will be reflected in these adjustments on a monthly basis.

The reasons for the introduction of Automatic Tariff Adjustments according to ERA include:

- i. Automatic Tariff Adjustments is not a new Policy on tariffs because adjustments have always been made to take care of these factors.
- ii. The difference is that in the past, the effects of these adjustments have been met through Government of Uganda subsidies.
- iii. In the January 2012 tariff review, Government removed subsidies from electric energy consumption in order to accelerate capital (long term Investment) in electricity infrastructure in priority projects such as Karuma Hydro Power Project (600MW), Isimba Hydro Power Project (120MW), and the transmission infrastructure among others.

Government of Uganda's decision to invest in capital projects such as named above benefits consumers for a longer period than end user consumption; however, it's important to note that Government is meeting the capital costs for Jacobsen Power Plant based in Namanve and Capital payments for Electromaxx (U) Ltd based in Tororo. These two remained in the energy mix as part of the strategy to ensure security of supply.

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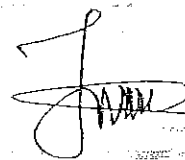


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The overall effect of Automatic Tariff Adjustments will be movements upwards or downwards on the final consumer tariff due to changes in Inflation, Exchange rates and Fuel Prices. The tariff will reduce when the Uganda Shilling appreciates against US Dollar and when fuel prices reduce and vice versa. Consumers will benefit when costs reduce. Companies/utilities will be allowed to recover additional costs incurred.

3.3.4 Findings

- i. The tariff methodology states that some of the targets i.e. target loss factor, provide strong incentive for improved performance by the utility Companies. However, this has not been the case for energy losses by electricity utility operators in Uganda. By the end of 2010, 33.4% of energy generated was lost in Uganda compared to only 16% in Kenya. The retail tariff in Kenya was 17.04 U.S cents/kWh (unsubsidized and fully cost recoverable) while that in Uganda stood at 13.89 U.S cents/Kwhr and was heavily subsidized at 44.6%, and therefore not fully cost recoverable.
- ii. With the exaggerated cost of generation for both hydro and Emergency Diesel thermal power plants, the inclusion of unrealistic operation and maintenance costs of the distribution concessionaire in the tariff computation and other would be disallowable costs, the Committee was, therefore, not surprised that Uganda has one of the highest end-user tariffs in Africa.
- iii. The power tariffs have remained at unsustainable levels and are the highest when compared with other countries within the region as shown in Table 3.2 below.


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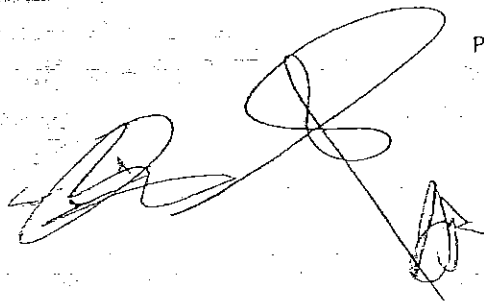


Table 3.2: Comparison of End User Tariffs in Uganda With Those of Selected Countries.

(Tariffs for selected countries have been converted to Uganda Shilling Equivalent)

	DOMESTIC	COMMERCIAL	MEDIUM INDUSTRIES	LARGE INDUSTRIES	EXTRA LARGE INDUSTRIES	STREET LIGHTING
	CUSTOMERS	CUSTOMERS	CUSTOMERS	CUSTOMERS	CUSTOMERS	
COUNTRY	(Shs./kWh)	(Shs./kWh)	(Shs./kWh)	(Shs./kWh)	(Shs./kWh)	(Shs./kWh)
UGANDA	524.5	487.6	458.9	312.8	-	488.7
KENYA	244	235	151	124	108	197
TANZANIA	205	205	205	135	126	205
GHANA	305	371	379	300	275	395

Source: Electricity Regulatory Authority(Uganda), Energy Regulatory Commission(Kenya), Tanzania Electricity Supply Company(TANESCO), Energy Commission Ghana


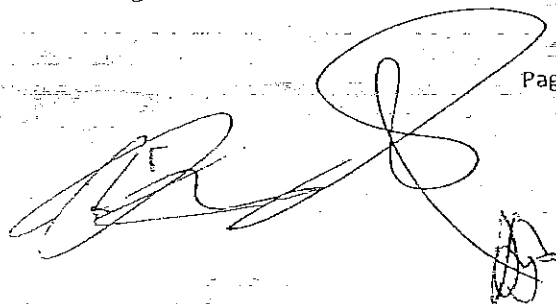
iv. The cumulative end user tariffs have risen by an average of 130% for domestic, commercial, medium industrial and street lighting customers since 2005. For large industrial customers the tariffs has risen by 206% cumulatively since 2005. This high rise in tariffs is contrary to one of the objectives of the reforms in sector where electricity is meant to be affordable by the consumers.

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- v. Umeme Limited currently gets a return on investment (ROI) of 20% per annum incorporated in the tariff. A return on investment of 20% per annum is high considering that interest rates charged by international financial institutions are hardly above 10% per annum. For example, Umeme Limited pays 8.5% for a loan obtained from International Finance Corporation (IFC).

3.3.5 Observations

- i. It was observed that high inefficiencies in the distribution segment had a major impact on the end user tariffs since they are factored in the tariff computation model.
- ii. High distribution losses that have hovered between 38% and 28% from 2005 to 2011 have led to high end user tariffs since these are considered during tariff computation. The main electricity distributor has no incentive to bring down these losses drastically since it is compensated through the tariff. The higher the energy losses the bigger the amount of compensation, given that a 1% loss is compensated with equivalent of USD4million per annum through the tariff.
- iii. The tariff setting model is complex one and not user friendly for the ordinary stakeholder.
- iv. The Committee also observed that ERA is set to introduce Automatic Tariff Adjustments beginning 1st October 2012. In case of very high depreciation of the Uganda shilling against the convertible currencies, high inflation rates and high price spikes of fuel in the international markets as were experienced last year, the automatic tariff adjustment lead to tariffs to go beyond affordable levels and thus cause anxiety among the consumers.



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3.3.6 Conclusion

High power tariffs are disastrous to the national economy in that production cost increases reduce the competitiveness of the local manufacturers at both local and international markets. And also high tariffs leads to power theft as most of the consumers cannot afford to pay for expensive electricity.

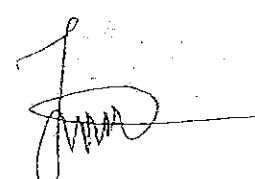
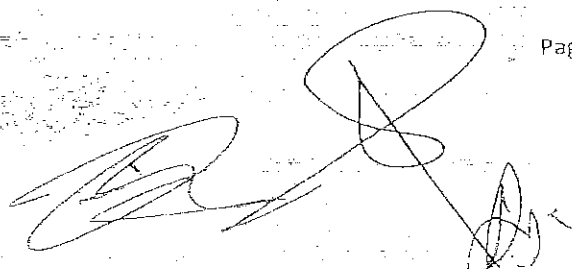
The Committee recommends that:

- i. The Auditor General carries out a forensic audit of the Tariff Review Methodology to ascertain among others, the disallowable costs which are the biggest cause of abnormal tariffs.*
- ii. The tariff setting model, must as a matter of necessity, be transparent and subjected to extensive stakeholder review over a specified period of time, not exceeding six months, sufficient to obtain stakeholder buy-in.*
- iii. ERA should first undertake nationwide Stake holder sensitization on the Automatic Tariff Adjustment billing scheme before its implementation since this may have far reaching consequences that are detrimental to the economy.*

3.4 Power Losses

One of the key objectives of the reforms in the electricity sector in the late 1990s was to reduce power losses. Power losses occur along the electricity supply chain from generation, transmission to distribution. At the transmission level, only technical losses are realized while at the distribution level both technical and non-technical (or commercial) losses are realized.

According to the Electricity Regulatory Authority, technical losses occur naturally and consist mainly of power dissipation in electricity system



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components such as transmission and distribution lines, transformers and measurement systems. Technical losses are valued at generation costs. The main contributors to technical losses include electrical losses due to theft and illegal connections, inadequate conductor capacity, and administrative losses. The level of technical loss depends on many variables including voltage levels and network design but ranges generally between 3% and 8%.

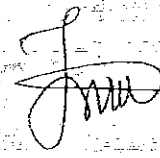
On the other hand, the non-technical or commercial losses are a result of administrative shortcomings by the utility operator with respect to inadequacy of the billing system, non-collection of bills, vandalism and power theft, meter tampering and estimated meter readings.

3.4.1 Status of Power Losses

Losses in the electricity distribution system are established as Energy Produced Less Energy Sold. If energy produced is, say, 100 units and only 80 units are sold to the consumers; therefore, 20 units are lost representing a 20% power loss.

According to ERA, by January 2006 the level of distribution losses (i.e. technical and non-technical) were ranging between 34% and 35%. The technical losses were between 14% and 17% while the non-technical losses ranged from 16% to 19%. By 2008, both the transmission and distribution losses stood at 40% and they were the highest in the continent. At that time the total power generation was about 250 MW and losses of 40% meant that 100 MW, including the expensive thermal power, ended up in losses.

Uganda continues to post the highest distribution power loss levels in the region and one of the highest in the world standing at 28% by 2011. And yet at the time Umeme Limited took over from UEDCL, power losses had reduced to about 27%. When compared with other Nile Basin countries namely; Kenya,

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Tanzania, Rwanda, Burundi, Sudan, Ethiopia and Egypt, Uganda has the highest power losses. Egypt on the other hand has the lowest losses at 12% while Burundi followed Uganda with total losses of 24%. The other six countries had losses ranging from 16% to 20%.

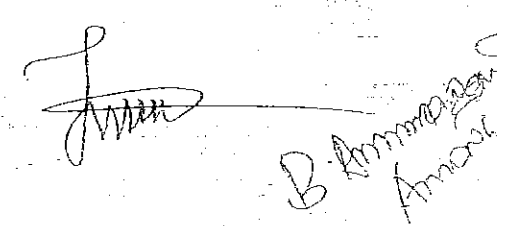
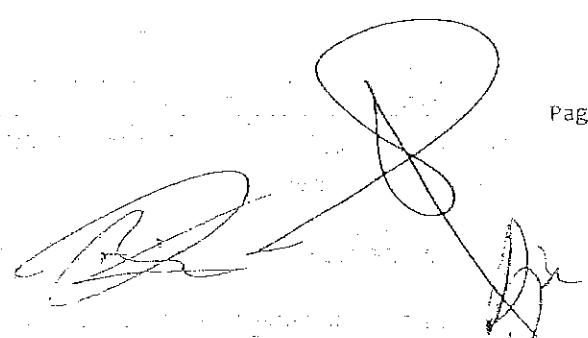
3.4.2 Trend of Distribution and Transmission Power Losses

At the time of take-over from UEDCL in March 2005, the starting level of distribution losses allowable to Umeme Limited for the first year of operation was tentatively set at 33% and was expected to be reducing by 0.83 percentage points per annum to reach 28% in the seventh year as per schedule A-4 to Annex A of the Distribution Supply License. Whereas Umeme Limited has made significant efforts towards improvement in collection rates, ERA and Government of Uganda in general is concerned that the level of distribution losses, which impact on tariffs, has remained relatively high compared to the levels of losses pertaining in other countries in Sub-Saharan Africa which have similar characteristics to the Ugandan economy.

In addition, Government of Uganda is concerned that if losses are not significantly reduced, the benefits from any additional generation may not be realised. For each percentage point of power loss, US\$3.2 million is lost annually. This means that for the non-technical (or commercial) losses estimated at 20%, US\$64 million (about Shs.160 billion) is lost annually. With such a magnitude of losses, efforts to improve power supply are greatly impeded.

For the period 2005 to 2011 the distribution losses as measured by Umeme Limited are as shown in Table 3.3 below.

Table 3.3: Trend of Umeme Distribution Losses from 2005 to 2011



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Year	2005	2006	2007	2008	2009	2010	2011
Set Distribution Losses Targets	33.0%	32.2%	31.3%	30.5%	29.7%	28.8%	28.0%
Distribution Losses Targets Used In Tariff	33.0%	32.2%	31.3%	34.1%	31.7%	28.2%	27.2%
Actual Distribution Losses	38%	34%	35%	34%	35%	30%	28%

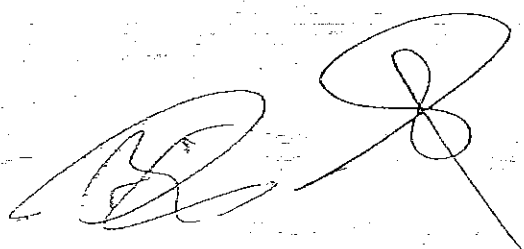
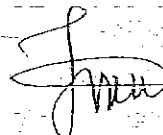
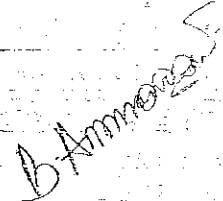
Source: Umeme Limited

From the above Table 3.3, it can clearly be seen that Umeme Ltd was not achieving the loss reduction targets. The actual distribution losses for Umeme have reduced from a peak of around 38% in 2005 to 28% by 2011. During the first seven years Umeme Limited was not able to reduce the actual losses, which were higher than the set losses targets. However, it was miraculous that the company was able to bring down the distribution losses to the target level of 28% in 2011 as set in the concessions agreements.

Umeme Limited attributes non-technical (or commercial) losses to illegal connections, meter bypasses and collusions between customers and its staff. The Company also attributes technical losses to insufficient investments in the network.

3.4.3 The Role of 'Prominent Persons' in Inflating Losses

The events leading to the Amendments of the Umeme Limited's concession agreements in 2006, witnessed among others, the convening of a meeting on the 23rd November, 2006 by a group of people calling themselves "prominent persons". This meeting was convened and chaired by Mr. Kabagambe Kaliisa, Permanent Secretary Ministry of Energy and Mineral Development and

attended by Mr. David Ssebabi, Director Privatisation Unit, MFPED, Eng. Elias Kiyemba, Managing Director UETCL, Mr. Sam Zimbe (Umeme), Mr. Buljan (Umeme) and one Mr. Paul Mare(Umeme). A copy of the minutes is attached as **Appendix III**.

This "prominent persons" in contravention of sections 15, 16, and 17 of the electricity act Cap 145 1999 overruled the then minister and arbitrarily increased the threshold of distribution losses from 33% to 38%, contrary to an earlier position taken by Hon. Daudi Migereko, the then substantive Minister of Energy and Mineral Development who had put the capping of distribution losses at 33% as the most acceptable benchmark level as per his letter dated 17th November 2006(**Appendix IV**). In a related communication to the Permanent Secretary /Secretary to the Treasury, the Chief Executive Officer ERA noted that in the worst case scenario, distribution losses could be capped at 35%, though the most acceptable level should have been 33% (**Appendix V**).

The Committee established that the above meeting which took a decision to increase the threshold of distribution losses from 33% to 38% was held when Hon. Kamanda Bataringaya was holding the portfolio of Minister of Energy and Mineral Development. He colluded with the three technocrats (namely, Kabagambe Kaliisa, Sebbabi and Eriasi Kiyemba) and the Umeme Officials to overturn the earlier decision of Hon. Migereko. The decision to increase the threshold of distribution losses from 33% to 38% was officially communicated to the Ministry of Finance by Hon. Bataringaya on 28th November 2006 and was written on Permanent Secretary's (Kabagambe Kaliisa) letter head bearing his reference and telephone number.

The Committee tasked Mr. David Sebbabi, Mr. Kabagambe Kaliisa and Eng. Kiyemba to produce the instrument that mandated them to hold this meeting and the Terms of Reference of the said meeting to no avail.

Consequently, power distribution losses were capped 38% in the amended Umeme concession agreements of 2006. Since then Umeme maintained high distribution losses between 35% -38% and Government has been absorbing the losses inherently through the agreed tariff methodology with the cost of each percentage loss estimated at U\$4 million per annum. This mechanism was bound to inherently give an incentive for the utility to overstate the losses.

Furthermore, the swiftness in which the earlier position of the sector Minister (Hon. D. Migereko), on losses was overturned while he was away, and the admission by Hon. Bataringaya that the Permanent Secretary Ministry of Energy drafted the letter overturning this position, is sufficient evidence to believe that such a decision was fraudulently taken.

3.4.4 Findings

- i. The distribution losses have remained relatively high and if they are not significantly reduced, the benefits of any additional power generation may not be realised. As already pointed out earlier on a one percentage power loss is equivalent to a loss of US\$4 million per annum.
- ii. Notwithstanding the slight decline in energy losses in 2011, several issues have remained outstanding, even after seven years into Umeme Limited's distribution concession. The split between technical and non-technical losses has not been determined by both the concessionaire (Umeme Limited) and the regulator (ERA).
- iii. There is no clear loss reduction strategy that has been developed and adopted by both ERA and Umeme Limited.

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- iv. The Company's metering inaccuracies and estimated meter readings have had a significant impact on the level of distribution losses and the ensuing tariff charge to the consumers.
- v. From the aforementioned, it is evident that there was a deliberate effort by Umeme Ltd to manipulate the said losses in order to obtain high compensation through the tariff and thus defraud Government and the people of Uganda.
- vi. The Committee further established that as a result of a number of reforms and programs prior to the unbundling of UEB, there were significant reductions in distribution losses from about 38% to 28% at the time Umeme Ltd took over the distribution concession from UEDCL in 2005. In fact, UEDCL and ERA indicated to the Committee that the losses were at 27% at the time of takeover compared to 38% losses claimed by Umeme Limited in the same year.
- vii. The team of 'prominent persons' increased the threshold of distribution losses for Umeme Limited from 33% to 38% while ignoring advice from ERA and the position that had earlier been decided by the substantive line Minister. The Committee found that this was not a policy matter but a regulatory one that should have been handled by ERA. This was a violation of Sections 15, 16 and 17 of the Electricity Act 1999 Cap 145 that empowers the Minister and ERA who objected to raising the loss threshold to 38%.
- viii. The UMEME has failed to curb power thefts and illegal power connections which are further compounded by high initial costs of connection and high end user tariffs.

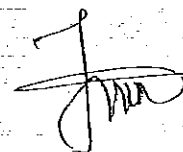
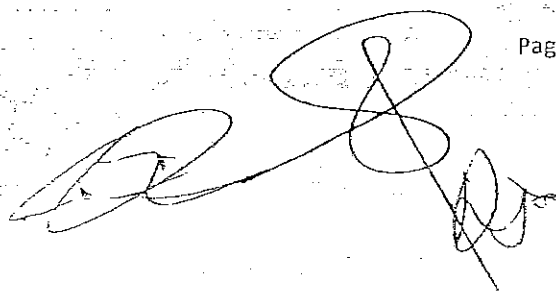
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3.4.5 Observations

- i. After failing to attain the set loss targets in the first six years of operation, it was noted that the Umeme miraculously brought down the distribution losses to the target level of 28% in 2011 as set in the concessions agreements. This abrupt attainment of the set target was due to the impending review of tariff parameters and the Company's performance in the last seven years by ERA in 2012.
- ii. ERA has not developed institutional and technical capacity to determine and monitor power losses in the sector. ERA relies on data submitted by Umeme Limited for distribution losses and yet the Regulator should be taking lead in establishing the distribution losses reported by the Company. It is therefore, irregular for ERA to rely on data on losses from Umeme Limited to evaluate performance of the Company.
- iii. Umeme Limited has no commitment to lowering distribution losses significantly because it gets compensated by having the distribution losses allowance incorporated in the tariff computation.
- iv. Umeme Limited has been reluctant to roll-out the prepaid metering system throughout the country that would reduce the non-technical losses significantly. The Company has been carrying out a pilot project in Kitintale District (Kampala) since last year, yet other electricity distributors operating in rural areas adopted the use of pre-paid metering system without having pilot projects.

3.4.6 Conclusion

From the aforementioned it can be concluded that high distribution losses have an impact on the end-user tariffs as they are included in tariff computation. Unless drastic measures are made by the electricity distributor



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(UMEME) to reduce power losses, they will keep end-user tariffs high as the Company gets compensated through the tariff.

The Committee recommends that:

- i. *Mr. Kabagambe Kaliisa (PS-MEMD), Mr. David Ssebabi (Director, PU) and Eng. Elias Kiyemba (MD, UETCL), should be held jointly and/or severally responsible for abuse of office and exacerbating the loss factor when they irregularly raised the loss factor capping from 33% to 38%.*
- ii. *The Committee further recommends that Hon. Dr. Kamanda Cos Bataringaya, former Minister of State for Energy and currently holding the portfolio of Minister of State for Education, be held personally and politically responsible for negligence when he sanctioned the raising of the loss factor capping from 33% to 38%, contrary to an earlier position by the substantive Minister.*
- iii. *ERA should develop a loss reduction strategy to cap energy losses between 14% and 16%, which would significantly lower end user tariffs as the case in Kenya.*
- iv. *All the distribution concessionaires should adopt the best available technologies and practices such as prepaid meters to curb the challenges related to thefts, billing, collection and customer care.*
- v. *The MEMD should introduce an amendment to the Electricity Act, making power thefts and vandalism least attractive venture and seriously punitive.*

3.5 Subsidies

A subsidy is the price paid by either the provider or third party (government) to help bring down the price of a product or service such as electricity. In

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Ugandan context the subsidies on electricity have been paid mainly by the Government and the Development Partners.

From 2005, the Uganda Government had been subsidizing tariffs for power consumers. This arose from the effect of procuring 200 Megawatts of thermal power to bridge the power shortage from private thermal generating companies whose costs of generation were high. Therefore, the Government intervened through provision of subsidies with the view to making electricity affordable to the consumers.

The subsidy used to be paid to Uganda Electricity Transmission Company (UETCL) for it to purchase electricity from generation companies, and paid the stated price. UETCL then would sell electricity to the distributors like Umeme Limited, to distribute at a lower rate to mitigate high tariffs.

This intervention, for example, had managed to artificially keep the power tariff for domestic consumers at UGX385.6 per unit of energy. Without the subsidy, the true cost of electricity in Uganda for domestic consumers by then would have been UGX845.8 per unit of energy, implying that the Government was paying the balance of UGX460.2 per unit of energy. The Government was therefore subsidising the cost of electricity consumed by the domestic users by 55% per unit of energy.

The policy on subsidies had been implemented from the year 2005 until January 2012 when the Government eventually deemed the subsidies unsustainable. The adoption of subsidies was contrary to the objectives set out in the Uganda Power sector restructuring and privatization strategy, 1999, which among others, was to make the power sector financially viable and able to perform without subsidies from the government budget.

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Over the years subsidies paid by government have been increasing to unsustainable levels as shown in Table 3.5 below. From 2005 to January 2012, the Government of Uganda had spent UGX1,992,840,000,000 only (say, Shillings one trillion, nine hundred ninety two billion, eight hundred forty million) equivalent to US\$800,000,000 (United States Dollars eight hundred million) on subsidies for electricity consumers.

Table 3.4: Subsidies paid by Government from 2005 to 2012

Year	2005	2006	2007	2008	2009	2010	2011	2012
Subsidy	53.66	130.80	247.47	242.90	258.93	310.89	633.99	114.20
Amounts in UGX Billions								

Source: UETCL

From the above Table 3.4, it is can be clearly seen that Government subsidies grew from UGX 53.66 billion in 2005 to UGX 633.99 billion in 2011. Over the eight (8) year period the total amount Government spent on subsidies paid to thermal generation companies stood at UGX 1.99 trillion which is a fifth of the national budget for the FY 2011/2012. Table 3.5 below shows the subsidy amounts paid to thermal generation companies.

Table 3.5: Government Subsidies Paid to Each Thermal Generation Company

	Aggreko	Aggreko	Jacobsen	Electromax	Total
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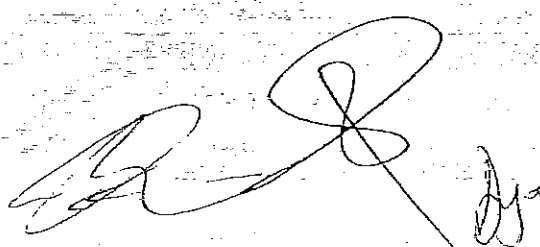
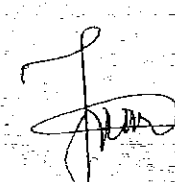
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Year	Lugogo/Kiira (UGX)	Mutundwe (UGX)	(UGX)	x (UGX)	(UGX)
2005	63,875,643,471	0	0	0	63,875,643,471
2006	130,922,714,454	0	0	0	130,922,714,454
2007	244,356,409,320	0	0	0	244,356,409,320
2008	227,508,875,088	0	23,265,888,732	0	250,774,763,820
2009	89,464,872,408	0	175,689,798,382	0	265,154,670,790
2010	85,467,300,438	15,950,078,640	171,013,273,605	32,737,430,150	305,168,082,833
2011	136,059,249,508	196,765,802,625	234,046,056,823	50,911,782,348	617,782,891,304
2012	0	58,163,757,840	50,469,186,812	5,570,962,740	114,203,907,392
Total	977,655,064,687	270,879,639,105	654,484,204,354	89,220,175,238	1,992,239,083,384

Source: UETCL

After the scrapping subsidies by GOU electricity bills increased by 36% domestic, commercial, and medium industrial consumers while the bills for the large industrial consumers rose by 69%. The reasons given by GOU for scrapping subsidies were:

- i. The money that had been spent on subsidies could easily have constructed another big dam or even two smaller ones.

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ii. It was better for consumers to pay extra now and in the end have reliable power supply in future.

iii. The money freed up would be used to finance the expansion of the Uganda's generation capacity which has been shrinking and it would also be used to finance the implementation of other critical government programmes.

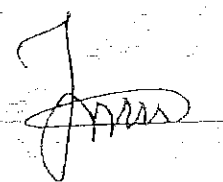
iv. The tariffs were not reflecting the current market price of generating electricity and were continuing to deny funding to other sectors of the economy.

The long term effects of scrapping subsidies on the economy are yet to be quantified and analysed. However, for the domestic and commercial consumers the effects have already been felt with payments of increased electricity bills.

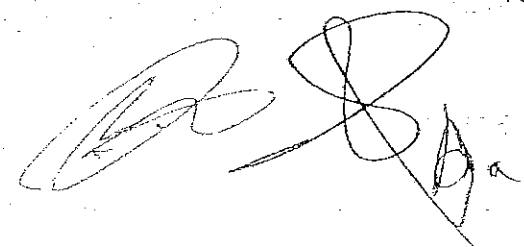
Rebates

In addition to the government subsidies on thermal power generation, UETCL offers rebates averaging Shs.8 billion to Shs.11 billion per month to Umeme Limited to prevent tariff increases by compensating all the stated power distributor's technical and commercial losses and any upward adjustments in the bulk supply tariff.

Just like the government subsidies on thermal power, the rebates offered by UETCL to Umeme Limited have been rising from UGX 25.43 billion in 2005 to UGX 431.33 billion in 2011. The total amount of rebate over the period 2005 to 2011 stood at UGX 878.74 billion as shown in Table 3.6 below.



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Table 3.6: Rebates Offered By UETCL to Umeme Limited from 2005 to 2011

Year	Gross Invoice Value UGX	Rebate UGX	Net Invoice Value UGX
2005	85,860,225,700	25,426,999,998	60,433,225,702
2006	184,802,939,633	92,895,000,001	91,907,939,167
2007	344,127,340,633	117,858,999,999	226,268,340,634
2008	319,195,299,209	78,477,000,003	240,718,299,206
2009	309,267,764,547	45,465,000,000	263,802,764,547
2010	376,807,503,744	87,289,002,000	289,518,501,744
2011	692,207,690,304	431,330,000,000	260,877,690,304
Total UGX	2,312,268,763,305	878,742,002,001	1,433,526,761,304

Source: UETCL

3.5.1 Findings

(i) The introduction of subsidies in the electricity sector in 2005 was contrary to government policy of using the private sector and efficient markets as a basis for the growth and development of the sector.

(ii) The expenditure of UGX 1.99 trillion paid by Government as subsidies on thermal power generated over the period 2005 to 2012 denied Ugandans resources for socio-economic growth, yet only 12 percent of the population had access to electricity.

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3.5.2 Observation

The technocrats charged with management of the power sector did not have the foresight to know that subsidies in the long run would not be tenable. The subsidies should not have been introduced in the first place since one of the objectives of the reforms was to allow market forces determine prices.

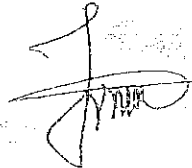
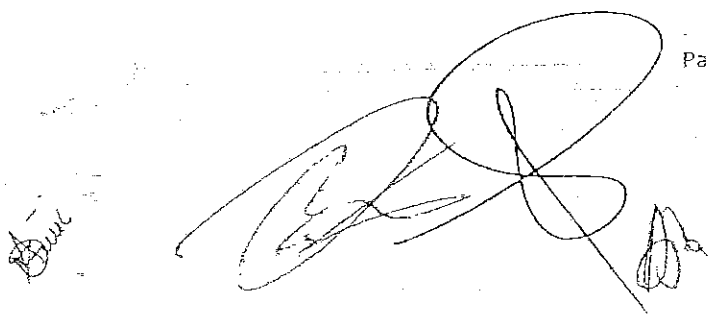
3.5.3 Conclusion

The subsidies paid by Government from 2005 to 2012 in the energy sector to the tune of UGX 1.99 trillion, benefitted only 12% of the country that is connected to the electricity supply network. The decision to subsidise the sector was caused by the poor planning and lack of foresight by the technocrats charged with the management of the energy sector. The subsidies should not have been entertained as market forces were supposed to determine the prices of electricity paid by consumers. The money spent on subsidies over those years deprived Government of valuable resources that would have been invested in other infrastructure development projects in the country.

The Committee recommends that Government should fast-track the construction of Karuma power plant and other small hydra power projects to ensure that the demand for power does not outstrip the supply as has been the case that warranted the acquisition of power from thermal generation companies.

3.6 POWER GENERATION

Uganda has diverse renewable energy potential. The country's known renewable energy resources are hydro, biomass, solar and wind. Discounting wood fuel biomass, Uganda's renewable energy resources are largely untapped except for the large hydropower plants at Kira-Nalubale, Bujagali and a few



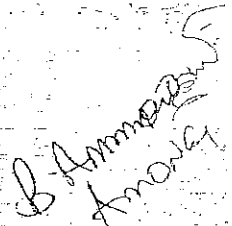
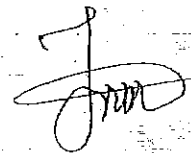
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mini-hydro plants. The most economic source of power supply for Uganda is hydro, although it is prone to seasonality factors, fraudulent manipulation of construction costs by Ministry of Energy and Ministry of Finance technocrats and the challenge of raising the initial investment capital for constructing the plants.

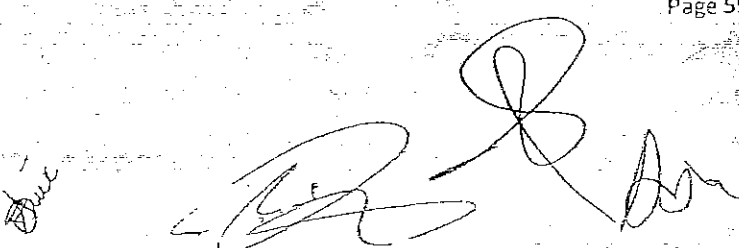
By May 2005, the installed electricity generation capacity in Uganda was 380 megawatts (MW) produced by the hydroelectric plants at Owen Falls, Nalubale, 180 MW and 200 MW at Kiira. The effective generation capacity of the complex was about 230MW. However, the capacity production by these plants dropped to about 140 MW in 2005 because of the supposedly prolonged drought that caused the water levels on Lake Victoria to drop. However, hydrological data showed that it was NOT the drought that significantly reduced the lake levels BUT the positioning of Kiira Dam parallel to the existing dam (Nalubale) which grossly caused the level of Lake Victoria to drop, resulting into reduced generation capacity of the two dams.

In spite of the decline in generation, demand for electricity continued to grow widening the gap between supply and demand. In 2006, peak demand reached 380MW resulting into persistent rolling blackouts at peak of 80-120MW. The shortfall in electricity supply was met through a combination of measures involving procurement of emergency diesel and heavy fuel generators, promotion of energy efficiency and renewable energy.

By July 2012, the total installed power generation capacity was 772MW, that is 630MW from the large hydro plants, 57MW from mini-hydro plants, 68MW from thermal plants and 17 MW from co-generation at the sugar industries. However, the total effective generation output from these sources was about 580MW in July 2012.



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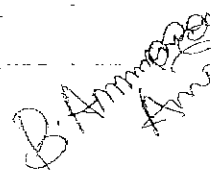
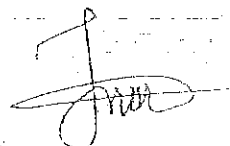
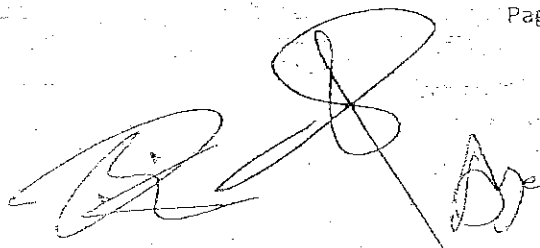
At the same time the power demand during peak hours (7pm - midnight), was at 443MW. Electricity demand increased sharply a month after the Bujagali Hydropower Project delivered 250MW to national grid. With the power demand growing at 10% per annum, it is estimated that every year the country will need to commission a 50MW project in order to avoid going back to the situation of load shedding.

The demand forecast was that the surplus energy would be consumed in the next 24 months before the undesired load-shedding returns. However, it is turning out that the excess electricity will be consumed faster than expected. Statistics from Uganda Electricity Transmission Company (UETCL) indicate that peak demand has grown by 9% to 487MW from the previous 443 MW in just over a month after July this year.

3.6.1 Existing Generation

- i. **Hydropower:** The existing hydropower plants in the country are the Kira-Nalubale power complex and Bujagali on the River Nile. These power plants are a cascade, and therefore their electricity outputs are directly related. Kira-Nalubale has a combined installed generation capacity of 380MW but their actual output has significantly dropped since 2006 averaging at 140 MW.

The sharp drop in generation capacity of Kira-Nalubale is reportedly attributed (MFPED and MEMD) to prolonged drought of 2005/06 that led to a significant drop in the Lake Victoria water levels. Even with the improved hydrology of this lake (restoration of water levels) and the purported heavy capital investment of Eskom (U) Limited into the same plant, the actual output of this plant has remained at its lowest (140MW).

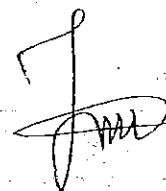


The Bujagali Hydro plant which was brought on board in July this year has the installed generation capacity of 250MW. The actual generation output is expected to be 250MW.

- i. **Mini-Hydro Plants:** There are a number of mini-hydro plants in the country which include Mpanga (Kamwenge) with installed generation capacity of 18MW, Hydromax-Buseruka 5MW, Bugoye 13MW and Ishasha mini-hydro with an installed generation capacity of 6.5MW. Other mini-hydro plants include Kilembe Mines Limited with installed generation capacity of 5MW and Kasese Cobalt Limited with an installed generation capacity of 9.5MW. The Nyagak mini-hydro plant was commissioned in early September this year with a generation capacity of 3.5MW.

- iii. **Thermal power:** The prolonged drought of 2005/06 reportedly reduced the water levels of Lake Victoria leading to a reduction in the hydro power generation capacity of the country which compelled Government to enter into agreements with private thermal power producers (M/s Aggreko, Jacobsen and Electromaxx) to supply power in order to reduce the power shortfall experienced from that time. These companies combined produced a total of 200MW.

Whereas thermal power generators were contracted to provide emergency power in Uganda (as a stop gap measure), their contracts/licenses had been regularly extended. These thermal power generation agreements did not clearly spell out the targets or objectives to be achieved, for whom the project was designed, the timeframe it was envisaged to take, among others.



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The continued extensions of these thermal power generation contracts while maintaining the same terms and conditions of the initial agreements had grave implications on the tariff. In effect, Government was stuck in thermal power generation agreements that had abnormally high tariff profile that were meant to be for a short time span but in actual sense lasted longer than envisioned.

A lack of integrated resources planning had given rise to the implementation of these thermal power projects in emergency situations, which unfortunately had accentuated the problems in the power sector. These emergency power solutions had become base load power plants at abnormally big cost to the country. Considering that about 30% of the expensive thermal power was lost in the transmission and distribution process, a clearly untenable situation unfolded in the country.

The retail tariffs paid by the power end users were not sufficient to pay for the power procured from thermal generation plants. Therefore, Government came in and paid the difference between retail tariff and the actual cost of supplying power.

iv. **Solar Energy:** Solar energy is a source of electricity in Uganda although it is not well tapped and developed to reasonable levels. Solar energy when well tapped would provide the remote and off grid rural locations in the country with power. A few homesteads and public institutions in remote areas have installed solar power systems.

v. **Standby and Embedded Generation:** There have been significant amounts of standby generation capacity owned by some industries and commercial establishments that were intended for operations during extended periods of blackouts. There was, however, no information

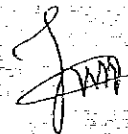
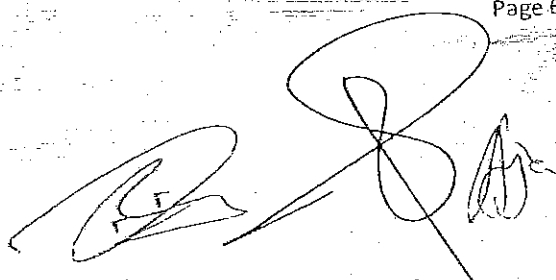
available on the total installed capacity of these standby generators countrywide.

- vi. **Wood Fuels:** Wood fuels account for more than 80% of total energy used in Uganda. It is the traditional energy source of Uganda. The bulk of the country's energy supply comes from wood. Wood fuel is renewable and sustainable if supply could increase to meet demand. Wood fuels provide the bulk of the energy needs for most informal enterprises such as bread baking, tobacco curing, brewing of local drinks, fish smoking.
- vii. **Co-Generation:** In addition to generation from mini-hydros, sugar companies have demonstrated potential to step up generation from bagasse and sell surplus power to the grid. It is now expected that by 2013, sugar companies will be selling up to 50 MW to the grid.

Kakira Sugar Works produces 12MW of electricity through co-generation. Co-generation is a process through which power is produced using bagasse (sugarcane waste). The Company started producing power from the sugarcane waste in 2005 and has established that it is so far the cheapest power source. According to REA, Kakira was one of the companies which received funds under the electrification for rural transformation to produce electricity through co-generation and the Company obtained a US\$3.3million grant in 2008. Kinyara Sugar Works likewise produces 5MW of electricity through co-generation for in house use.

Generation Mix

Until 2006, hydropower was major source of electricity in the country which contributed 100% of power into the national grid. Owing to the supply deficit arising from the 2005/06 drought and the resultant compulsion of



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Government to enter into agreement with private thermal power producers to supply power to reduce the shortfall, there was a shift in the generation mix, with Emergency diesel thermal power and Heavy fuel oil (HFO) thermal power contributing 56% of power into the national grid while 44% has been coming from hydro generation. Of course, this shift towards thermal generation introduced higher generation costs into the generation mix.

With the closure of Emergency Aggreko thermal generation plants at Lugogo, Kira and at Mutundwe in April 2012, there was a remarkable tilt in the generation mix. By April 2012, the generation mix had changed to 74% of power produced from large hydro power plants, 14% from thermal generation plants, 5% from mini-hydro generation plants and 3% from co-generation. The situation has been boosted by the commissioning of Bujagali Hydro power plant in July 2012 delivering 250MW.

3.6.2 Construction Power Generation Projects

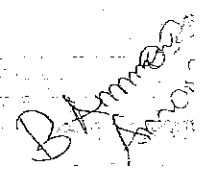
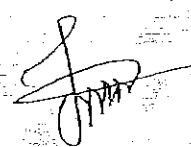
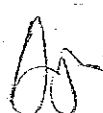
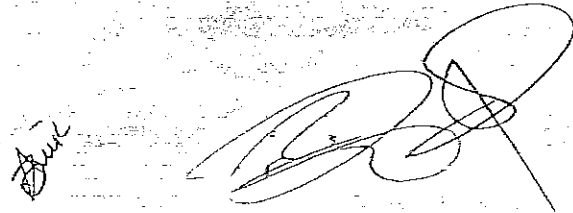
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Bujagali Hydro Power Plant

As part of the wider efforts to increase power generation, the Bujagali Hydropower Plant contract was awarded in 2005. The initial contract cost was US\$460million. However, the cost of this project had risen to US\$893 million by 2011 making Bujagali a very expensive Hydro Power plant considering the expected generation capacity of only 250MW. The Committee could not obtain the actual construction cost for the Bujagali plant even after requests had been made to the relevant Ministry and Agencies.

The tariff profile for the Bujagali Power plant will not be constant, but will be averaging between US\$0.12 (12US cents) per Kilowatt hour (kWh) over the 30years before this plant reverts to Government ownership and peaking at 16US cents/kWh in 2022. In the first 13 years the tariff for Bujagali will be in the range of US12-16cents/kWh which is almost the same for Heavy Fuel Oil (HFO) and the thermal power generators which sell between 24- 34 US cents depending on the exchange rate and fuel prices. It is important to note that if the Bujagali generation tariff was to be within the internationally acceptable range, then it would be US\$0.05 to US\$0.07 (or 5 US cents to 7 US cents) per kWh.

Taking into account that US\$893million had been spent on the Bujagali power plant by 2011, it is considered a very expensive project when compared with other power plants constructed within the same period in other countries. For example, Sudan built a 1,500MW hydro power plant at US\$1.95 billion which translates to US\$1.3 million per MW. The Grand Ethiopia Renaissance Dam hydro power project with an expected generation capacity of 6,000MW upon completion in 2014 is being constructed at a cost of US\$4.8 billion, that is, US\$0.8 million per MW. Taking into considerations the above parameters, the construction of the Three Gorges Dam in China, the biggest hydro power plant



in the world with installed generation capacity of 22,000MW, cost the Chinese Government US\$25 billion, that is, US\$1.2 million per MW.

From the above examples, it can be seen that there is a very big variance in construction costs in the countries mentioned when compared to the construction cost of the Bujagali Plant that cost US\$3.44 million per megawatt before addition of interest during construction. The industry benchmark construction cost of hydropower projects is US\$1.5 million per Megawatt as it is the case in other countries the world over. It is therefore in the interest of Ugandans that further details regarding the procurement of Bujagali Hydro power plant and how its generation tariffs were determined be availed in a bid to mitigate the likely consequence to the growing public apprehension that electricity tariffs will hit abnormal levels despite the completion of this plant.

The committee also noted that the cost escalations from the bidden price by the eventual winner of the Bujagali power plant M/s Salini was done outside the ambit of the Electricity Act. The electricity act Cap 145 1999 section clearly explains that matters to do with tariffs are the responsibility of ERA unless otherwise delegated by ERA. The approval process for cost overruns in Bujagali was fraudulent and designed to cheat by increasing the costs illegally avoiding the oversight of the Auditor General and ERA.

The process increasing and approving the cost of constructing Bujaggali Hydropower Plant from the initial US\$460million to a high US\$893million was highly suspicious. This astronomical increase in the plant cost was done between the Ministry of Energy, Ministry of Finance, UETCL and UEGCL the project supervisor on behalf of the project contractor M/s Salini. ERA whose mandate includes tariff management was never involved. Therefore the

astronomic cost of Bujaggali adversely impacts of the tariff paid by electricity consumer was reviewed without the expert input of the sector regulator (ERA).

ii. Karuma Hydro Power Plant

The procurement process for Karuma is ongoing. However, the Committee established that it has been marred by irregularities in the procurement process. Due diligence on the prequalified firms was done by police and other Government agencies on the instructions of the Executive arm of Government after the technical evaluation of bids at Chobe Hotel, Murchison falls National Park.

There were also some complaints raised with the Public Procurement and Disposal of Assets (PPDA), which were reportedly resolved.

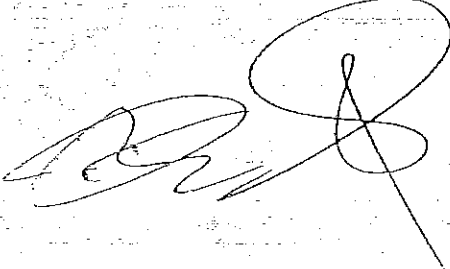
iii. Integrated Gas Power at Kabaale-Hoima

As part of the early production scheme, Government is in the final stages of developing a power plant at Kabaale in Hoima. This plant is expected to generate 50MW using crude oil from extended Well Testing.

3.7 Findings

- i. There are still many untapped sources of energy to be exploited in order to increase electricity supply.
- ii. The construction cost was Bujaggali Hydropower Plant suspiciously increased from US\$460million in 2005 to US\$893million by 2011 without the expert input of the sector regulator ERA, which was in contravention of sections 15, 16 and 17 of the Electricity Act.
- iii. The Bujaggali plant generation tariffs of US\$0.12 to US\$0.16 per kWh are high when compared with the internationally acceptable generation

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tariffs for similar hydro power plants which range from US\$0.05 to US\$0.07.

3.8 Observations

- i) Even when one considers the fact that the cost of constructing a hydropower plant depends on its location, size, investment risks, accessibility to raw materials and the economic conditions of the country, it is still inconceivable that Bujagali Hydropower Plant with its expected generation capacity of 250MW can cost over US\$893million!
- ii) The Committee takes cognizance of the fact that hydropower is cheaper than thermal power although the initial investment cost of hydro power generation is much higher than the investment for thermal power generation. The running costs of hydropower generation are cheaper than those for thermal power generation.
- iii) Uganda energy consumers have reason to worry because a high tariff outstrips their domestic earnings (if the utility bills exceed 10% of their domestic income), depriving them of a decent life, since they will be left with no income to cater for other basic needs. Suffice to say, distorted costs also distort life. It is therefore in the interest of Ugandans that further details regarding the procurement of Bujagali Hydro power plant and how its tariff was determined be availed in a bid to mitigate the likely consequences to the growing public apprehension that electricity tariffs will hit abnormal level despite the completion of this plant.

3.9 Conclusion

There is still a lot of potential for hydropower generation power in Uganda if the untapped sources of energy are exploited. It is therefore incumbent on Government to explore financing options to tap into this resource.

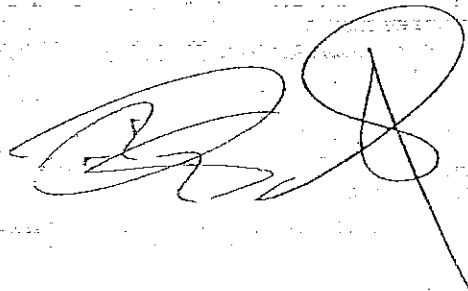
The Committee recommends that:

- i) The Auditor General institutes a technical and financial audit of Bujagali Hydropower plant and report back to Parliament within six months after the adoption of this report.
- ii) The Inspectorate of Government should take interest in the manner in which the power plant at Kabaale in Hoima was /is being procured.
- iii) The IGG, the OAG and the Parliamentary Committee on Natural Resources take keen interest in the procurement process for the construction of the Karuma power plant to guarantee value for money.

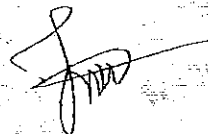
4.1 REGULATION OF THE ELECTRICITY SUB-SECTOR

4.1.1 ERA Structure, policies and procedures

- i) Whereas the functions, powers and independence of the regulator are defined in the Electricity Act of 1999, the committee found out that there was apparent misinterpretation of the Authority's independence visa-a-vis the powers of the Minister, either deliberately or otherwise. In some instances the differences in interpretation of the provisions of the Act resulted in the executive arm of the government usurping the functions of regulator with respect to tariffs setting, energy losses and human resources management. The case in point being the dismissal of the former CEO Eng. Ssebowa and the Authority Secretary Mr. Johnson Kwesigabo.
- ii) MEMD established REA to facilitate the GOU goal of achieving a rural electrification rate of at least 10% by the year 2012 from 1% at the beginning of the decade. REA carries out planning activities for rural

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electrification, which function should be part of sector wide integrated resources planning.

iii) The composition of the board of ERA is not in accordance with the electricity Act with respect to qualification, expertise and conflict of interest. These are key aspects of good corporate governance.

iv) **ERA Staffing Gaps.** Examination of the Authority's structure and the staffing levels revealed that most departments have staffing gaps in critical areas. Until September 2012, the Director Economic regulation was also the Acting CEO of ERA both of which posts are very demanding. The review of the organizational structure also revealed that, the Manager Legal Services is also acting as the General Counsel to the Authority. Out of the 11 vacant posts, 7 are managerial posts. This situation impacts negatively on the capacity of ERA to effectively execute its mandate of sector supervision and monitoring.

It is also the Committee's considered view that the current organizational structure of ERA is devoid of other equally key positions. The Authority needs a more robust structure to effectively execute its mandate.

v) **Lack of a Risk Management Manual.** Given the susceptibility of the electricity sector sub-sector to risks, the regulator (ERA) has not been able to develop a risk management manual neither does it periodically review its major risks. Potential risks are not identified, measured, mitigated, tested, monitored nor reported. Therefore, failure by ERA to periodically identify and update its risks exposes management to crisis situations.

vi) **Irregular appointment of ERA Board:** The appointment of the current board of ERA was marred by irregularities. Apparently, it is evident while appointing the current ERA board in his capacity as

former Minister of Energy and Mineral Development Hon. Hillary Onek, exhibited conflict of interest. It is highly probable appointed the Board without carrying out due consultations with the relevant government agencies in the energy sector.

The Committee found out that Hon. Hillary Onek is the Chairman Pakwach Power (an electricity company) while Mr. Apiire Santo the current ERA Board Chairman is a finance director in the same company.

4.1.2 Sector oversight roles vis-à-vis MEMD

- i) ERA is less involved in power sector planning, which leads to large private sector investment projects such as Bujaggali, Karuma, yet it is expected to issue licences for the operation of these power plants. These large projects, when completed, have a huge impact on power transmission and distribution networks, which are not being planned centrally.
- ii) The board of ERA has over the period of the reforms, lost its power to other government departments and units such as the MEMD, MOFPED and privatization unit. ERA has thus suffered mandate drift.

4.1.3 Licensing procedures

- i) In the interest of the transparent and predictable regulation, it is important that the process for issuing, amending and revoking licences are clearly spelt out, and are as open as possible. ERA has not properly coordinated this process due to mandate drifts.
- ii) Revocation of licences has never been done, as ERA is not well resourced to effectively monitor compliance. Amendments made to date

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on some licences are as a result of external situations and not internally flagged by ERA.

- iii) There are clear instances of non-compliance with grid code provisions, poor quality of supply, and high levels of actual losses in comparison with peers in East Africa. The high level of subsidies in the sector raises questions of financial viability.

4.1.4 Monitoring and supervision

- i) ERA does not have adequate human resource capacity to carry out efficient sector monitoring and supervision in the areas of environmental compliance, inspection, and investigations.
- ii) Even if the licencees provide ERA with performance information, it does not analyse the information for decision making in the public interest. For instance, the grid code sets performance targets with respect to quality of supply, which targets are being violated without any corrective action on part of ERA. These performance targets have an impact on the tariff.
- iii) The Uganda electricity supply industry is based on a monopoly in generation; that is "single buyer" market model where many generators sell their power to UETCL. At the distribution and supply end there is a private monopoly.

General findings

- i) Electricity meters are key to sector economic efficiency. Currently each licensee is required to provide, test, calibrate and certify its meters without any third party involvement. The absence of the third party to certify electricity metres UMEME Ltd has installed a sophisticated test bench that it uses to test, calibrate and certify meters.

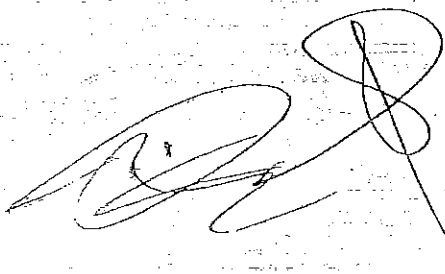
ii) Protecting the environment has become topical in light of green house gas emission reduction and climate change mitigation. According to the National Environment Act (NEA), an environment clearance by the National Environmental Management Authority (NEMA) in the form of an Environmental impact Assessment (EIP) must be given for any generation, transmission and distribution of electricity in Uganda to occur. There after environmental audits is condition precedent to the issue of a license by ERA. There is lack of specific clauses in the licences issued by ERA with respect to regular environmental audit reporting and with how non- compliance can be dealt.

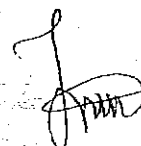
iii) ERA currently has only one environmental officer who is responsible for environmental compliance for the entire electricity sector. The review shows that there is not enough manpower capacity to effectively monitor environmental compliance.

The Committee recommends that ERA should expeditiously develop a Risk Management Manual so as to mitigate the effects of potential risks to the sub-sector.

5.1 INVESTMENTS IN THE ELECTRICITY SUB-SECTOR

The main purpose of the reforms that led to the privatization of the electricity sector was to develop an environment which would attract capital and entrepreneurs, and to realize competition benefits. The privatization process culminated into the establishment of the generation and distribution concessions with the private companies. This sub-section of the Chapter assesses the level of investment by Umeme Limited and Government investment in the sector.

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At the beginning of the Power Distribution Concession in March 2005, investments by Umeme Limited in the network were supposed to be guided by the Restoration and Reinforcement Plan as stipulated in the Support Agreement signed by Government and the Concessionaire. The five year Restoration and Reinforcement Plan that was to commence in 2005 and end in 2010; was supposed to be approved by the Electricity Regulatory Authority. This Restoration and Reinforcement Plan was meant to be a tool to guide both Government of Uganda and the Concessionaire by clearly defining and stipulating the critical areas of investment in the distribution network, the expected outputs, the required resources and performance standards among others.

As a regulatory requirement, before the beginning of each tariff year, Umeme Limited is required to submit an Investment Plan, which obviously feeds into the Restoration and Reinforcement Plan for ERA's approval. The Investment Plan is submitted together with an Annual Application for the tariff review. The Investment Plan must be detailed enough showing areas of the network where these investments are to be deployed and giving the justification that is borne out of the network / system analysis / status report.

The annual tariff application must also show the expected benefits in terms of energy loss reduction, improvements in quality of supply and service delivery, billing efficiency among others. The submission must also be accompanied by detailed schedules that would enable ERA to monitor the implementation of the approved investment. ERA then approves Umeme's investment Plan after it has been fully satisfied that the investments will go into strategic areas of the network where they are needed most to deliver the expected benefits in terms of loss reduction, improved quality of supply and service delivery.

By the close of the tariff year, specifically by 1st February of the subsequent year Umeme is required to submit to ERA and UEDCL the list of assets transferred to the Asset Register, the financial statements for that year and "As Built" diagrams for the assets. The investment verification is jointly conducted by ERA and UEDCL, the assets owner.

5.1.1 Umeme's Investments Submitted to UEDCL for Verification and Approval

From Table 3.7 below, the total verified Umeme Limited's investments by December 2010 amounted to UGX 165.3 billion and those pending verification by December 2010 were valued at UGX 33.1 billion. The total investment value submitted for verification and approval was UGX 198.5 billion at December 2010.

Table 3.7: Umeme Limited Investments

Period	Verified/ Confirmed as at October 2011 (UGX)	Pending Verification at 24 October 2011 (UGX)	Total Investments - (UGX)
March -Dec 2005	9,214,922,313	439,580,686	9,654,502,999
Jan- Dec 2006	5,480,393,471	2,019,863,124	7,500,256,595
Jan- Dec	25,810,602,358	565,921,763	26,376,524,121

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Jan- Dec 2008	42,235,579,806	200,759,601	42,436,339,407
Jan- Dec 2009	51,489,093,658	6,666,558,257	58,155,651,915
Jan- Dec 2010	31,120,630,973	23,246,380,204	54,367,011,177
Sum Total	165,351,222,579	33,139,063,635	198,490,286,214

Source: UEDCL

Operation and maintenance costs under the Umeme Power distribution Concession are directly recovered from the tariff while investment costs are provided with a clear return on investment of 20% per annum. Unfortunately, when officials from both the Regulator (ERA) and the power distribution asset owner (UEDCL) appeared before the Committee, they all admitted the absence of a clear mechanism of verifying Umeme's investments and distinguishing investment costs from the concessionaire's operation and maintenance costs.

It is quite astonishing to note that with purported level of investment made by the Concessionaire in the network, Umeme Limited is still incurring operation and maintenance costs amounting to an average **US\$36million** per annum. The committee considers Umeme Limited's purported investments amounting to US\$130 million in the last 7 years as highly exaggerated and therefore unacceptable since the alleged investment should have led to improved power

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system efficiencies, which in turn translates into less operation and maintenance costs.

5.1.2 Umeme's Level of Investment

Information available from Umeme Limited indicates that from 2005 to 2011, the shareholders of Umeme Limited have contributed to a total of US\$13,333,332 only in form of share capital and equity (See Table 3.8 below for breakdown). Umeme Limited has also obtained loans from Globeq Holdings and International Finance Corporation totaling to US\$51,666,668 as shown in Table 3.9 below.

It is imperative to note that M/S Globeq Holdings continues to own 100% shares of Umeme Limited since 2006. This implies that since 2006 to 2008 M/S Globeq Holdings has lent itself (Umeme Limited) US\$26,666,667 at an interest rate of 12% per annum. In view of the above, the total sum of money invested by the company by 2010 i.e. Shareholders' funds and loans totals to US\$65,000,000.

Table 3.8 UMEME LIMITED'S EQUITY AND SHARE CAPITAL FUNDS

DESCRIPTION	PERIOD	DATE	PRINCIPAL AMOUNT US\$
Share Capital			
Share Capital	2004/2005	28th May 2004	22,000
Share Capital	2004/2005	28th May 2004	28,000
			50,000
Equity in April 2004			
Equity Portion	2004/2005	1st April 2005	733,333

Globleq Limited	2004/2005	1st April 2005	933,333
	2007	15th February 2007	5,000,000
	2008	15th May 2008	3,333,333
	2008	15th October 2008	3,333,333
			13,333,332
			13,333,332
Total Equity and Share Capital			

SOURCE: UMEME LIMITED

Table 3.9 LOANS OBTAINED BY UMEME LIMITED FOR INVESTMENT IN THE POWER NETWORK

	LENDER	DATE OF BORROWING	CURRENT OUTSTANDING LOANS (US\$ EQUIVALENT)	LENDING RATE
1	Globleq Holdings	15th February 2007	10,000,000	12%
2	Globleq Holdings	15th May 2008	3,333,334	12%
3	Globleq Holdings	15th May 2008	6,666,667	12%
4	Globleq Holdings	15th October 2008	6,666,667	12%
5	International Finance Corporation	30th December 2009	5,000,000	8.5%
6	International Finance Corporation	07th May 2010	10,000,000	8.5%

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7	International Finance Corporation	10th February 2011	10,000,000	8.5%
		TOTAL	US\$51,666,668	

SOURCE: UMEME Ltd

According to Umeme Limited, the company had invested US\$130 million by 2011. It is important to note that at the time Umeme Limited took over the Distribution Concession in 2005, it is reported that the power distribution network and infrastructure was in a sorry state, dilapidated, and the energy/system losses stood at 33-35%. It is therefore logical to say that with Umeme Limited claiming to have invested about US\$130 million in the distribution network, the country should have witnessed correspondingly, a big improvement in the efficiencies characterized by a significant drop in losses, decreased tariff, limited power outages and load shedding among others. Unfortunately, the reverse is true.

Conversely, such a hefty operation and maintenance budget lends credence to the Committee's earlier assertion and belief that Umeme Limited's purported level of investment is a fraudulently concocted amount meant to benefit both Umeme Limited and their accomplices.

5.1.2 Government Investments in the Power Network

Whereas the main purpose of Government signing the Umeme Limited distribution concession was to attract private sector investment, the GOU continued to inject resources into the network through acquired loans and grants from development partners. Government of Uganda provided an investment package of **US\$11million (Power IV Loan)** which constituted part of the investment in the distribution network. These were:

- i. Investments in electricity poles and transformers to tune of **US\$6 million.**

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- ii. To help in reducing the retail tariff, a commitment of US\$5million was used to finance modifications on the power distribution network. It is on record that Umeme Limited was not meant to refund this sum of money.

In addition to the above, GOU also secured an ADB loan amounting to UGX36 billion, which was meant to be invested in the power network infrastructure (Urban Power Rehabilitation project). The project was aimed at significantly reducing the technical losses specifically in the distribution network in Kampala, Jinja and Tororo. Other investments in the power network have been capital contributions from new customers requiring connections to the electricity supply network and also from fully funded schemes.

5.1.3 UMEME's claim for depreciation from UEDCL Assets

The Committee shockingly found out that since 2005, UMEME Ltd has continued to claim depreciation from the same Government assets, yet according to the Lease and Assignment Agreement between UEDCL and UMEME Ltd, these assets (Distribution system) remained under the legal ownership of Government of Uganda (UEDCL) and there is no option of transferring them to UMEME even at the end of the lease period.

According to the nature of this agreement, it is essentially an operating lease and not a financial lease. An operating lease allows the leaser (UEDCL) to claim the capital deductions and the lessee (Umeme) to expense the lease rentals. Therefore the treatment that UMEME should have applied was to expense the entire lease rental as the only available deduction arising from the use of these assets. However UMEME instead has continued to claim capital deductions on these assets. This treatment that Umeme employed is for finance leases but not operating lease. In doing this UMEME has been able to conveniently understate its tax liability and neither UEDCL nor URA had detected this anomaly for all these years.

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5.1.4 Findings

- i. It is regrettable to note that seven years into the power distribution concession, no Restoration and Reinforcement Plan (RRP) has been developed by Umeme Ltd. In the absence of an RRP, and the total failure by ERA to put in place investment guidelines clearly specifying the strategic areas to invest in; and the absence of a water tight mechanism for verifying these investments, Umeme Limited has continued to dictate when and where to invest including largely, none core items such as office furniture and fittings, motor vehicles, building official residences and rehabilitation of former UEB offices from which they recoup a 20% return per annum.
- ii. The Committee found out that there are no Investment Regulations and Verification Guidelines that Government can use to determine the level of investment made by Umeme Limited in the distribution network and ascertain whether or not the objectives of unbundling UEB and the subsequent leasing of the power distribution are being realized.

5.1.5 Observations

- i. In the absence of a Restoration and Reinforcement Plan to guide investments, the Committee finds it extremely difficult to believe the level of investment claimed by Umeme Limited. An investment in the distribution network to the tune of US\$130million that Umeme Limited wants Ugandans to believe, would have substantially turned around the efficiency of the distribution network. Umeme Limited would have installed prepaid meters, improved accuracy in billing and therefore recorded a significant reduction in energy losses to acceptable benchmark levels.

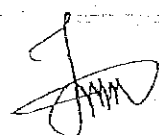
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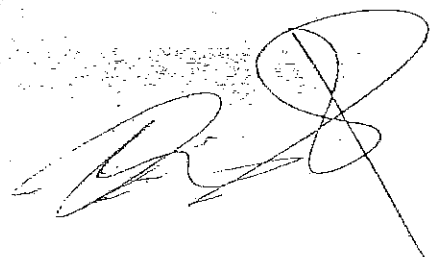
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- ii. The Committee considers the claim by Umeme to have invested US\$130 million as a means of upping their stake of the "Buy Out Amount" (which is based on amount invested and not recovered by the Company), in the event of early or natural termination of the Power Distribution Concession by Government.
- iii. Whereas Umeme Limited and some top bureaucrats in the Finance and Energy Ministries have continued to claim that the Company has recorded such levels of investment in the power distribution network, the committee finds such a claim misleading because such huge amounts of money, if invested, would have translated into new efficient technologies, a better and improved network with a service that is satisfactory to power consumers in the country. All this, unfortunately, makes the Ugandan power consumers feel quite nostalgic for UEB.
- iv. A decade since the unbundling of UEB, Government has made little effort to build and enhance the capacity of both the Regulator (ERA) and the asset owner (UEDCL) to be able to independently verify investments in the distribution network, determine the level of losses and make a split between technical and commercial losses.
- v. The submission of the Asset Register by Umeme in February 2012 for the whole of the previous calendar year comes as a huge backlog whose verification always takes long. It would be better if these submissions were made within a shorter period instead of once in a year.
- vi. For over seven years since Umeme secured the Power Distribution Concession in Uganda, the Concessionaire has successfully continued to file its Annual Investment Plan which prominently includes none core



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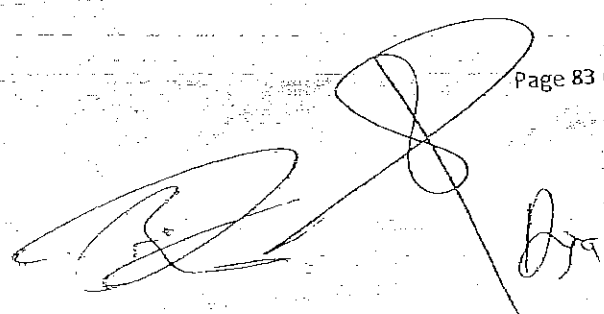
items like office furniture and fittings, building residences for its management staff and renovation of former UEB buildings as part of its critical investment areas. Shockingly, these none core items have always been approved by both the Regulator (ERA).

vii. It is painful to note that at the end of the day, Umeme Limited recoups an annual return on investment of 20% on these kinds of investments and will continue doing so until the end of the 20 years of the Concession period. No reasonable person would approve, among others, office furniture and fittings as core investment items in a power distribution system!

The Committee recommends that:

- i. The Auditor General carries out an audit to verify the amounts Umeme Limited claims to have invested since 2005.
- ii. The Office of the Auditor General should carry out an audit into the US\$11million (Power IV Loan) and the UGx 36billion loan given to UEDCL and also ascertain the amounts in the tariff earning return on investments from Umeme Limited that were covered by these loans.
- iii. The Committee recommends that Government urgently puts in place an Energy Coordination Committee headed by the Minister of Energy and Mineral Development to effectively monitor the power generation, transmission, and distribution segments, review progress and report to Parliament on a quarterly basis. This committee should comprise representatives of key Agencies in the Power sector (UEGCL, UETCL and UEDCL), ERA and a representative from each of the Concessionaires.
- iv. The Office of the Auditor General should carry out an audit to verify the amounts of Income tax defrauded by Umeme Limited.

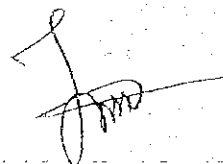
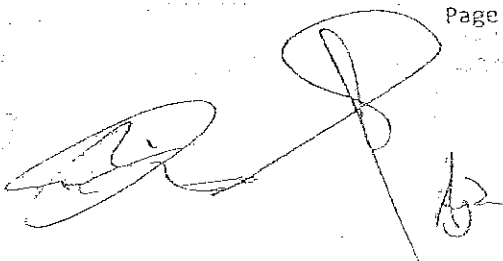
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- (iv) The Committee recommends that Uganda Revenue Authority takes up the matter of Umeme's Claim of Depreciation from UEDCL Assets and raise the appropriate assessment to recover the tax due from UMEME with in two months after the adoption of this report.

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CHAPTER FOUR

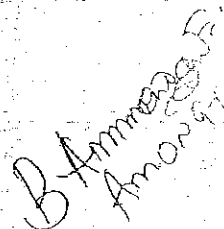
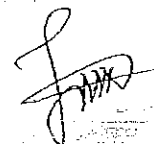
SCRUTINY OF AGREEMENTS SIGNED BETWEEN GOVERNMENT OF UGANDA AND ELECTRICITY UTILITY SERVICE PROVIDERS

4.1 Introduction

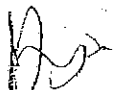
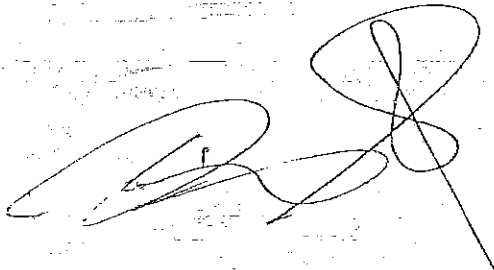
This chapter addresses the Term of Reference that requires the scrutiny of agreements between Government of Uganda and the Independent Power Suppliers. It therefore, presents information on the review of key agreements executed in the electricity sector in Uganda. The first part of this chapter focuses on the agreements signed by GOU and Umeme Limited for electricity distribution. The second part focuses on the agreements signed for power generation by the GOU with Eskom Uganda Limited and other thermal power generators.

4.2 Background to the Privatization of Electricity Distribution Business

The privatisation process of the electricity distribution business was conducted through the international tendering process which started in June 2001. By September 2001, six bidders had expressed interest in the business and these were: CDC Capital Partners (UK), Eskom Enterprises (Pty) South Africa, Union Fenosa International (Spain), Cinergy Global Power (USA), Electricity Supply Board International (Ireland) and Tata Power (India). The firms which were prequalified were Tata Power (India), Union Fenosa International (Spain), and Eskom Enterprises in partnership with CDC Capital Partners.



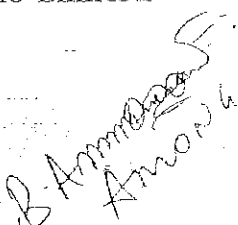
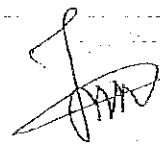
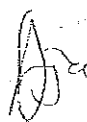
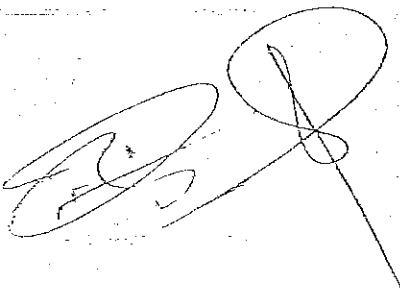

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respectively. On the 28th November 2006, Eskom sold its 44% investment in Umeme Limited to Globeq, thus making Globeq the sole shareholder with 100% ownership by end of 31st December 2006. In October 2009, the ownership of Globeq was transferred to CDC Group Plc. On the 15th October 2009, Globeq was renamed Umeme Holding limited, and on the 3rd December 2009, the ownership of Umeme Holding Limited was transferred from CDC Group Plc to Actis Infrastructure 2 LP.

Umeme Limited signed concession agreements with Government of Uganda (GOU) to manage the power distribution network previously operated by Uganda Electricity Distribution Company Limited (UEDCL) in 2004. The agreements signed by the Company and GOU at the time of handover of the distribution network were:

- (i) **Lease and Assignment Agreement** – in which UEDCL leased its power distribution assets to Umeme Limited to operate for 20 years from the 17th May, 2004. This agreement was signed on behalf of UEDCL by Eng. Irene Muloni M.D., and Esther N. Mulyagonja, Company Secretary UEDCL as a witness. On behalf of Umeme Limited it was signed by D. Grylls, Director and witnessed by T. Caesar, C. Maloka and Velile Dube all Directors.
- (ii) **Support Agreement** – in which GOU is to use its good offices to support the Company's performance of its obligations to design, insure, rehabilitate, operate and maintain the Distribution System for 20 years from the 17th May, 2004. This agreement was signed on behalf of the Government of the Republic of Uganda by Hon. Gerald M. Sendaula Minister, Ministry of Finance Planning and Economic Development (MFPED) and witnessed by Prof. Peter Kasenene, Minister of State Privatisation, MFPED. On behalf of Umeme Limited



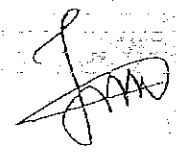
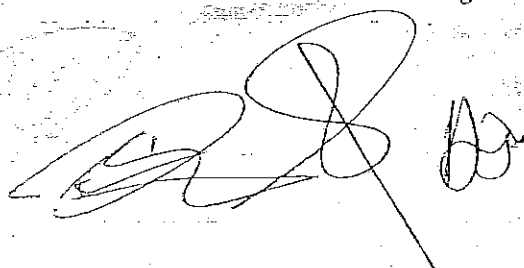
it was signed by D. Grylls, Director and witnessed by T. Caesar, C. Maloka and Velile Dube all Directors.

(iii) **Power Sales Agreement** – in which Uganda Electricity Transmission Company Limited (UETCL) is to sell and the Company is to purchase electricity in quantities adequate to fulfill the Company's service obligations under the Licences for 20 years from the 17th May, 2004. This agreement was signed for and on behalf of UETCL by Eng. Kiyemba Erias M.D, UETCL and witnessed by Dennis Wamala, Company Secretary. On behalf of Umeme Limited it was signed by D. Grylls, Director and witnessed by T. Caesar, C. Maloka and Velile Dube all Directors.

(iv) **Escrow Agreement** – in which an Escrow Account opened with Citibank N.A., London is initially funded by UEDCL to accumulate up a required amount to provide a source of payment to Umeme in the event of certain events described in the Lease Agreement and to serve as security for obligations of GOU under the Support Agreement. This agreement was signed on the 18th February, 2005 by Eng. Irene Muloni M.D., on behalf of UEDCL and witnessed by Esther N. Mulyagonja, Company Secretary UEDCL. On behalf of Umeme Limited it was signed by Luka Buljan, Director and witnessed by P.J. Mare, General Manager.

(v) **Licences** – Besides the above agreements, the Electricity Regulatory Authority issued Licences for Distribution and Supply of Electricity to Umeme Limited on the 1st March 2005. The Distribution Licence was to enable Umeme Limited to perform the activity of distribution of electricity subject, to the Licence Conditions. The Supply Licence was to enable the Company to perform the activity of supply of electricity, subject to the Licence Conditions. Both Licences are to continue in

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effect for a period of 20 years plus 30 days from the Transfer Date as defined in the Licence Conditions.

The following are key clauses and sections in the privatisation of generation and distribution concession agreements as noted in the following sections.

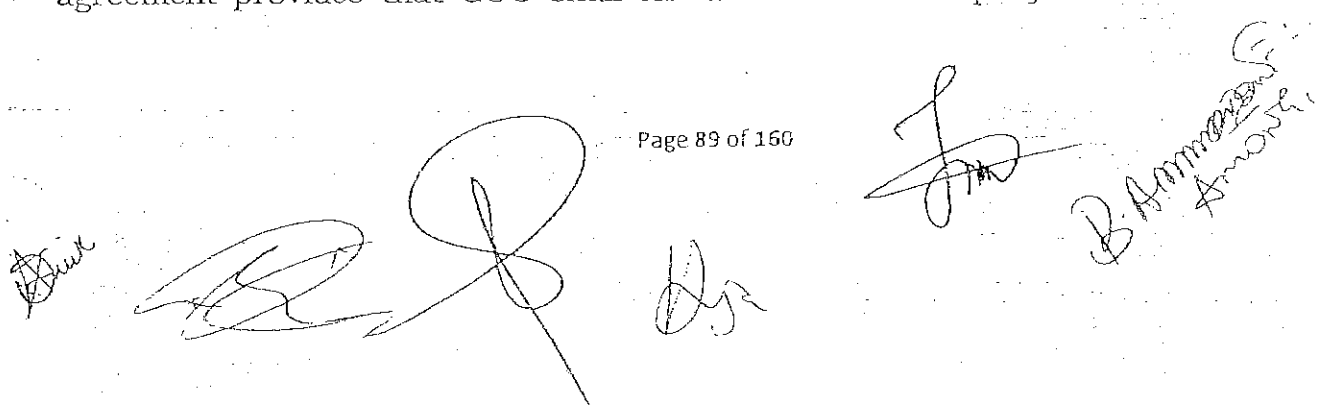
4.2.2 Support Agreement with Umeme

The Support Agreement in which Government of Uganda is to support Umeme's performance of its obligations to design, insure, rehabilitate, operate and maintain the Distribution System for 20 years. For the purpose of this report, the key extracts from this agreement are:-

Under section 2.1, the agreement commenced on 17th May, 2004 and unless extended or terminated earlier, would continue in full force and effect until the 20th anniversary of the transfer date and, subject to payment of the buyout amount. The buyout amounts are funds to be paid to the Company in case of early termination of this Agreement or at the end of its natural Term.

Section 2.2 described matters related to transfer of distribution systems at the end of the term. It states that at the end of Term, unless there is an early company termination, in which case GOU shall pay to the Company the buyout amount as described above, pursuant to Article XII of this Agreement and the Company's rights, title and interest in the distribution system shall terminate. Upon the termination, the distribution system shall be retransferred to UEDCL in accordance with the terms of Lease Agreement.

Under section 4.4 on convertibility of foreign currency and repatriation, the agreement provides that GOU shall ensure that the Company and its direct

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contractors may convert shillings into Foreign Currency, and repatriate any capital, dividends, distribution or other proceeds from the company.

Section 4.5 on Legal Opinion states prior to the transfer date, GOU shall ensure that the Attorney General of Uganda issues an opinion substantially in the form set forth in Annex D of this Agreement.

In **section 6.1** on acquisition of shares or assets, the GOU undertook to the company that neither it nor any relevant authority shall expropriate, compulsorily acquire, nationalize or otherwise compulsorily procure any ordinary share capital, the leased assets, assigned interests or other rights or material assets of the company or its shareholders' interest in relation to the company or distribution system or other rights and interests that are the subject of the lease agreement and the power sales agreement.

Section 9.3 discusses how arbitration of disputes shall be conducted. In the event the parties agree as follows:

- The dispute shall be finally settled by arbitration before a tribunal conducted in accordance the rules of the United Nations Commission and International Trade Law (UNCITRAL).
- Any arbitration shall be conducted in Uganda provided that if the company desires that arbitration be conducted outside Uganda, the arbitration shall be conducted in London, England, and the company shall pay all costs of the arbitration as and when incurred by GOU.
- Notwithstanding the foregoing, if the matter of Dispute involves a sum of **US\$7million** or more, any arbitration as such Dispute shall be conducted in London, England, and in such case, each party shall pay its own costs on arbitration as and when incurred.

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Section 9.5 states issues on sovereign immunity. It posits that Government of Uganda shall unconditionally and irrevocably agrees that should any proceedings be brought against it or its assets, other than its air craft, naval vessels, and other defense - related assets protected by diplomatic and consular privileges, no claim of immunity from such proceedings will be claimed by or on behalf of GOU or any of its assets that is now has or may in the future have in any such jurisdiction in connection with any such proceedings. It also waives any right of immunity which it or may in the future have in jurisdiction in connection with any such proceedings. It too consents generally to the jurisdiction of any court of competent jurisdiction of the arbitration Tribunal appointed under this Agreement to resolve any dispute between the Parties.

Section 12.1 explains the buyout amount options upon Termination. This section documents three main options:

- In case Umeme Limited defaults, the buyout amount shall equal the cost of the Modifications (i.e. upgrade or expansion of the Distribution system and other capital investments made by the company) that is un-depreciated and un-recovered by the company through the tariff multiplied by a percentage equal to 80% if the termination occurs during the period from the end of the initial Period through the 13th anniversary of the Transfer date; such percentage increasing 2% per annum to 94% in the year that is the 20th anniversary of the Transfer Date.
- In the case GOU defaults, buyout amount shall equal the cost of the Modifications that is un-depreciated and unrecovered by the company through the tariff under the licenses as of the date of retransfer of the distribution system to UEDCL multiplied by a percentage equal to 120%

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from the end of the initial period through the 13th anniversary of the transfer date; such percentage declining 2% per annum thereafter to 106% in the year that is the 20th anniversary of the Transfer Date.

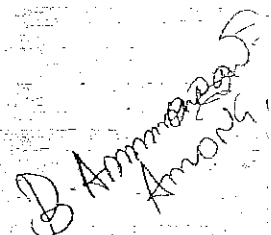
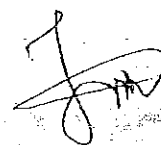
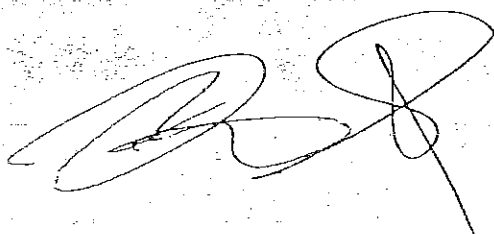
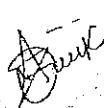
- For natural termination, the buyout amount shall equal 105% of the cost of the Modifications that is un-depreciated and unrecovered by the Company through the tariff under the Licenses as of date of retransfer.

4.2.3 Lease and Assignment Agreement

In this agreement the UEDCL leased its power distribution assets to Umeme Limited to operate for 20 years with effect from 17th May, 2004. Some of the salient extracts in the agreement are:

Section 2.1 Clause (b) states that the occurrence of the transfer date is subject to the following conditions precedent:

- Receipt by the company of Specified Consents that are required to execute activities under the Privatization Agreement.
- Establishment and funding of the Escrow Account by UEDCL.
- Evidence that the Retail Tariff shall have been approved by ERA.
- Receipt by the company of a Uganda Shillings working capital facility from banks in amount equivalent to US\$5million.
- Evidence that the company Escrow Account has been established and funded in the amount of US\$5million.
- Receipt by the Company of an opinion of the Attorney General attached as Annex D to the Support Agreement.
- Receipt of the Company of a list of UEDCL's securely stored stocks, spare parts and other items used by UEDCL in connection with the operation and maintenance of the Distribution System.



- GOU shall have committed to finance investment in the poles and transformers to be incorporated into the Distribution system, in an amount of US\$3million (or equivalent) during each of the first two Agreement Years.

In order to reduce the level of the Retail Tariff applicable in the first Agreement Year, an amount of no less than US\$5million (or equivalent) shall have been committed to the Company to finance Modifications through any combination of funds to be provided by GOU on terms and conditions reasonably acceptable to GOU and the Company and **loans from Ugandan investors in the Company** on terms and conditions reasonably acceptable to GOU, the Company and its shareholders, which Company loan obligations, if any, existing at the time of any termination of this Agreement, shall be assumed by or paid-off and cancelled by GOU upon the termination of this Agreement.

Article III of the lease agreement sets out the terms of termination as follows:

- The Lease Agreement can be terminated by either UEDCL or Umeme Limited.

Section 3.2 Company Events of Default - stipulates the company's events of default which UEDCL may apply to terminate the Lease Agreement.

Section 3.3 UEDCL Events of Default - stipulates UEDCL's events of default which the company may apply to terminate the Lease Agreement.

4.2.4 Power Sales Agreement

An agreement in which UETCL is to sell and the Umeme Limited is to purchase electricity in quantities adequate to fulfill its service obligations under the Licenses for 20 years.

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4.2.5 Escrow Agreement

An agreement in which an Escrow Account opened with Citibank N.A., London is initially funded by UEDCL to accumulate up to a required amount to provide a source of payment to Umeme in the event of certain events described in the Lease Agreement to serve as security for obligations of GOU under the Support Agreement.

The funds deposited in the escrow Account is provide a source of payment to Umeme in the event of certain events described in the Lease Agreement and to serve as security for obligations of GOU under a Support Agreement.

Clause 2 Appointment of Escrow Agent:

Umeme Limited and UEDCL appointed Citibank London, as the Escrow Agent.

Clause 3 Establishment of Escrow Accounts:

The Escrow Accounts were to be opened in the names of UEDCL for US Dollars and Uganda Shillings. The Escrow Account may not go into overdraft. Escrow Account and Escrow Amount shall be the exclusive property of UEDCL, but UEDCL shall have no right to use any part of the Escrow Amount during the term of the Escrow Agreement, and UEDCL hereby grants a first lien and security interest in favor of Umeme in all of its right, title, and interest in and to the Escrow Account and all monies deposited therein.

Clause 6 Operating/ Release Procedure:

The Required Amount on the Transfer Date shall be US\$5million.

The Escrow Account shall be operated as follows:

- Umeme Limited only issues withdrawal certificates to Citibank to access funds on the Escrow Account.

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- Umeme Limited issues Type B Withdrawal Certificate to Citibank to claim lost revenue due to lack of timely tariff approval by the Authority.

Clause 8 Escrow Agent:

To induce the Escrow Agent to act hereunder, it is further agreed by Umeme Limited and UEDCL that:

- The Escrow Agent is under no duty to ensure that funds withdrawal from the Escrow Account are actually applied for the purpose for which they were withdrawn, or that any claims made in any Withdrawal Certificate or other instruction or direction by Umeme Limited or UEDCL is accurate.
- The Escrow Agent may act upon any Withdraw Certificate without being required to determine the correctness of any fact stated therein.

Clause 11 Fees and Expense:

The Escrow Agent shall be entitled to total fees of US\$50,000 for first year and thereafter to total fees of US\$20,000 per annum. The Escrow Agent's annual fees shall be paid in advance in 4 installments. If the Escrow Amount is insufficient to cover the payment of the Escrow Agent's fees, such fees shall be paid by UEDCL within 30 days of the Escrow Agent's delivering its invoice to UEDCL and Umeme Limited shall not be liable therefore.

4.2.6 Power Distribution and Supply Licences

These were issued by ERA to Umeme Limited on 1st March 2005. The Distribution Licence enables Umeme Limited to perform the activity of distribution of electricity and while the Supply Licence enables the Company perform the activity of supply of electricity, subject to the License Conditions. Both Licences are to continue in effect for a period of 20 years plus 30 days from the Transfer Date as defined in the Licence Conditions.

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4.3 Findings

i. Peripheral role played by the Attorney General

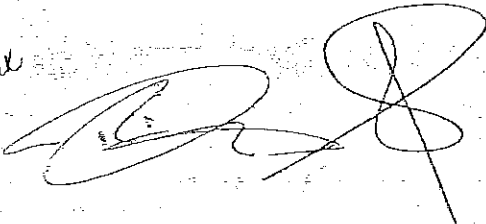
The divestiture and reform process of UEB and the subsequent procurement of Umeme Limited, the power distribution concession in Uganda was directed, managed and overseen by the Privatization Unit of Ministry of Finance, Planning and Economic Development with little or no involvement of other key Government institutions, notably the Attorney General.

From the submission made before the Ad hoc Committee by Mr. David Ssebabi, the Director, Privatization Unit MFPED, and leader of the Government of Uganda Negotiation Team, the Privatization Unit hired "Transaction Advisors" in the name of Hutton and Williams (a US based private firm) on whose purported legal/technical expertise and wealth of experience in the utility sector they relied upon to draft, negotiate and finally sign all the power distribution concession agreements with Umeme Limited. The office of the Attorney General was just represented by a legal officer whose contribution in the exercise is not documented.

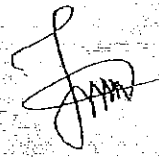
The Attorney General played a peripheral role in the preparation, drafting and signing of the Umeme Limited's agreements. According to Mr. David Ssebabi, the Privatization Unit procured and contracted Transaction Advisors who performed the Attorney General's Constitutional duty of drafting and perusing agreements on behalf of Government.

It was also found that Counsel to UMEME in conjunction with Uganda's Transaction advisors hired by PU/MFPED drafted the Umeme Power Distribution Concession agreements and dictated the format the Attorney General's opinion would take. Mr. David Ssebabi informed the Committee

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that the Attorney General's opinion was also negotiated among other clauses of these agreements.

Article 119(4)(b) of the Constitution of Uganda enjoins the Attorney General 'to draw and peruse agreements, contracts, treaties, conventions and documents by whatever name called, to which the Government is a party or in respect of which the Government has an interest'. It is a Constitutional duty that cannot be delegated. The committee failed to get proof from the current Deputy Attorney General Hon. Fredrick Ruhindi who represented the Attorney General during this investigation, that the Attorney General performed this duty.


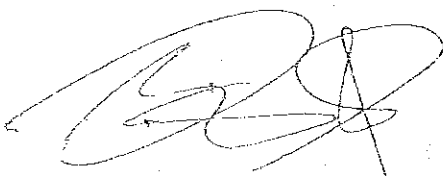
ii. No Benchmark Studies Done Prior to Negotiations

The Government of Uganda team that negotiated the Concession agreements other than admitting their technical ineptitude and lack of experience did not carry out prior benchmark studies and therefore lacked critical information needed at the time to plan and conclude negotiations in national interest. They did not carry out prior studies to appreciate the state of dilapidation of the distribution network in the country; the actual level of losses (both technical and non-technical), the critical areas of investment and ultimately the level of investments required to rehabilitate and restore the network and reduce losses to acceptable best practice levels.

iii. Negotiations Held in Washington, USA

It also emerged during this investigation that, the negotiations between Government of Uganda Umeme Limited took place in Washington in the United States of America. There was no justification whatsoever, for Government to have chosen Washington as the venue for negotiations with Umeme Limited, for a service to be locally contracted in Uganda. This lends credence to the belief that the whole process of procuring,

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drafting, negotiating and signing the power distribution concession was controlled, directed and managed by the Concessionaire (UMEME).

iv. Lack of Experience and Technical Competence by the GOU Negotiating Team

During the appearance of the of the Government of Uganda negotiating team led by led by Mr. David Ssebabi (Current Director of Privatization Unit, MFPED) before the Committee, they admitted their lack of experience and technical competence in the sector, and interestingly they were oblivious of the details of the terms and conditions of these agreements. But the team went ahead consciously or unconsciously to make a deal on behalf of GOU.

v. Concession Procurement Process

As stated above and in response to a written question as to how Umeme secured the distribution concession, the Committee did not receive any answer. How then did Umeme come to know of the business opportunity in the power sector in Uganda? The Committee did not receive any answer. The Committee found as a fact that:

a. Umeme Limited was not in existence at the time of bidding and negotiation. The Umeme Limited that finally signed the concession agreements is not the one that bidded. The Umeme Limited that signed the concession agreements was formed eleven (11) days before the signing of agreements. This means the negotiations for the power distribution concession agreements which took some months were prejudiced since ESKOM Enterprises was negotiating with itself through Paul Mare' and that UMEME Limited was formed after negotiations were complete.

b. Of all the six bidding companies, only a seemingly unregistered "consortium" of CDC and Eskom submitted their bid but which was

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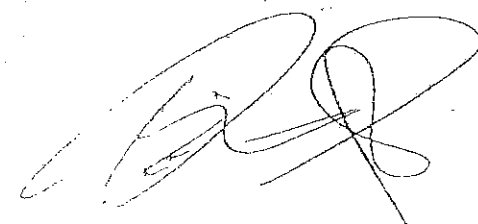
strangely accepted by Government. However, these "consortium" never appeared anywhere thereafter. Instead a new company in form of Umeme Ltd was incorporated on 6th May, 2004 with the principle objective of signing a Lease and Assignment agreement with the Government. It would appear on the face of it, that this transaction was pre-decided before incorporating the company.

c. It should be noted that at this time Eskom Enterprises had already obtained the electricity power generation at Nalubaale.

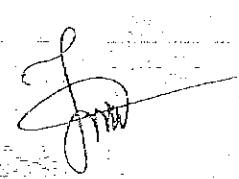
d. The Committee further observes that whereas the envisaged "consortium" was seemingly between CDC Capital Partners and Eskom Enterprises, Umeme was only registered with two shareholders: Globleq Holdings (Conco Ltd), whose address is CANON'S Court, 22 Victoria Street, Hamilton, Bermuda HM12 and Eskom Enterprises (Pty) Ltd whose address is: Maxwell Drive Sunninghill 2157 Republic of South Africa. CDC Capital Partners, registered in the U.K., does not appear in the company (Umeme), which eventually signed the Concession agreement even when it was supposedly the second partner in the "consortium".

e. Whereas the Committee was informed by the Attorney General that the Government accepted the single bid of the consortium between CDC Partners and Eskom Enterprises, no single document was availed in proof of the alleged consortium. In his submission, dated 12th May, 2012, the Deputy Attorney General, Hon. Fredrick Ruhindi informed the Committee that Umeme Ltd. was established as a Special Purpose Vehicle by CDC and Eskom to manage the Concession, Umeme's Articles and Memorandum do not indicate CDC as a shareholder or participant in any way in the process leading to the incorporation leading to Umeme.

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f. The Committee further noted that whereas the learned Deputy Attorney General presents Umeme Ltd as a special purpose vehicle to manage the concession, from the evidence available, such was neither envisaged nor stipulated in the Article and Memorandum of Association. This is further evidenced by the Umeme Ltd's objects contained in their Memo, No. 3 (b) is "to generate (if permitted under relevant licenses), distribute and supply electricity", and neither does Umeme refer, anywhere in its establishment, to the said "consortium".

g. This confirms the reason why when Umeme Limited was asked by the Committee as to who Umeme was, they simply responded by attaching the Certificate of Incorporation, dated 6th May 2004 and the Articles and Memo of Association of 4th May, 2004. This was as if to admit the above irregularities without necessarily stating them.

vi. No Early Termination Option by Government

Section 10.6 provides that only the Company and not the Government may, in its sole discretion, commence early termination proceedings by giving reasonable notice to Government but in any case not later than 60 days prior to the end of the initial period. Clearly the Government has no option of an early termination and upon receipt of the notice the option of Government is to receive its assets in whichever form. Without doubt, the Government, in these provisions, does not have an option for early termination.

vii. Compensation to Umeme Limited in Case of Company Default

From Section 12.1 of the Support Agreement, even if Umeme Limited defaulted in carrying out its obligations as stipulated in the agreement and initiated the termination of the agreement, GOU would still have to

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pay the Company a buyout amount equal the cost of the Modifications (i.e. upgrade or expansion of the Distribution system and other capital investments made by the company) that is un-depreciated and unrecovered by the company through the tariff multiplied by a percentage equal to 80% if the termination occurs during the period from the end of the initial Period through the 13th anniversary of the Transfer date; such percentage increasing 2% per annum to 94% in the year that is the 20th anniversary of the Transfer Date.

viii. According to documents accessed from the Uganda Registration Services Bureau (the Articles and Memorandum of Understanding among others) the Committee established that Umeme Limited was formed in April 2004 by two companies i.e. CDC Globlec Holdings (Conco) Limited with 56% shareholding and Eskom Enterprises (PTY) Limited with 44%. However, upon scrutiny of the UMEME file, the Committee found out that the signature placed alongside the directorship of Globlec Holdings Limited is the signature of a lawyer called Ezekiel Tuma. The second signature placed next to the directorship of ESKOM Enterprises is the signature of Allan Shonubi. Both **Ezekiel Tuma and Allan Shonubi** work for the same law firm of M/S Shonubi, Musoke and Company Advocates, the same people whom GOU contracted as Transaction Advisors during the procurement of the Umeme Limited's Concession.

ix. Lack of Powers of Attorney and Company Resolution

The Committee after thorough scrutiny of Umeme Limited's file obtained from the Uganda Registration Services Bureau also found that, there were neither Powers of Attorney nor a company resolution from CDC Globlec or Eskom Enterprises permitting Allan Shonubi and Ezekiel Tuma to endorse on their behalf. The signatures in the Memorandum

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and Articles of Association for purposes of having Umeme Limited incorporated are therefore, from a legal point of view, a nullity and void.

x. Lack of Memorandum and Articles of Association


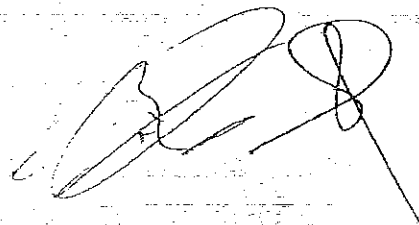
It is important to note that under the Companies Act of Uganda it is a legal requirement that any foreign company conducting any business in Uganda ought to deposit at the Company Registry its original Memorandum and Articles of Association from its home country. Unfortunately, these key documents as required by the law could not be found on the file of Umeme Limited. Efforts by this Committee to secure these documents from Umeme Limited bore no fruits.

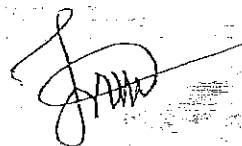
xi. Unresolved Tax Evasion by Eskom Enterprises

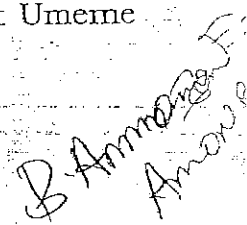
When Eskom Enterprises sold its 44% share investment in Umeme Limited to Globlec in 2006, the Company did not pay Capital Gains Tax (CGT) to URA. The URA argues that since the transfer of shares was between foreign companies that are not liable to paying CGT and therefore there was no case for the transferor to pay Capital Gains Tax. However, the Committee strongly objects to the URA explanation since Umeme is a locally incorporated Company which is bound by the Municipal laws. Equally so, in the recent past Foreign Oil companies operating in Uganda were compelled (after Parliament's objection to their none-tax compliance) to pay Capital Gains Tax.

4.4 Analysis and Observations

- i. Section 9.5 of the Support Agreement removes the immunity of Government of Uganda from claiming its assets that it has now or may have in future in case Umeme Limited brought any legal proceedings against Government. This provision was meant to ensure that Umeme



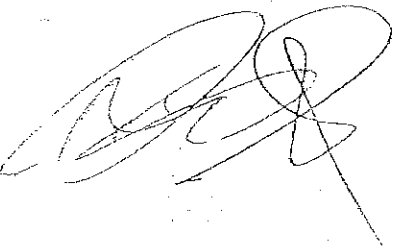

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Limited is paid at whatever cost by GOU in case of any legal proceedings brought by the Company against Government. The Committee observes that since the immunity of a country's assets is a matter of law it cannot be amended by an agreement. To this extent the provision of Section 9.5 of the Support Agreement is unfair and a nullity.

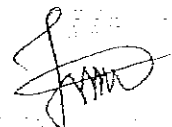
- ii. Section 2.1 Clause (b) of the Lease and Assignment Agreement had a provision stating that upon the occurrence of the transfer date the Company should have received from GOU Uganda Shillings working capital facility equivalent to US\$5 million. This was a case of a private investor being funded by GOU before it could commence its operations.
- iii. The GOU was also to provide evidence to the Company that the Escrow Account had been established and funded in the amount of US\$5 million. Whereas the monies from this Escrow Account provided security to Umeme, there was no corresponding security from Umeme to Government in the event of the breach.

Secondly, there was no determined independent mechanism stipulating when Umeme would have recourse to the moneys in the Escrow account, how much and what remedies would be available to Government in the event of a wrongful withdrawal. As it stands, Umeme is at liberty to withdraw and simply notify Government of the recourse to the account.

- iv. Again in Section 2.1 Clause (b) of the Lease and Assignment Agreement the GOU was to provide to the Company a list of UEDCL's securely stored stocks, spare parts and other items used by UEDCL in connection with the operation and maintenance of the Distribution System. The stored stocks and spare parts had been procured by

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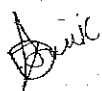
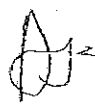
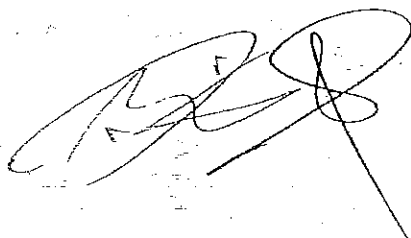
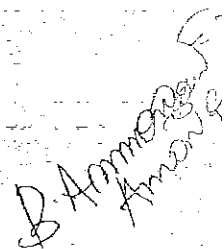
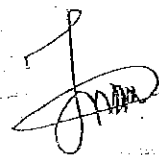
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UEDCL with a loan from the International Development Agency (IDA) and the Company was to take over the stored stock without any payment to UEDCL. The Committee received no evidence that the value of the stored stock was ever ascertained and taken into account during or after the negotiations or was ever applied in diminution in the Government financial obligation under the agreement. Such must have occasioned an unascertained loss to Government, more so having acquired them on loan from the IDA.

- v. The private Company was required to invest in the rehabilitation of the electricity distribution network. But in Section 2.1 Clause (b) of the Lease and Assignment Agreement GOU was required to have committed to finance investment in the poles and transformers to be incorporated into the Distribution system, in an amount of US\$3million (or equivalent) during each of the first two Agreement Years. The private investor was expected to have come with its capital for investment in such activities and yet the agreement provided for GOU financing.

This clause does not make sufficient provision for Government monitoring, evaluation, verification, value for money audit and or quality assurance. In addition to the lack of investment plan, there were no procurement guidelines that would guarantee sufficient protection of Government interests.

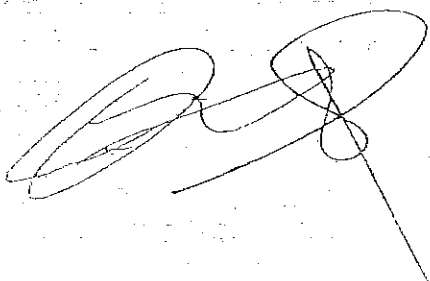
- vi. In view of the above, the Committee finds that the negotiations, procurement process between Uganda and the European companies reduced Uganda preposition below European private companies. Indeed, Spanish Prime Minister Mariano Rajoy is reported to have said "We're the number four power in Europe, Spain is not Uganda", in an effort



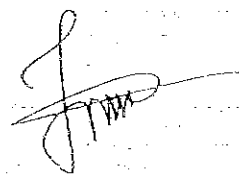
to encourage his Minister for finance to stay strong in securing a bailout package.

Note: In the absence of Powers of Attorney and company resolution from CDC Globleq and Eskom Enterprise authorizing **Ezekiel Tuma and Allan Shonubi** to endorse the incorporation of Umeme Limited on their behalf, and the failure by CDC Globleq and Eskom Enterprises to deposit with the Company Registry their original Memorandum and Articles of Association from their respective home countries, it can be concluded that there were some fraudulent players in the procurement of Umeme's power distribution concession and thus objection to Umeme Limited's locus and status in law.

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EXAMPLES OF SCENARIOS IN CASE OF TERMINATION OF AGREEMENTS

The following scenarios show the possible Buy Out Amounts that would be paid to Umeme Limited in case the Agreements signed with the Company are terminated earlier or reach end of natural term.

The Date of Commencement of Agreements was 17th May 2004. The Initial Period as defined in the Lease Agreement is 668 days from the date of handover of the Distribution System to Umeme Limited. The Initial Period started on 17th May 2004, and ended 18 months thereafter.

Scenario 1: Case of GOU Initiating Termination of Contract

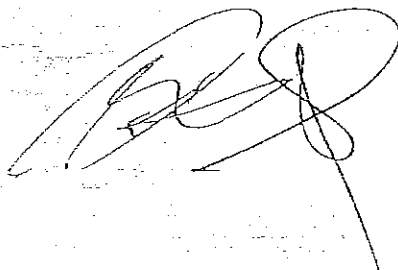
Pursuant to Buy Out Provisions Article XII, Section 12.1 Clause (b) of the Distribution Support Agreement, if GOU terminated Umeme Limited's Concession Agreements, the Buy Out Amount shall be calculated as follows:

- (i) the cost of modifications that is undepreciated and unrecovered by Umeme Limited at the time of retransfer of the Distribution System to UEDCL, multiplied by
- (ii) a percentage equal to 120% from the end of the Initial Period through the 13th Anniversary of the transfer date, such a percentage declining 2% per annum thereafter to 106% in the year that is the 20th Anniversary of the transfer date.

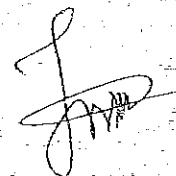
(a) Amount Umeme Limited claims to have invested as at August 2011 is US\$130 million.

(b) The Company also claims to have only recovered US\$7 million leaving an undepreciated and unrecovered amount of US\$123 million. Therefore, the Buy Out Amount shall be calculated pursuant to the Buy Out Provisions as mentioned above.

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The computation of Buy Out Amount if GOU initiated termination of the Concession Agreements now would be as follows:

Amount unrecovered US\$123 million x 120% = US\$147.6 million

The GOU would have to pay Umeme Limited a Buy Out Amount of US\$147.6 million if it initiated the termination of the Concession Agreements now.

It is important to note that the Buy Out Amount calculated shall be paid by GOU to Umeme Limited within 91 days, short of this GOU shall be required to pay 20% interest per annum on the outstanding Buy Out Amount until such a time when it is fully paid.

Scenario 2: Case of Umeme Limited Initiating Termination of Contract

Pursuant to Buy Out Provisions Article XII, Section 12.1 Clause (a) of the Distribution Support Agreement, if Umeme Limited initiated termination of Concession Agreements, the Buy Out Amount shall be calculated as follows:

- (i) the cost of modifications that is undepreciated and unrecovered by Umeme Limited at the time of retransfer of the Distribution System to UEDCL, multiplied by
- (ii) a percentage equal to 80% if the termination occurs during the period from the end of the Initial Period through the 13th Anniversary of the transfer date, such a percentage increasing 2% per annum to 94% in the year that is the 20th anniversary of the transfer date.

(a) Amount Umeme Limited claims to have invested as at August 2011 is US\$130 million.

- (b) The amount Umeme Limited has invested and is undepreciated and unrecovered as of August is US\$123 million. Therefore, the Buy Out Amount shall be calculated pursuant to the Buy Out Provisions as mentioned above.

The computation of Buy Out Amount if Umeme Limited initiated termination of the Concession Agreements now would be as follows:

Amount unrecovered US\$123 million x 80% = US\$98.4 million


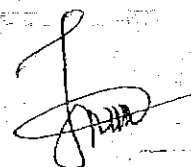
From the above calculation GOU would have to pay Umeme Limited a Buy Out Amount of US\$98.4 million if the Company initiated the termination of the Concession Agreements now.

It is important to note that as in Scenario 1, the Buy Out Amount calculated shall be paid by GOU to Umeme Limited within 91 days, short of this GOU shall be required to pay 20% interest per annum on the outstanding Buy Out Amount until such a time when it is fully paid.

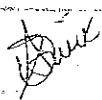
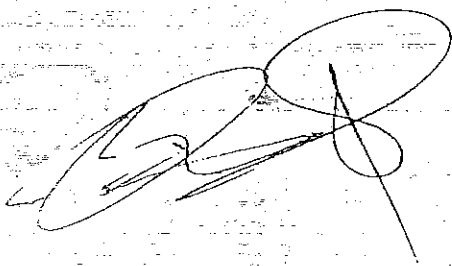
Scenario 3: Case of Natural Termination of Contract

Pursuant to Buy Out Provisions Article XII, Section 12.1 Clause (d) of the Distribution Support Agreement, if Umeme Limited operates until the 20th anniversary of the Contracts, that is, up to the end of the 20th year contract period,

- (a) the Buy Out Amount shall be equal to 105% of the cost of modifications that is undepreciated and unrecovered by Umeme Limited at the time of retransfer of the Distribution System to UEDCL.



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(b) Assume amount invested by Umeme Limited that is undepreciated and unrecovered as at the end of the natural term is US\$123 million. And also assume that the end of the Natural Term is now. Therefore, the Buy Out Amount would be calculated pursuant to the Buy Out Provisions as mentioned above.

The computation of Buy Out Amount if the end of the Natural Term of the Concession Agreements was now would be as follows:

Amount unrecovered US\$123 million \times 105% = US\$129.15 million

The GOU would have to pay Umeme Limited a Buy Out Amount of US\$129.15 million if the Natural Termination of the Concession Agreements was now.

As in the previous two scenarios above, the Buy Out Amount would be paid by GOU to Umeme Limited within 91 days, short of this GOU shall be required to pay 20% interest per annum on the outstanding Buy Out Amount until such a time when it is fully paid.

N.B. Pursuant to Buy Out Provisions Article XII, Section 12.1 Clause (a) and (b) of the Distribution Support Agreement, either Umeme Limited or GOU can initiate the early termination of this Agreement. It should be noted, however, that the longer Umeme Limited continues operating the power distribution network the higher the amount of money it will claim to have invested over the years. This will mean a high Buy Out Amount will have to be paid if Umeme Limited either operated up to the end of natural period or if the Agreements are terminated early.

The support agreement has documents regarding the payment modalities. In case of early termination of the Support Agreement, GOU shall pay the appropriate buyout amount in US Dollars not later than 270 days following

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receipt or issuance of the termination notice or 90 days following the final resolution of any dispute related thereto. In addition a percentage equal to 120% from the end of the initial period through the 13th anniversary of the transfer date; such percentage declining 2% per annum thereafter to 106% in the year that is the 20th anniversary of the transfer date.

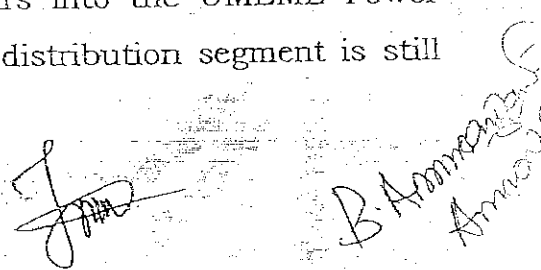
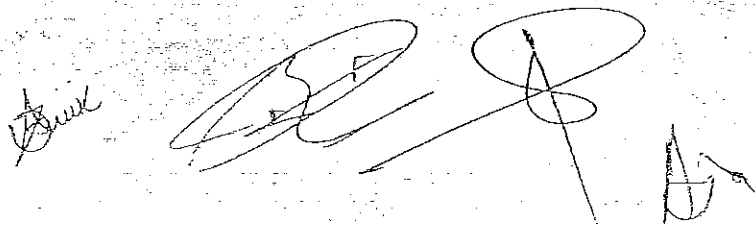
The company shall deliver to GOU not later than 90 days prior to the end of the Natural Term, and if this agreement is terminated earlier not later than 45 days following the commencement of the retransfer transition period, a statement of the estimated buyout amount payable. The estimate of the buyout amount will be reconciled to determine the final buyout amount. Amounts claimed shall be subject to audit by GOU.

If VAT or any other sales tax is required to be charged by the company on the buyout amount, GOU shall pay such taxes in addition to the buyout amount so that the company receives the full benefit of the relevant buyout amount calculated.

In the case of a termination before the end of the Natural Term, if the payment of the Buy Out Amount is delayed 150 days following the delivery of a Termination Notice or 90 days following the final resolution of any dispute related thereto, GOU shall pay the Company interest on any outstanding portion of the Buy Out Amount at a rate of 20% for the period from and after 91 days after the Buy Out Date.

Were/are the Umeme Power Distribution Concession Agreements therefore fair to Government and the People of Uganda?

It must be reiterated that more than seven years into the UMEME Power Distribution Concession, the country's electricity distribution segment is still



characterised by dilapidated infrastructure (despite the claim by UMEME to have invested over \$130million in the network), high energy losses, poor quality of supply, energy utilization inefficiencies and high end-user tariff.

Whereas the concession agreements are reported to have generally conformed to basic international standards, they were crafted to strongly favour UMEME Ltd at the expense of the Government and people of Uganda in terms of return on investment, arbitration, buy-out conditions on termination of the contract, days lag/working capital allowance, and risk allocation.

In view of the provisions of these agreements that are highly skewed in favour of UMEME, it is highly questionable whether the learned Attorney General addressed his mind to the finer details and implications of these provisions on the people and Government of Uganda.

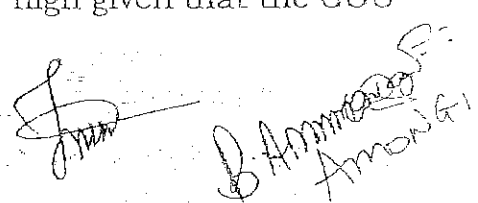
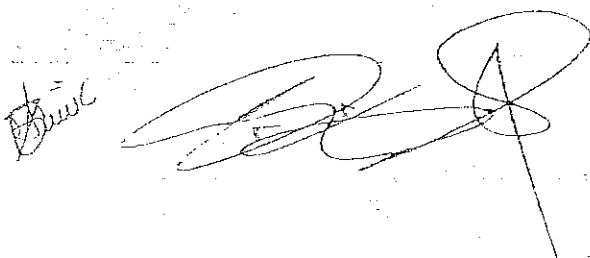
The concession agreements lack key performance indicators and standards that would enable the efficient and effective monitoring of the concessionaire. The agreements predominantly reflect the strengths of Globeleq/Actis(UMEME Ltd), who were the lead partner in the concession.

A Reflection on Specific Provisions

Committee deems the following specific provisions of the Lease and Assignment Agreement between UEDCL and UMEME Ltd outrageous, and therefore too unfavourable to the people and Government of Uganda:

i) Return on Investment

Return on investment levels are generally higher where the perceived investment risks are high. The return on investment set as 20% is high given that the GOU



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had assumed most of the risks associated with investments in the sector. Whilst the 20% was agreed upon in the LAA it was not reflective of similar and comparable target returns.

ii) Dispute Resolution

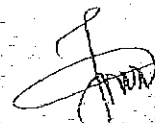
Parties under the agreement are required to attempt to resolve any disputes through their authorised representatives. Failure to resolve the dispute within 30 days from the date of service of notice of dispute necessitates the parties to refer the dispute to a tribunal to be arbitrated under the NNICTRAL Rules and decision by such tribunal would be final and binding as the sole and exclusive remedy between the parties.

In the event that certain rights of appeal, not waived by the parties do exist, they shall be exercisable by the interested party after full implementation of the tribunal award or payment under such award if payment is required but not before.

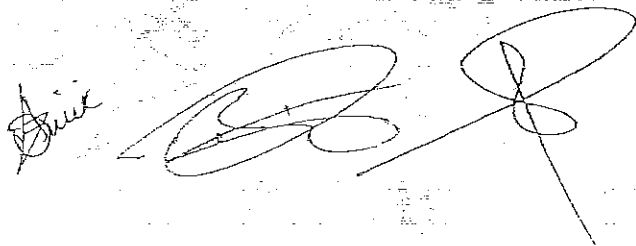
Enforcement of awards is subject to the jurisdictions of the courts or tribunals in Uganda, and the United Kingdom. Much as arbitration can be conducted in Uganda, UMEME Ltd. has the right to opt to have the arbitration conducted in the United Kingdom and would also pay any out of pocket expenses over and above what would have been incurred had the arbitration been held in Uganda.

UMEME Ltd. retains the right to determine whether any dispute of a value of over \$7 million can go to international arbitration.

GOU under the dispute resolution agreement waived its sovereign immunity and jurisdictions over its current and future assets in any part of the world save for its aircraft, naval vessels and other defence related assets or assets



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protected by the Diplomatic and Consular privileges under the 1976 Sovereign Immunities Act of the UK or the 1976 Sovereign Immunities Act of the USA or any analogous legislation, for purposes of enforcement of any award under the Arbitration Agreement. UMEME Ltd. also consented that jurisdiction over its current and future assets and rights be subject to any court of competent jurisdiction for any action filed by GOU.

iii) Termination

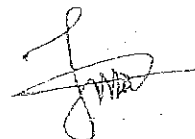
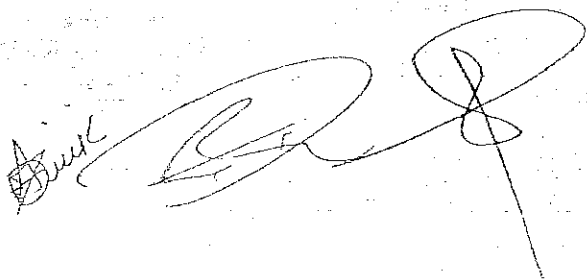
The Support Agreement offers several options for termination. The GOU is given the right to terminate the agreement due to the occurrence of an UMEME Ltd event of default, which is not cured within the permitted time.

Such events include a breach by the company due to a force majeure event, a breach by GOU under the Support Agreement, a breach by UETCL under the Power sales Agreement, a breach by UEDCL under the Lease and Assignment Agreement or any event, which would constitute an event of default by GOU, UETCL or UEDCL under the respective agreements.

UMEME Ltd also has a right to terminate based on a GOU event of default, which is not cured within the prescribed time as long as an event does not substantially result from a breach by UMEME Ltd. of any of the privatisation agreements.

iv) Buy out provisions

Considering that the option of early termination during the initial period was not exercised, UMEME Ltd. is entitled to be paid a buyout amount upon termination of the agreement. This termination can be due to the occurrence of



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a company event by default, GOU event of default, political force majeure event.

The buyout amount (BOM) is given by the product of the cost of modifications undepreciated and unrecovered (CM) by UMEME Ltd through the tariff under the license as of the date of retransfer of the distribution system to UEDCL or its designee and a multiplier (M) equal to percentages.

v) Sovereign Immunity

Section 9.5 of the support Agreement states issues on sovereign immunity. It posits that Government of Uganda shall unconditionally and irrevocably agrees that should any proceedings be brought against it or its assets, other than its air craft, naval vessels, and other defense - related assets protected by diplomatic and consular privileges, no claim of immunity from such proceedings will be claimed by or on behalf of GOU or any of its assets that is now has or may in the future have in any such jurisdiction in connection with any such proceedings. It also waives any right of immunity which it or may in the future have in jurisdiction in connection with any such proceedings. It too consents generally to the jurisdiction of any court of competent jurisdiction of the arbitration Tribunal appointed under this Agreement to resolve any dispute between the Parties.

Observations

The concession agreements, while generally conforming to the basic standards, were crafted to strongly favour the private concessionaire at the expense of the people and government of Uganda in terms of return on investment, arbitration, buy-out conditions on termination of the contract, and risk allocation.

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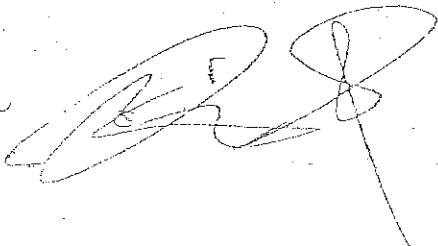
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- i) In the dispute resolution provisions, the location of arbitration is London for amounts above US\$7. million. The GOU waived its sovereign immunity on its assets other than those protected by diplomatic and consular privileges.
- ii) UMEME Ltd gets compensated on termination of the agreement irrespective of the cause. Where the government causes the termination, UMEME Ltd gets paid a higher percentage than it gets paid when it is the cause.
- iii) There is an absence Key performance indicators (KPIs) and standards that would enable the efficient and effective monitoring of the concessionaire. The agreements are predominantly legal, commercial and financial reflecting the strengths of the lead partner in the concession.
- iv) The minimum level of service guiding principles should have been used to determine key performance indicators like actual energy losses, customer interruptions etc. that would be used for monitoring supervising the concessionaire.

Conclusion

It is the Committee's firm conviction that if the learned Attorney General had carried out his/her Constitutional duties as provided in Article 119(3), (4) and (5), by addressing his/her mind to the finer details of these agreements there is no way he/she could have committed Government and people of Uganda to such lopsided power distribution, concession agreements with such unfair provisions like the abnormal buy out amounts, loss of sovereign immunity and working capital allowances among others.

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The Committee recommends that:

i. Due to the gross legalities and manipulations encountered surrounding the procurement of the Umeme Concession and the scandalous provisions of these power distribution agreements signed between Government of Uganda and Umeme Limited, this contract should be terminated.

ii. The URA should take up the matter of evasion payment of Capital Gains Tax by Eskom Enterprises when it sold its shares to Globeq and ensure recovery of the said tax.

4.7 THE ESKOM POWER GENERATION CONCESSION

The privatisation process of the electricity generation business was conducted through the international tendering process which started in 2001. By September 2001, the firms which were prequalified to bid for Generation Concession were Tata Power (India), Union Fenosa International (Spain), and Eskom Enterprises (South Africa). Request for Proposals were sent to the three pre-qualified bidders but Tata Power did not submit its bid thus effectively leaving only two bidders Union Fenosa International and Eskom Enterprises.

As part of procurement procedure, these firms conducted due diligence in order to prepare their bids. However, Union Fenosa did not attend the pre-bid meetings that had been scheduled to take place in January 2002 and hence no bid was submitted by this Company. This effectively left Eskom Enterprises as the only bidder for Generation Concession.

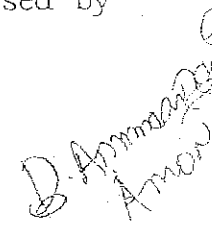
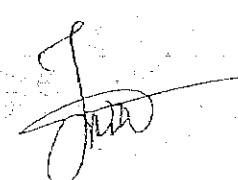
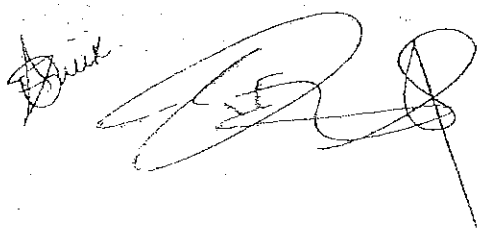
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4.7.1 Agreements Signed by Government of Uganda and Eskom (U) Ltd

Eskom Uganda Limited, the main electricity generator in Uganda is a private limited liability company which was incorporated under the Laws of Uganda. Eskom Uganda Limited signed Concession and Assignment Agreement with Uganda Electricity Generation Company Limited (UEGCL) relating to the Nalubale and Kiira Hydroelectric Facilities located near Jinja, Uganda on the 26th day of November 2002. The concession agreement gave authority to Eskom Uganda Limited to manage power generation previously operated by UEGCL in 2002. Other agreements signed by the Company included the Support Agreement signed with Government of Uganda, the Power Purchase Agreement signed with Uganda Electricity Transmission Company Limited (UETCL), and the Escrow Agreement signed with UEGCL.

- (i) **Concession and Assignment Agreement** – in which UEGCL granted Eskom Uganda Limited and the Company accepted from UEGCL the Concession Interest and the right to sell and transfer the Available Capacity of the Nalubale and Kiira Complex and the Net Electrical Output generated by the Complex to UETCL in accordance with the terms of the Power Purchase Agreement to operate for 20 years from the transfer date. The transfer date was the date on which UEGCL delivered possession of the Concession Interest, Assigned Interest and Other Rights to the Company pursuant to Clause 2.1 (b) of this agreement. The transfer date in this case was 90 days after the signing of the Generation Concession Agreements.

This agreement was signed on behalf of UEGCL by Mr. John Mugenyi, Managing Director, and by Mr. Emmanuel Lubandi, Company Secretary UEGCL as a witness. On behalf of Eskom Uganda Limited it was signed by Dr. Enos Ned Banda, Chairman of the Board and witnessed by



Stephanus Christiaan du Plessis, Venture Development Manager (Hydro).

(ii) **Support Agreement** – in which GOU is to support the Company's operation and maintenance of the Complex and finance, undertaking and managing of the restoration and reinforcement of the Complex's generation substations. This support was to be implemented in a manner that reflected the cooperation and support provided by the public sector in Uganda to the private companies operating facilities for the generation of electricity for sale on the national grid for 20 years from the 26th November, 2002. This agreement was signed on behalf of the Government of the Republic of Uganda by Hon. Gerald M. Sendaula Minister, Ministry of Finance Planning and Economic Development (MFPED) and witnessed by Prof. Peter Kasenene, Minister of State Privatisation, (MFPED). On behalf of Eskom Uganda Limited it was signed by Dr. Enos Ned Banda, Chairman of the Board and witnessed by Stephanus Christiaan du Plessis, Venture Development Manager (Hydro).

(iii) **Power Purchase Agreement** – in which Eskom Uganda Limited is to sell to Uganda Electricity Transmission Company Limited (UETCL), and UETCL is to purchase from the Company, the Available Capacity and the associated Net Electrical Output of the Complex and Ancillary Services for 20 years from the 26th November, 2002. This agreement was signed for and on behalf of UETCL by Eng. Erias Kiyemba, Managing Director UETCL, and witnessed by Dennis L. Wamala, Company Secretary. On behalf of Eskom Uganda Limited it was signed by Dr. Enos Ned Banda, Chairman of the Board and witnessed by Stephanus Christiaan du Plessis, Venture Development Manager (Hydro).

(iv) Escrow Agreement – in which an Escrow Account opened with an Escrow Agent agreeable to the Parties to the Concession Agreement.

(v) Licences – Besides the above agreements, the Electricity Regulatory Authority (ERA) issued Licences for Generation and Sale of Electricity to UETCL. The Generation Licence was to enable Eskom Uganda Limited perform the activity of generation of electricity subject, to the Licence Conditions. The Sales Licence was to enable the Company to perform the activity of selling electricity, subject to the Licence Conditions. Both Licences are to continue in effect for a period of 20 years from the Transfer Date as defined in the Licence Conditions.

The following are key clauses and sections in the privatisation of generation concession agreements as noted in the following sections.

4.7.2 Support Agreement with Eskom(U) Ltd

The Support Agreement in which Government of Uganda shall use its good offices to support Eskom Uganda Limited's performance of its obligations to design, insure, rehabilitate, operate, and maintain the Generation Complex. For the purpose of this report, the key extracts from this agreement are:-

Under Part II, Clause 2.1, the agreement commenced on 26th November, 2002 and unless extended or terminated earlier, would continue in full force and effect until the 20th anniversary of the Transfer Date; provided, however, if the term of the Power Purchase Agreement is extended the Term shall also be extended for a period equal to the period of extension of the Power Purchase Agreement.

Clause 2.2 described matters related to transfer of the Generation Complex at the end of Term. It states that at the end of Term, GOU shall pay to the Company the Buy Out Amount pursuant to Part II, Clause 11.1 of this Agreement and the Company's rights, title and interest in and to the Concession Agreement shall terminate. Upon the termination, the Complex shall be retransferred to UEGCL in accordance with the terms of Concession Agreement.

Clause 2.4 on Legal Opinion states that, this Agreement will only come into full force and effect and binding on GOU and the Company, on receipt by the Company of a legal opinion, to its satisfaction and acceptance by the Attorney General of Uganda that all the necessary authorisations and permissions have been granted in terms of the Laws of Uganda for execution of this Agreement by GOU and the Agreement is enforceable against GOU as set out herein.

Under Part IV Clause 4.3 on convertibility of foreign currency and repatriation, the agreement provides that GOU shall ensure that the Company and its direct contractors may convert shillings into Foreign Currency, and repatriate any capital, dividends, distribution or other proceeds from the Company.

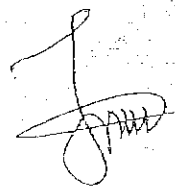
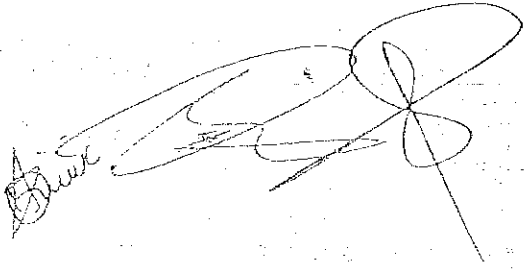
In Part VI, Clause 6.1 on acquisition of shares or assets, the GOU undertook to the company that neither it nor any relevant authority shall expropriate, compulsorily acquire, nationalize or otherwise compulsorily procure any ordinary share capital, the concession interest, assigned interests or other rights or material assets of the Company or the other rights and interests that are the subject of the Concession Agreement and the Power Purchase Agreement.

Part VIII, Clause 8.3 discusses how arbitration of disputes shall be conducted. In the event the Parties are unable to resolve any dispute pursuant to Clause 8.2, then the Parties agree as follows:

- The dispute shall be finally settled by arbitration before a tribunal conducted in accordance with the rules of the United Nations Commission and International Trade Law (UNCITRAL).
- Any arbitration shall be conducted in Uganda provided, however, that if the Company desires that arbitration be conducted outside Uganda, the arbitration shall be conducted in London, England, and the Company shall pay all costs of the arbitration as and when incurred by GOU.
- Notwithstanding the foregoing, if the matter of Dispute involves a sum of **US\$7million** or more, any arbitration of such dispute shall be conducted in London, England, and in such case, each party shall pay its own costs on arbitration as and when incurred.

Clause 8.5 states issues on sovereign immunity. It posits that Government of Uganda shall unconditionally and irrevocably:

- (i) agrees that should any proceedings be brought against it or its assets, other than its air craft, naval vessels, and other defense -related assets protected by diplomatic and consular privileges, no claim of immunity from such proceedings will be claimed by or on behalf of GOU or any of its assets that is now has or may in the future have in any such jurisdiction in connection with any such proceedings;
- (ii) It also waives any right of immunity which it or any of its assets now has or may in the future have in jurisdiction in connection with any such proceedings; and



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- (iii) It too consents generally to the jurisdiction of any court of competent jurisdiction for any action filed by the Company to enforce any award or decision of the Arbitration Tribunal appointed under this Agreement to resolve any dispute between the Parties.

Part IX Clause 9.1: Explains the main causes for early termination of the agreement by either the GOU or by the Company. Termination may be due to Company Event of Default or GOU Event of Default as detailed in the stated Clause. Termination will also occur due to a Political Force Majeure Event or at the Natural end of the Term.

GOU may initiate termination of the agreement in case of 'Company Event of Default' provided, however, that no such event shall be a Company Event of Default if it results from (i) a breach by GOU of this Agreement, (ii) a breach by UETCL of the Power Purchase Agreement, (iii) a breach by UEGCL of the Concession Agreement, or (iv) the occurrence of a Force-Majeure Event.

The Company can also initiate the termination of the agreement in case of a 'GOU Event of Default' provided, however, that no such event shall be GOU Event of Default if it results substantially from (i) a breach by the Company of the Privatisation Agreements, the Licences or Consents, or (ii) the occurrence of a Force Majeure Event.

Clause 9.3: Upon the expiration or earlier termination of this Agreement, the Parties shall have no further liabilities or obligations except for those that arose prior to or arise upon such expiration or termination and obligations that expressly survive such expiration or termination pursuant to this agreement; provided, however, that the rights and obligations set out in Clause 4.4 with respect to conversion into Foreign Currency and repatriation

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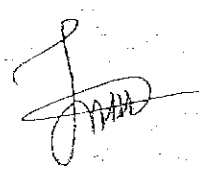
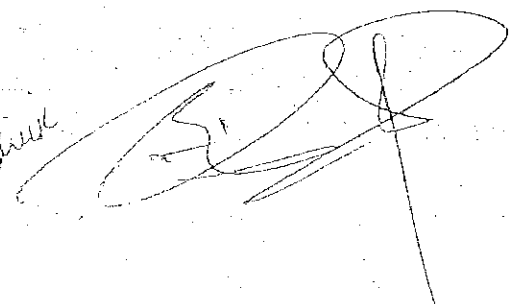
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and Part IV shall survive any termination or expiration of this Agreement until funds payable by UETCL under the Power Purchase Agreement, if any, are received by the Company, and the Company has been afforded a reasonable opportunity to convert and repatriate the Buy Out Amount.

Part XI, Clause 11.1, documents the Buy Out Amount provisions upon termination of the Agreement. Upon termination of the Agreement by either Party, Government of Uganda will pay the Company in immediately available funds within 270 (two hundred seventy) days from the date of termination of this Agreement the applicable amount (the 'Buy Out Amount') specified below:

- (a) In case Eskom Uganda Limited defaults, the Buy Out Amount shall equal (i) the cost of the Modifications (i.e. any restoration, reinforcement, replacement, or upgrade of the Complex by the Company and all other capital investments made by the Company) that is undepreciated and unrecovered by the Company through the Capacity Payment as at the date of the termination of the Agreement, multiplied by (ii) a percentage equal to 80% from the Transfer Date through the 13th anniversary thereof, such percentage increasing 2% per annum (straight line) for each year thereafter to 94% in the year that is the 20th anniversary of the Transfer Date. *(Capacity Payment is the amount to be paid by UETCL to the Company per kWh of Net Electrical Output for any month).*
- (b) In the case GOU defaults, the Buy Out Amount shall equal (i) the cost of the Modifications that is undepreciated and unrecovered by the Company through the Capacity Payment as at the date of the termination of the Agreement, multiplied by (ii) a percentage equal to 120% from the Transfer Date through the 13th anniversary thereof, such percentage declining 2% per annum (straight line) for each year

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thereafter to 106% in the year that is the 20th anniversary of the Transfer Date.

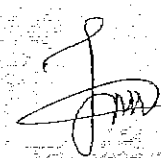
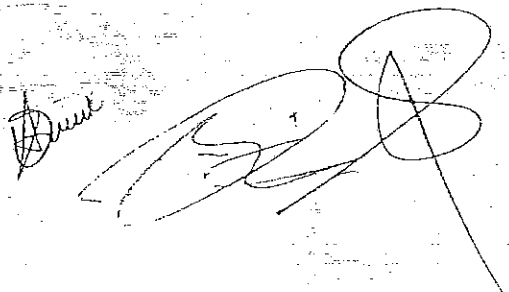
- (c) For natural termination of this Agreement, the Buy Out Amount shall equal 105% of the cost of the Modifications that is undepreciated and unrecovered by the Company through the Capacity Payment as of the date of such termination.

Clause 11.2 Upon early termination of this Agreement, GOU shall pay the appropriate Buy Out Amount in Dollars not earlier than 45 (forty five) days and not later than 270 (two hundred and seventy) days following the receipt of the Termination Notice. In case of natural termination of the Term, GOU shall pay the Buy Out Amount not later than 30 (thirty) days following the last day of the Term.

Unless the transfer of the Complex and payment of the Buy Out Amount is delayed by the Company, late payment of the Buy Out Amount shall bear interest at LIBOR plus five percent from the date that is 90 (ninety) days following the delivery of the Termination Notice until paid by GOU.

4.7.3 The Concession Assignment Agreement

In this agreement UEGCL granted to the Company and the Company accepted from UEGCL the Concession Interest and the right to sell and transfer the Available Capacity of the Complex and Net Electrical Output generated by the Complex to UETCL in accordance with the terms of the Power Purchase Agreement for 20 years with effect from 26th November, 2002. (*Net Electrical Output is the net electrical energy expressed in kWh delivered to the Interconnection Point and measured at the Output Meters by the Company when Dispatched by UETCL*).



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Some of the salient extracts from the Concession Agreement are:

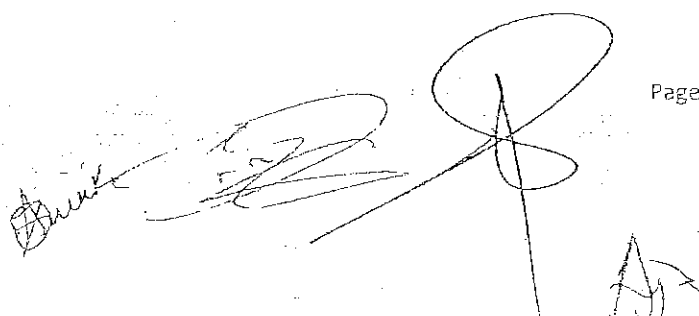
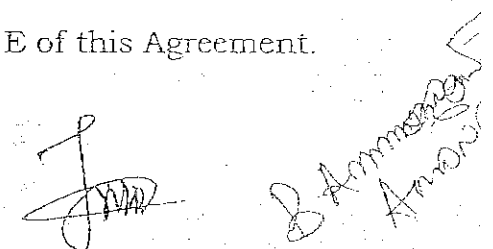
Article II, Clause (b) states that the occurrence of the Transfer Date is subject to the following conditions precedent:

- Establishment by UEGCL of the Escrow Account.
- Receipt by the company of Specified Consents that are required to execute activities under the Privatization Agreements.
- Evidence provided by the Company to UETCL that the Company has adequate funds available to make all payments required for Restoration and Reinforcement, and for working capital requirements of the Company and the operation and maintenance of the Complex.
- Delivery by UEGCL of the following: (i) the Records; (ii) the lists of employees, fixed assets, site and complex, leased assets etc. and (iii) a deed duly executed unconditionally releasing Business Assets and consenting to their transfer pursuant to this Agreement.

Clause 2.1 (e): The Company shall restore and reinforce the Complex in accordance with the requirements of and within the schedule in the Restoration and Reinforcement Plan to this Agreement.

Clause 2.3 (d): By no later than 30 days prior to the Transfer Date, UEGCL shall deliver to the Company an updated stock inventory in addition to the stock inventory dated 20 November 2002 and evidenced in the Disclosure Letter in Annex F hereto.

Clause 2.4: The amount of the Concession Fee payable each month by the Company to UEGCL in consideration for the grant and assignment by UEGCL to the Company of the Concession Interest, Assigned Interests and Other Rights shall be determined in accordance with Annex E of this Agreement.

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Clause 2.8 (a): After the Transfer Date, the Company, at its sole expense, shall have the right and obligation to make all Modifications necessary to cause the Complex to remain in compliance with all requirements of the Laws of Uganda and the Licence.

Clause 2.8 (d) requires the Company furnish to UEGCL a monthly report stating that the total cost of all Modifications to the Complex and describing separately and in reasonable detail each Modification with a cost in excess of US\$5,000 in the aggregate.

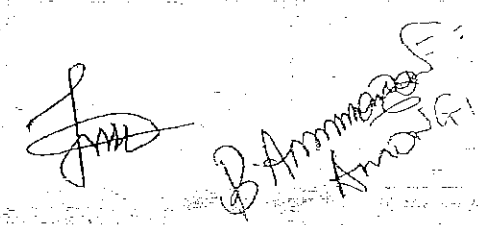
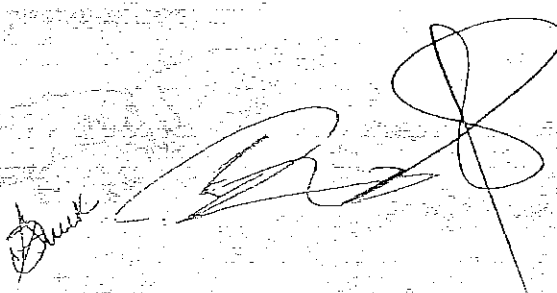
Part III of the Concession and Assignment Agreement sets out the terms of termination. UEDCL can initiate termination of the Agreement in case of Company Event of Default. The Company, likewise, can initiate termination in case of UEGCL Event of Default as spelt out in the Agreement.

Clause 3.1 (b) of the agreement provides that if the term of the Power Purchase Agreement is extended, the Term of this agreement shall also be extended for a period equal to the period of extension of the Power Purchase Agreement. And if the Power Purchase Agreement is terminated, this Agreement shall terminate simultaneously with the Power Purchase Agreement.

Clause 3.2: 'Company Events of Default' - stipulates the Company's Events of default which UEGCL may apply to terminate the Concession Agreement.

Clause 3.3: 'UEGCL Events of Default' - stipulates UEDCL's events of default which the Company may apply to terminate the Concession Agreement.

4.7.4 Power Purchase Agreement



This is an agreement in which Eskom Uganda Limited is to make available to UETCL the Available Capacity and the Net Electrical Output of the Complex to the extent that it is Dispatched, and shall provide to UETCL the Ancillary Services. And subject to and in accordance with the terms of this agreement, the Company shall declare to UETCL for each hour of the following day the Available Capacity, expressed in kilowatts per hour, capable of Dispatch by UETCL. UETCL shall accept all the Net Electrical Output, as well as any energy produced during testing.

Part VI Clause 6.1, (a) states the Term of this Agreement which commenced upon the Effective Date and unless extended or terminated earlier in accordance with the provisions of this Agreement, shall continue to be in force and effect until the 20th anniversary of the Transfer Date.

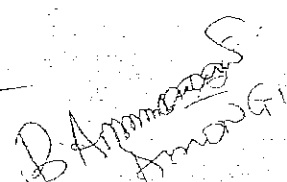
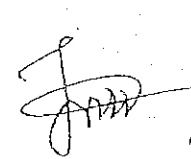
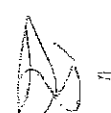
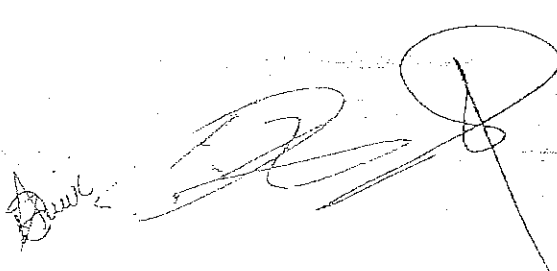
(b) If a Political Force MAJEURE Event reduces the output of Available Capacity by more than 50%, the Term of the Agreement will be extended for the period equal to such a period during which the Available Capacity was so reduced.

Clause 6.2 details the Company Events of Default that can lead to UETCL initiate the termination of this Agreement.

Clause 6.3 details UETCL Events of Default that can make the Company initiate the termination of this Agreement.

4.7.5 Escrow Agreement

Part V Clause 5.1 of the Concession and Assignment Agreement requires the Parties to enter into the Escrow Agreement with an Escrow Agent selected by the Parties, which agent shall establish and maintain the Escrow Account, to be held at a bank designated under the Escrow Agreement in trust for the



benefit of GOU and the Company. The Escrow Agent shall have the sole right of withdrawal with respect to the Escrow Account. Each of the Parties and the Escrow Agent intend that no creditor of UEGCL, the Company, or the Escrow Agent shall have any interest in the amounts on deposit in the Escrow Account.

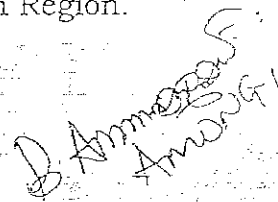
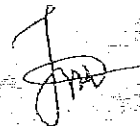
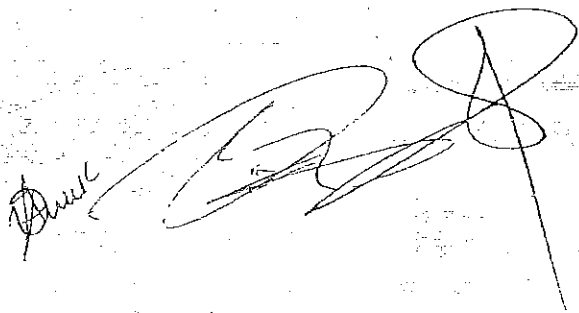
Clause 5.2 (a) states that after the Transfer Date and throughout the Term, the Company shall deposit all Concession Fees in the Escrow Account, net of the Administration Fee Component of the Concession Fee. In section (b) of this Clause, if during any month the Company fails to receive an amount due and payable to the Company under the Power Purchase Agreement due to (i) UETCL's failure to pay any monthly Capacity Payment to the Company by the due date for such a month, or (ii) due to a Political Force Majeure Event, then upon notice to UEGCL, the Company may reduce the payment of the Concession Fee for each month in which there is a payment shortfall.

4.7.6 Generation and Sales Licence

The Generation and Sales Licence was supposed to be issued by ERA to Eskom Uganda Limited. The Generation and Sales Licence enables the Company to perform the activities of electricity generation and sale of electricity to UETCL subject to the Licence conditions. The Licence is to continue in effect for a period of 20 years from November 26th 2002 as defined in the Licence Conditions.

4.7.7 Findings

- i. The leasing of Kiira and Nalubaale Hydropower generation plants to Eskom (U) was misconceived. It was irregular for Government to concession the two power plants yet they are reported to have been operating at the highest efficiency levels in the East African Region.



ii. Despite the reported level of investment by Eskom (U) Ltd in the Kiira-Nalubaale Hydropower plants, the generation capacity of the two plants has continued to deteriorate. At the time of takeover by Eskom Uganda Limited in 2002, the two plants were generating 280MW but since then the generation capacity has significantly reduced to 140 MW.

iii. The Committee established that world over, the management of hydropower plants/ generation is either under direct Government control or under a Public Private Partnership (PPP) arrangement, with Government still retaining majority shareholding. It is therefore ironical as to how GoU chose to abdicate its sovereign responsibility to a foreign state-owned but locally registered private company.

iv. While Government continues to pay Eskom Uganda Limited huge sums of money for the operation and maintenance of the two plants, at the same time, GoU incurs huge financial expenses by way of funding the operations/programs of a statutory body called UEGCL. Both institutions (ESKOM and UEGCL) which carry out similar functions/activities are funded by Government. While appearing before the Committee, the UEGCL officials confirmed that given the opportunity, they would run and manage the generation of power more efficiently, an argument seen as meriting to the Committee. The double funding (notably the exorbitant wage bill) of these companies has continued to adversely impact on the end user tariff.

v. It was established that Eskom Uganda Limited runs an electricity sub-station illegally at Jinja. This is contrary to Section 53 of the Electricity

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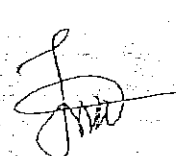
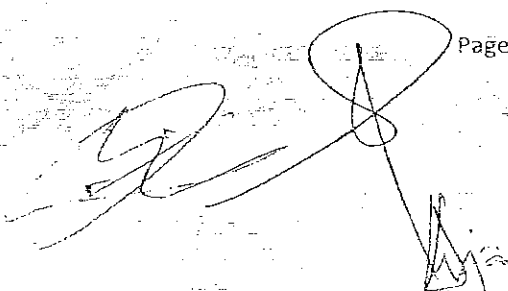
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Act, which prohibits any person from constructing, owning and operating an installation for transmission of electricity without a transmission license. Additionally, the same company participating in generation and transmission gives rise to conflict of interest and role play.

The Committee accordingly recommends the immediate termination of the Eskom Power Generation Concession on the following grounds:

- i) *Despite the reported level of investment by Eskom (U) Ltd in the Kiira-Nalubaale Hydropower plants, the generation capacity of the two plants has continued to deteriorate. At the time of takeover by Eskom Uganda Limited in 2002, the two plants were generating 280MW but since then the generation capacity has significantly reduced to 140MW.*
- ii) *The Committee established that world over, the management of hydropower plants/ generation is either under direct Government control or under a Public Private Partnership (PPP) arrangement, with Government still retaining majority shareholding. It is therefore inconceivable how GoU chose to abdicate its sovereign responsibility to a foreign state-owned but locally registered private company.*
- iii) *While Government continues to pay Eskom Uganda Limited huge sums of money for the operation and maintenance of the two plants, at the same time, GoU incurs huge financial expenses by way of funding the*

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operations/programs of a statutory body called UEGCL. The Ugandan taxpayer cannot afford to continue paying colossal sums of money to the two institutions (ESKOM and UEGCL) which carry out similar functions/activities. It is not sustainable.

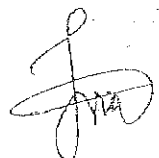
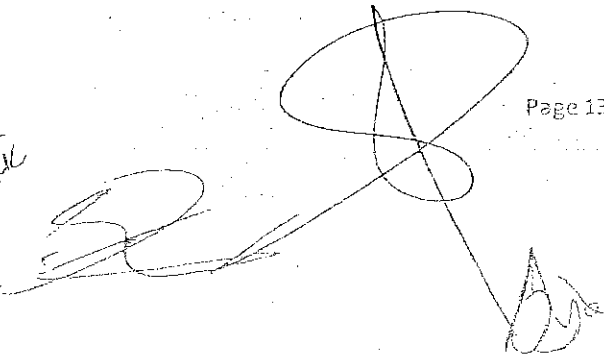
- iv) The double funding (notably the exorbitant wage bill) of Eskom (U) Ltd (a South African Government company) and UEGCL (a Uganda Government Company) is an avoidable expense which adversely impacts on the end-user tariff.

It is the Committee's strong conviction that UEGCL has the technical expertise run and manage the generation of power more efficiently. The generation component should revert to government control as it is the practice world over. UEGCL and UETCL should be merged into one Company in order to eliminate the double costs of funding of these companies by Government.

4.3 POWER PURCHASE AGREEMENTS BETWEEN GoU AND THERMAL POWER SUPPLIERS

Following the reported drop in the water levels of Lake Victoria due to prolonged drought in 2005/06 and the resultant reduction in hydropower generation capacity of the country, Government was compelled to enter into agreement with private power producers (Aggreko, Jacobsen and Electromaxx) to supply emergency power.

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Government signed Power purchase agreements (PPA) and issued licenses to Aggreko, Jacobsen and Electromaxx. The Committee reviewed these documents to find out whether they are fair or not to both parties and the extent to which their provisions have been complied with.

The Committee established that whereas these thermal plants were contracted to provide emergency power generation in Uganda (as a stop gap measure), their contracts/ licenses have been regularly extended; which is an indication of poor planning on the part of Government generally and the regulator (ERA) in particular. The first two Aggreko licenses which were of three year terms were extended for more than three years each. If the licences had initially been for a duration of six years, the tariff would have been much lower.

These thermal power agreements do not clearly spell out the targets /objectives to be achieved, for whom the project is designed, the time frame it is envisaged to take, among others.

The continuous extension of these thermal power contracts (which were meant to have a short time span) without changing but maintaining the same terms and conditions has had grave implications on the tariff and the Government subsidy profile. In effect, Government has for long been trapped in thermal power projects with abnormally high tariff profile and huge subsidy requirements.

A lack of integrated resources planning has given rise to the implementation of these thermal power projects in emergency situations, which unfortunately has further complicated the power sector. These

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emergency power solutions have become base load power plants at an abnormal huge cost to the country.

During its visit to Kenya and Ghana, the Committee found out that thermal power generation continues to constitute a significant component of the generation mix and power supply in these countries, and plays a big role in supplementing hydropower and other sources of power especially during emergencies. However, the contracts signed with thermal power generating companies are long term but not for a short time span like in Uganda's case. This arrangement therefore helps in ensuring that the end-user tariff is favourable.

4.8.1 Other Findings about Thermal Power Generation

i. Illegal raising of the fuel consumption of Aggreko Kiira

The Committee found out that in 2009 Mr. Kwesigabo Johnson Secretary to the ERA Board, who was then Acting CEO, in concert with Eng. Kiyemba Elias, Managing Director UETCL arbitrarily amended the terms of the license to Aggreko Kiira by raising the fuel consumption rates of this power plant from 0.262 litres per kilowatt hour to 0.277 litres per kilowatt hour.

According to the Auditor General's report on the Financial Statements of ERA for the year ended 30th June 2011, the fuel consumption rates of Aggreko thermal plants both Mutundwe and Kiira were 0.262 litres per kilowatt hour. Mr. Kwesigabo Johnson (Ag. CEO then) did not seek the approval of ERA Board before issuing out the said letter. This action resulted into a loss of US\$4,078,329 to Government.

ii. Fuel consumption for Jacobsen Thermal Power plant

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According to Auditor General Report on Financial Statements of ERA for the year ended June 2011, Jacobsen thermal plant in Namanve uses CSt 380 Heavy Fuel Oil (HFO) to generate power instead of CSt 180 HFO. The Committee for the Interim review of Electricity Tariff (2009) also extensively analysed the same matter and decried the discrepancy in the fuel consumption rates which are way above those warranted by the manufacturer in the Jacobsen power purchase agreement.

Jacobsen thermal plant continues to use the cheaper, but poor-quality CSt 380 HFO to generate power while billing Government for the more expensive and good quality CSt 180HFO. As a result of this, the Company makes a margin of US\$25-30 per ton, leading to a loss of approximately Shs. 480,000,000 per month. While all this has happened over the years ERA has not made any effort to stop it and recover any funds unfairly claimed by the Company.

It is imperative to note that continued use of the cheaper CSt 380HFO, which is of poor quality will significantly compromise the lifespan of generators at the Jacobsen. On the contrary, the use of CSt 180HFO guarantees the longevity of generators.

iii. Suffice to note, the Jacobsen thermal plant at Namanve was procured under the Build Own Operate and Transfer arrangement for a period of six (6) years. During the investigation, the power plant underwent major repairs and overhaul of some machines barely three years after they were installed. The Committee was therefore concerned as to what will be the mechanical status of these generators at the end of the 6year BOOT period! The level of repairs also negatively impacts on electricity tariffs because of additional costs of maintenance.

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iv. Fuel Handling Charge/Fee

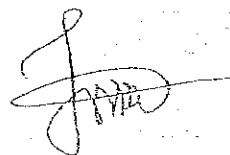
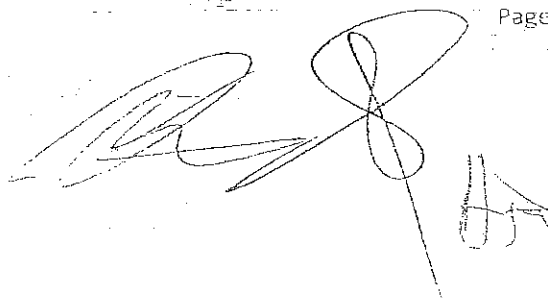
The Committee established that one of the specific incentives Government of Uganda extended to all thermal power plants was diesel tax exemptions. Despite this incentive that applied to all HFO thermal power plants, the Committee was concerned to find out that Jacobsen was given a special consideration handling fee of 5% of fuel supply costs. The special facility of 5% fuel handling fee given to Jacobsen further enhanced the profit margin of this company which translates to US\$3million (UGX 7billion) per annum. This is based on taxation rate on diesel which is approximately UGX 580 per litre.

If the fuel handling fee for Jacobsen was a fixed sum of approximately US\$4/Mwh as is the case with the other HFO plants Government would be saving US\$1460,000= per month.

The Committee Recommends that:

- i) *Eng. Elias Kiyemba, MD UETCL should immediately be interdicted for his role in illegally raising the fuel consumption of Aggreko Kiira, which is an act of gross misconduct that tantamounts to abuse of office and subsequently causing financial loss to Government.*
- ii) *The Inspector General of Government and the DDP take up the matter of illegal increase of fuel consumption for Aggreko Kiira with the view of possible prosecution of Mr. Kwesigabo Johnson, former Counsel/Secretary ERA and Eng. Elias Kiyemba, MD UETCL for abuse of office and causing financial loss to Government.*
- iii) *Government should recover all the monies that Jacobsen Elektro AS has fraudulently claimed for using CSt 380HFO to generate power.*

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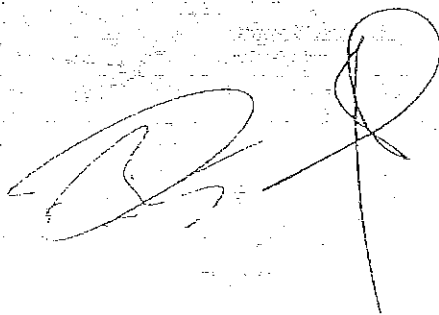


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iv) The high fuel consumption of generators resulting from poor operation and maintenance of the equipment should not be rewarded in the tariff.

v) Government should immediately scrap the fuel handling charge/fee given to Jacobsen Thermal generation Company.

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CHAPTER FIVE

REVIEW OF THE SALIM SALEH REPORT ON ELECTRICITY TARIFF REDUCTION

5.1 Introduction

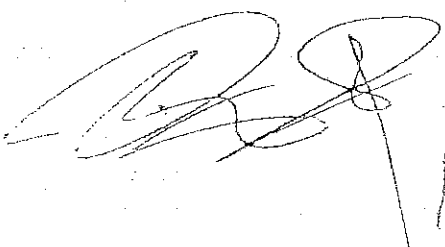
This chapter highlights the key recommendations of the Committee on the Interim Review of Electricity Tariff, which is also often referred to as the General (Rtd) Salim Saleh Committee 'Report on Electricity Tariff Reduction, 2009.' The key objective is to find out the extent to which these recommendations were implemented by Government Ministries, Departments, Agencies as well as Private Companies engaged in the electricity sub-sector in Uganda.

5.2 Objective of Interim Review of Electricity Tariff

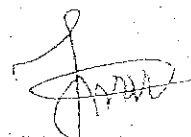
Taking cognizance of the problems and challenges in the electricity sector, and in a bid to find a sustainable solution to the increased Government subsidies to the electricity sector amidst the high tariffs and energy losses, the then Minister of Energy and Mineral Development instituted an inquest into the sector in 2009. The 'Interim Review of Electricity Tariff' Committee appointed by the Hon. Minister had the following as its Members:-

1. (Rtd) General Caleb K. Akandwanaho SalimSaleh Oriba (PSC) – Chairman
2. Mr. Muyanja Mbabaali – Vice Chairperson
3. Mr. Perez Bukumunhe (FCIB) – Chairperson Technical
4. Dr. Muhammad Serunjogi – Secretary
5. Hon. Jacob Oulanya (Now the Rt. Hon. Deputy Speaker of the Parliament of Uganda) – Counsel

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6. Mr. Robert Segonja – Member (Consumer's Representative).

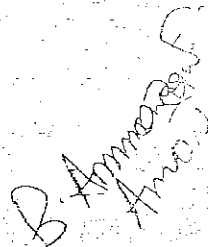
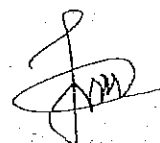
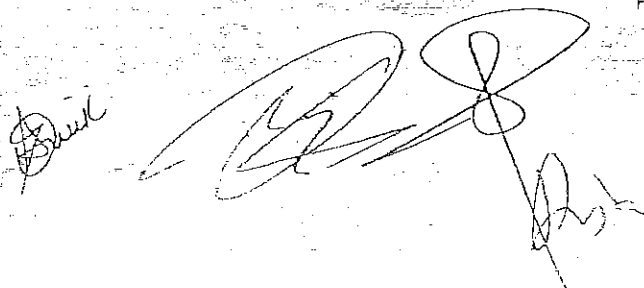
The Terms of Reference for the Committee for Interim Review of Electricity Tariff were as follows:-

- i. Review all power contracts and identify the prudence of each of the costs allowed to be recovered in the tariff as well as those financed by government through subsidies.
- ii. Assess how much fuel is being used by each of the thermal plants vis-à-vis what they claim through the tariff.
- iii. Propose which of the costs should be disallowed and indicate the impact on the tariff.
- iv. Provide information on the investment made by UMEME Ltd since takeover from UEDCL and the financing of these investments.
- v. Indicate the levels of profitability for each of the companies.
- vi. Provide concrete proposals on how the tariffs can be reduced.

Whereas Committee for Interim Review of Electricity Tariff was constituted by the then Minister of Energy and Mineral Development, Hon. Hillary Onek and efforts were later made to have its report considered by Cabinet, the Minister of Energy realized that since this was a tariff matter and therefore, according to section 10 of the Electricity Act 1999, a matter under the purview of the sector regulator (ERA). Thus, Hon. Hillary Onek accordingly sent the report to the ERA Board for scrutiny and eventual implementation.

5.3 Key Recommendations in the Report

In its report titled 'Report on Electricity Tariff Reduction, 2009', the Gen. Saleh Committee for Interim Review of Electricity Tariff recommended that:-



a) Government should commission forensic investigations to:-

- i. Examine the UMEME Ltd Concession Agreements (negotiations and implementation).
- ii. Determine why Aggreko-Mutundwe thermal power plant (which is zero tariff rated) raised the Bulk Supply Tariff despite protests by ERA.
- iii. Examine the real baseline distribution system losses at the time of the hand over of the electricity distribution network from UEDCL and UMEME Ltd.
- iv. Ascertain the investment level as at September 2006 and the source of information for subsequently misrepresenting levels of investments. The effect of this anomaly and how they are treated in the UEDCL accounts.
- v. Determine rebates paid to UMEME Ltd.
- vi. Find out how power losses were determined since 2006.
- vii. Find out why the 'Prominent Persons' increased the system losses from the Ministerial capping of 33 percent to 38 percent in 2006.
- viii. Determine why despite the GOU/IDA loan of US\$ 11million channeled through UEDCL to procure system loss reduction materials to be

installed by UMEME Ltd, there has been no visible impact in the UMEME Ltd reported system losses.

- ix. Find out why the Company Escrow Account originally envisaged by the first concession agreement as a mechanism to track any new investment financing by UMEME Ltd and enable independent monitoring of any disbursement of funds by ERA from a bank point was closed. And why UMEME Ltd refused to reopen the account when requested by the Regulator.
- x. Establish income tax reported by UMEME Ltd over the years.
- xi. Establish return on investments for UMEME Ltd allowed in the tariff.
- xii. Establish the anomalies in the meters and metering system used by UMEME Ltd.
- xiii. Ascertain the Fuel Logistics Costs (FLOC) and Diesel Consumed by Aggreko.
- xiv. Establish the negotiation, implementation and performance of the Jacobsen thermal power plant.
- xv. Establish why the licensing process of the Buyoge Tronder Energy Project was handled differently from that of other licences.

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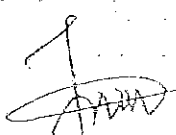
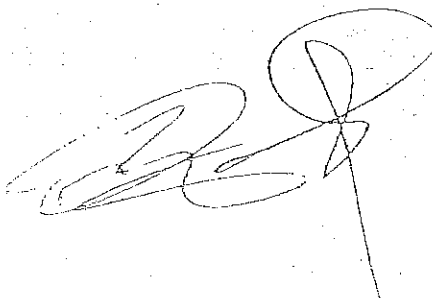
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xvi. Find out the relationship between M/S Globeq, Eskom Enterprises and Actis Infrastructure 2LP at the time of negotiating the concession with a view to ascertain whether there was insider trading at the time of unbundling of UEB, making of Lease and Assignment Agreements and presentation of wrong data to be used as the basis for agreements or subsequent amendments.

b) Other policy recommendations in the report also covered the following areas:-

- i. Reviewing the UMEME Ltd Concession Agreements.
- ii. Power Generation mix.
- iii. Transmission and distribution infrastructure.
- iv. Elimination of all Diesel Based Thermal Generation.
- v. Licenses and Power Purchase Agreements for Heavy Fuel Oils (HFO) thermal generation plants.
- vi. Rationalize and merge the UEB successor companies under the line Ministry of Energy and Mineral Development (MEMD) to avoid a repetition of the political oversight.
- vii. Remove the monopoly in the electricity distribution segment and create billing and collecting franchises similar to the ones in mobile phone companies with super dealers and sub-dealers for gazette areas.
- viii. Undertake a comprehensive electricity demand analysis in the country so that generation and distribution planning can be firmed up.
- ix. Rollout unconditionally prepaid meters throughout the country to address billing and working capital requirements which impact on the tariff.
- x. Ring fence customer deposits (estimated at over UGX 28 billion at the time of the report) through the use of an Escrow Account in trust

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control by ERA to prevent the possibility of these monies being accounted for as investment for which a return on investment will be embedded in the tariff.

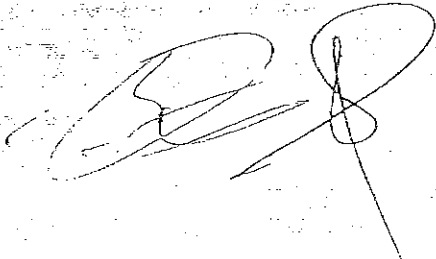
- xi. Reduce the long period of processing licenses for potential investors in the sector.
- xii. There should be no overlaps in the investments of the successor companies – generation, transmission and distribution.
- xiii. Strengthen the independence and autonomy of ERA.
- xiv. Engage UMEME LTD. on further tariff reduction proposals.
- xv. Encourage various forms of co-generation arrangements.

5.4 Findings on the extent of implementation of the Saleh Report

The Adhoc Committee Energy found out that despite the critical findings and recommendations of the Saleh Committee as contained in its report entitled the Report on Electricity Tariff Reduction(2009), no forensic investigations were instituted by the relevant Government institutions to examine the various pertinent issues arising from that report. Among others, the Adhoc Committee established the following:

- i. No forensic audit was carried out to ascertain the actual level of investment by UMEME Ltd. Limited on the power distribution network. There was also no audit on the return on investment recouped by UMEME Ltd. Limited through the tariff.
- ii. No investigation was done to verify whether the faulty meters that were imported and installed by UMEME Ltd were retrieved from the consumers.
- iii. No renegotiation of the power distribution agreements signed between GOU and UMEME Ltd was done. The renegotiation was

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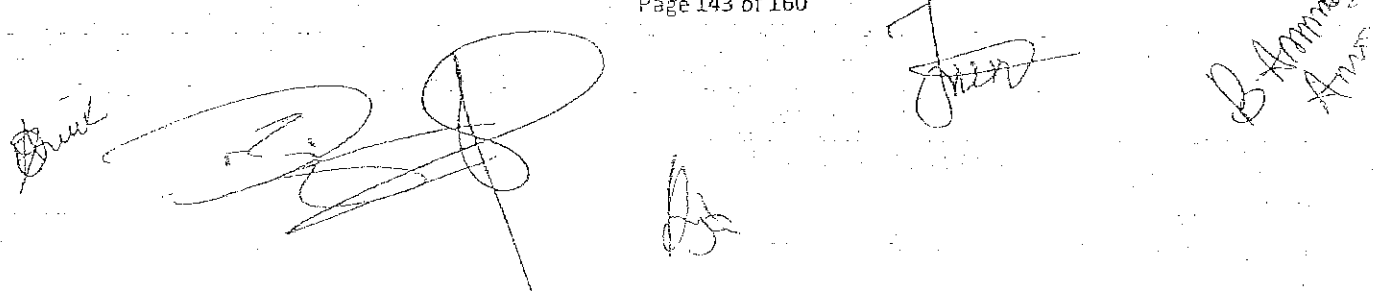
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meant to adjust the lopsided nature of the agreements that favoured the Concessionaire at the expense of Ugandans.

- iv. No review of agreements signed between the thermal power generators and GOU was done in order to ascertain whether the Companies conform to what is stipulated in the agreements.
- v. There were no attempts made towards the reduction of tariffs as was envisaged and recommended in the report.
- vi. No investigation was instituted against the committee of 'Prominent Persons' to ascertain why and where they obtained the mandate to increase the system losses from the Ministerial capping of 33% to 38%.
- vii. No audit of income tax payments reported by UMEME Ltd over the years has been done.
- viii. No comprehensive electricity demand analysis in the country has been carried out to aid in planning the future energy needs.
- ix. No attempts to remove the monopoly in the electricity distribution segment and create billing and collecting franchises similar to the ones in mobile phone companies were made.
- x. UMEME Ltd has not rolled out pre-paid meters throughout the country as was recommended in the report.

5.5 Conclusion

From a review of the (Rtd) General Salim Saleh Report on Electricity Tariff Reduction, 2009' and the issues raised by the Adhoc Committee with the officials of various relevant Government institutions, it can be concluded that no deliberate action was instituted to see to it that the recommendations in that report are implemented. No institution took the lead to get the recommendations implemented

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save for the basic implementation of selected recommendations by ERA. Consequently, the intended benefits would have accrued from the implementation of the said recommendations have not been realised.

5.6 The Committee recommends that:

- i. Since the regulator (ERA) formally accepted and owned up the report of the Committee on the Interim Review of Electricity Tariff, it is prudent that ERA and the sector Ministry should take the lead to pick out and implement some of the recommendations therein that could still be relevant in a bid sustainable solutions to issues like high tariffs, energy losses etc.
- ii. UEDCL and ERA should to ensure that all UMEME investments are verified as per the report's recommendation.
- iii. The Attorney General together with Ministry of Energy and Mineral Development and ERA institute a review of the Concession Agreements signed with UMEME Ltd. The Attorney General should take a lead in all the future reviews and amendments to such agreements when required.

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CHAPTER SIX

REVIEW OF OPEN TENDER SYSTEM WITH RESPECT TO ITS BEARING ON POWER GENERATION COST

6.1 Introduction

This chapter starts with defining the Open Tender System (OTS). It clearly explains how it is used in transacting oil products in Kenya. It examined how the OTS is used in procuring oil products for thermal generation in Uganda.

6.2 Open Tender System

For practical reasons the Refinery serves customers with a pool in which an individual user or customer wins a tender to deliver crude through the Open Tendering System form which after processing, all other customers draw product. Subsequent deliveries are also tendered through the OTS with the Refinery keeping account of crude oil delivered, crude oil stocks, products in stock and products drawn.

- i. Examine the open tendering system

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- ii. Terms and conditions of the agreements
- iii. Compare oils prices prior to and after the OTS
- iv. The impact of OTS on timeliness of delivery of oil product, cost and availability

6.3 OTS management and its bearing on production costs of Thermal Power

1. Uganda is a landlocked country and imports over 90% its petroleum products through Kenya as the route is shorter. Other imports of less than 10% pass through Tanzania. The monthly importation/consumption figures currently stand at a total of 112.5 million litres detailed as:

- 60 million litres of automotive gas oil (AGO/diesel), of which 18 million litres is for thermal power generation;
- 32 million litres of premium motor spirit (PMS/petrol);
- 12 million litres of aviation fuels/jet; and
- 8.5 million litres of bulk illuminating kerosene (paraffin).

2. The resultant monthly importation bill is US\$ 137,449,600 of which taxes and other (making and clearing) fees accounts for US\$24,040,000. There is zero tax on both Jet and Kerosene. The tax per litre on petrol and diesel is Ushs. 850 and Ushs. 530 respectively. This tax has remained unchanged for the last 5 years. The companies pay taxes at the border through Gross payment Accounts (GPA) they have with Uganda Revenue Authority (URA).

3. The major components of prices of petroleum products in Uganda are:

- i) Mombasa landed price, contributing 67.85% of pump price per litre;
- ii) Logistics from Mombasa to Eldoret, contributing 6.34%;
- iii) Transportation ex Eldoret, Taxes, Company and Dealer Margins, Clearing and Quality Assurance Fees, contributing a sum of 26.08%

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4 The critical challenge in the region lies in adequate importation, storage, transportation and distribution infrastructure to cope with the rising demand. To alleviate on this challenge that contributes to sporadic supply shortages in the region, there has been need to address congestion in Mombassa. The congestion is mainly caused by unscheduled deliveries.

5 To address this issue, the major measure taken was to organise the oil marketing companies (OMCs) to use the open tender system (OTS) for import. The measure is based on the experience on Kenya. The OTS works in such a way the companies bid for bulk supply of products for specific month. The tenders are normally split into two and per product. The company with the lowest bid price wins the tender. The Uganda OTS works hand-in-hand with that of Kenya and there is no tax on this system. In addition, fuel supply for thermal power plants does not form part of the OTS as it is procured separately and is accorded priority in the Kenya Pipeline System.

6 One of the challenges identified was inadequate storage space in the pipeline system that is mainly attributed to (i) increase in demand and (ii) slow evacuation of products from the system by some middlemen who extend bond periods. To address this problem, it was among others agreed that Kenya allocates dedicated storage space to Uganda-bound products based on transit share (which is above 72%). The allocated space per month is 41.5 million litres of diesel, 30 million litres of petrol, 12 million litres of jet and 8.5 million of kerosene. This is in addition to dedicated monthly storage space of 18 million litres for diesel supply to Aggreko IPP by shell (U) Ltd for thermal generation.

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7 The allocated monthly space is utilised by Ugandan companies through their sister companies in Kenya (as companies registered in Kenya and contributed to line fill are the only ones authorised to import in to the Kenya pipeline system). The allocation is based on weighed average share of import (70%) and retail network (30%) figures that Uganda avails Kenya. The OTS started in April 2011 with some anomaly in which some companies that had not been forwarded to Kenya found their way on the list. However, the matter has since been addressed by the Kenyan Authorities.

8 From the foregoing, therefore, the OTS does not affect fuel supplies for thermal power generation and hence has no bearing on production costs for thermal power.

9 Otherwise, the supplies to the country are at the moment normal with 9 days of stock for diesel and 12 days stock for petrol. This has been made possible with enforcement of the requirement for the oil marketing companies to keep 10 days' operational stocks.

CHAPTER SEVEN

WAY FORWARD

(A) Salient issues worth noting

From the foregoing, it is evidently clear that the restructuring and reform process in Uganda's Electricity sub-sector was mismanaged despite the well intentioned objectives. The PERD Statute which was meant to provide a legal framework for the privatization of the sector did not empower the sector institutions to make crucial decisions especially in circumstances where their technical expertise was critically needed. Consequently, some ill-intentioned technocrats and political leaders in the Ministry of Finance and the privatization Unit manipulated the process for selfish ends. To-date, the Ministry of Finance and the Privatisation Unit continue to exert its hegemony over the UEB Successor companies as evidenced by the 100% shareholding, and appointment of Board and management of UETCL, UEGCL and UETCL.

More than ten years after the reforms in the power sector were carried out, the generation capacity/output at the main Kiira-Nalubaale hydropower dropped from a high 270MW (when Eskom took over) to a low generation output of 140MW, while the power distribution segment is still characterized by dilapidated infrastructure in most areas (despite a claim by UMEME Ltd to have invested \$130million in the network), high energy losses, high tariffs, high levels of government subsidies (until Feb 2012), poor quality of supply and energy utilization inefficiencies.

The inherently poor performance of the power generation and distribution segments of Uganda's electricity sector is attributable to mismanagement of the reform process by PU-MFPED, the inefficiency of ERA, the ineffectiveness of UEDCL and the failure by both Eskom and UMEME Ltd to manage those assets as was intended. For the

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electricity sector to succeed it is mandatory to have a technically astute and experienced regulator, asset owner and asset manager.

There is urgent need for well thought out reforms with the focus on addressing the inherent legal, institutional and policy deficiencies such as streamlining political supervision of the sector, enhancing the technical competence of the Regulator and engage the private sector players on terms and conditions that do not compromise national interests, among others. A Comprehensive National Energy Plan that addresses the critical short, medium and long term energy and development needs of the country needs to be put in place. This will ultimately make the industry more competitive with reduced energy losses and much more affordable electricity tariffs.

(A) The Umeme Power Distribution Concession

The Committee having satisfied itself with the manner in which the UEB was unbundled and having reviewed the resultant procurement and signing of the Umeme Power Distribution Concession agreements and the provisions of these agreements, it is hereby recommended that the Umeme Limited' power distribution concession be terminated. The recommendation is premised on the following grounds:

- (a) The Attorney General of the Republic of Uganda did not perform the Constitutional duty required of him under Article 119(2), specifically that of drawing and perusing all the agreements signed between GOU and Umeme Limited regarding the Power distribution concession. This Constitutional obligation was hijacked and therefore abused by the Privatization Unit who hired Transaction Advisors, who did not transact in the best interest of Government and the people of Uganda.

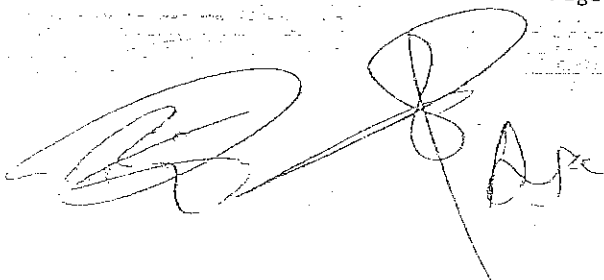
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- A signature labeled "B. Ammend" on the right.
- Other smaller initials and marks scattered at the bottom.

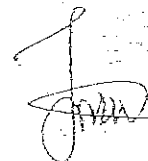
(b) **Lopsided Agreements:** It is the Committee's firm conviction that if the learned Attorney General had carried out his/her Constitutional duty as noted above there is no way he/-she could have committed Government and people of Uganda to such a raw deal. All the three Agreements signed between GOU and Umeme Ltd regarding the power distribution concession were skewed in favour of the company to the detriment of the Ugandan citizenry. The common denominator across these agreements are the scandalous provisions like the abnormal 'Buy Out Amounts', generous working capital allowances and compensation of Umeme Limited for making losses among others.

(c) **Exaggerated level of losses:** Even with the investments made by Government in the electricity sector before and after the UMEME concession, Umeme Ltd has for the last 7 years continued to post the highest level of energy losses (at 35-38%) until 2010 (following the Salim Saleh Inquiry), when they brought losses down to 28%. This level of losses still remains the highest in the region and far below acceptable industry levels.

(d) **Exaggerated Level of Investment:** The claim by Umeme Limited to have invested U\$130million in the network in the period 2005-2012 is unfounded. Such massive level of investment would have turned around the sector and resulted into distribution network efficiency, substantial reduction in losses and more new connections to the grid. Suffice to note; this exaggerated level of investment is aimed at upping Umeme's 'Buy Out Amount' in case of early or natural termination of the concession.

(e) Over seven years into the power distribution concession, Umeme Ltd and the regulator (ERA) have deliberately refused to put in place a **Restoration and Reinforcement Plan** (a requirement in the contract)

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to guide investments in the distribution network. This is a plan that would have clearly defined the critical areas of investment, the required resources, expected outputs and performance standards. Without it, UMEME continues to dictate where and how to invest. No wonder it invests in non-critical areas like peripherals, office furniture and fittings and recoups a return on such investments. As a country, we cannot allow this to continue.

(f) Generous working capital allowance/days lag

According to the Umeme contract with Government of Uganda, the Government is under obligation to pay Umeme Ltd such amount of monies equivalent to the uncollected Umeme bills from power consumers after 40 days. The committee finds this arrangement unprecedented in the business or commercial world since nowhere in the world can a company/individual can be paid for their inefficiencies. What other incentive did Umeme have to reduce the energy losses and even improve its collection rate!! Indeed this was a well orchestrated scheme to benefit Umeme and the bureaucrats in the Ministries of Energy and Finance who crafted this contract!

It is imperative that Government immediately initiates the termination arrangement since it is evident from on the onset that further significant costs will be incurred with the continuation of current power distribution concession agreements. Government should therefore consider sourcing for other companies with the capacity and technical capability to manage the power distribution business after Umeme Limited's concession has been terminated. Preference should be given to local companies with the experience, capacity and expertise to take over the management of the electricity distribution business in the country.

Further to the above, the Committee also recommends the following in respect of the Umeme Power Distribution Concession:

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- i) All transactions on the Escrow Account must stop immediately until an audit into its management has been carried out.
- ii) The Auditor General carries out a forensic to ascertain the level of investment made by Umeme in the network since 2005. The Auditor General also carries out a forensic audit to ascertain the actual amount paid to UMEME Ltd in form of customer deposits since 2004.
- iii) The Inspector General of Government and the Auditor General interest themselves into the management of the Escrow Account with the view of unearthing any possible abuse. Particular interest should be taken in respect of possible double budgeting specifically by UPDF, Uganda Police, Uganda Prisons and UBC.
- iv) The generous capital allowances that Government has been paying Umeme Ltd must be scrapped, and neither should they be extended to any other future power distribution company.
- v) ERA should ensure that the power distribution loss targets in the next five years be put at 18% which is the acceptable industry level.
- vi) There must be a clear split between technical and commercial losses.
- vii) Government through the Regulator should put in place clear key power sector performance indicators and standards.
- viii) The generous capital allowances that Government has been paying Umeme Ltd must immediately be

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scrapped, and neither should they be extended to any other future power distribution company.

ix) Mr. David Ssebabi, in his capacity as Director Privatization Unit, head of Technical Committee and leader of the Government of Uganda negotiation team hijacked the Constitutional mandate of the Attorney General by recruiting transaction advisors - Hutton and Williamson on whose purported legal and expertise he based to entrench the unfavorable provisions in the Umeme contract. The committee therefore finds him culpable of consciously misguiding and committing Government and the people of Uganda to a bad contract with Umeme. This, without doubt, was a well-orchestrated ploy to fleece the citizenry.

x) Accordingly, Mr. David Ssebabi, Director Privatization Unit as head of GOU Umeme Concession Negotiation Team should be relieved of his duties and be prosecuted for abuse of office, causing financial loss and colluding with CDC Globeq and Eskom Enterprises through Umeme Limited to defraud Government and the people of Uganda.

xi) Members of the Divestiture and Reform Implementation Committee should also be held culpable for abuse of office by approving the execution of bad agreements with Umeme Ltd and for conveniently keeping the Attorney General out of the drafting and perusal of these agreements well knowing that this is a Constitutional duty that cannot be delegated. The members in question

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are Hon. Gerald Sendawula former Minister of Finance, Planning and Economic Development, Hon. Syda Bumba, Former Minister of Energy.

(C) The ESKOM Power Generation Concession

The concessioning of the Kiira and Nalubaale Hydropower generation plants to Eskom (U) was misconceived. It was irregular for Government to concession the two power plants yet they were reported to have been operating at the highest efficiency levels in the East African Region. The committee accordingly recommends the immediate termination of the Eskom Power Generation Concession on the following grounds:

- v) *Despite the reported level of investment by Eskom (U) Ltd in the Kiira-Nalubaale Hydropower plants, the generation capacity of the two plants has continued to deteriorate. At the time of takeover by Eskom Uganda Limited in 2002, the two plants were generating 280MW but since then the generation capacity has significantly reduced to 140MW.*
- vi) *The Committee established that world over, the management of hydropower plants/ generation is either under direct Government control or under a Public Private Partnership (PPP) arrangement, with Government still retaining majority shareholding. It is therefore inconceivable how GoU chose to abdicate its sovereign responsibility to a foreign state-owned but locally registered private company.*

vii) While Government continues to pay Eskom Uganda Limited huge sums of money for the operation and maintenance of the two plants, at the same time, GoU incurs huge financial expenses by way of funding the operations/programs of a statutory body called UEGCL. The Ugandan taxpayer cannot afford to continue paying colossal sums of money to the two institutions (ESKOM and UEGCL) which carry out similar functions/activities, it is not sustainable.

viii) The double funding (notably the exorbitant wage bill) of Eskom (U) Ltd (a South African Government company) and UEGCL (a Uganda Government Company) is an avoidable expense which adversely impacts on the end-user tariff.

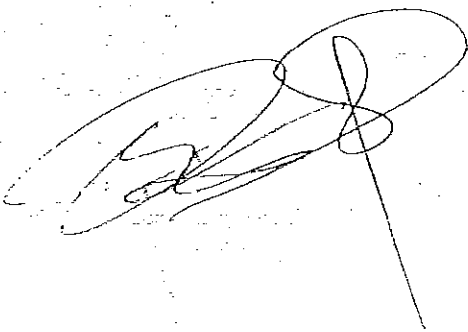
It is the Committee's strong conviction that UEGCL has the technical expertise run and manage the generation of power more efficiently.

In view of the aforementioned, it is imperative that Government immediately initiates the termination arrangement since it is also evident that further unnecessary costs will to be incurred with the continuation of Eskom power generation concession.

Other Recommendations

1. The Committee recommends that once the Umeme power distribution concession is terminated, the power distribution segment should be managed under a Public-Private Partnership framework with Government having atleast a 51% shareholding.
2. Government should prioritize further exploration and development of a wide range of available energy resources in the country. These

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much desired investments (normally requiring significant return) this is a smarter and more sustainable way of subsidising the sector.

8. The electricity distribution segment should be opened up to other players in order to remove the monopoly by one company, which was one of the key objectives of the power sector reform process. This will ultimately bring about competition and the resultant efficiency in service delivery and lowering of end-user tariffs.
9. The relevance and significance of an independent Electricity Regulatory Authority should be enhanced through institutional and legal framework. The Board of ERA should therefore be reviewed by the Minister of Energy and Mineral Development to ensure that the desired skills mix is adequately catered for. Specifically, the Electrical Engineering representation must be given the desired due significance.
10. ERA should, in conjunction with relevant players, develop a Power Loss Reduction Strategy to bring down the distribution losses to 18% in the next five years and eventually to match the regional distribution losses average of 15%.
11. As a matter of urgency, prepaid metering system should be installed all over the country. This is one of the key measures that will substantially reduce distribution losses and end-user tariffs.
12. URA should take up the matter of evasion of payment of Capital Gains Tax by Eskom Enterprises when it sold its shares to Globleg and ensure recovery of the said tax. It should also recover all the taxes Umeme has evaded by declaration of depreciation from UEDCL assets.
13. The National Bureau of Standards should in collaboration with ERA develop and establish minimum energy efficiency standards and labels for energy consuming appliances imported or manufactured in

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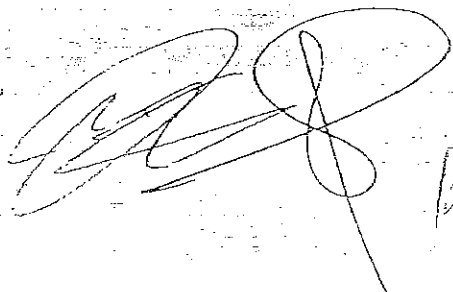
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Uganda. These include electricity metres, air conditioners, refrigerators and deep freezers, industrial electric monitors etc.



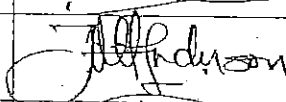
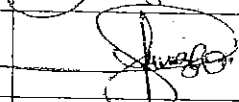
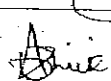
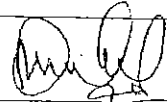
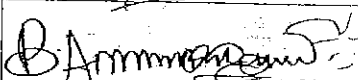
14. The Committee recommends that owing to the strategic importance of electricity projects to the country, the Prime Minister through the responsible sector Minister should institute a water tight supervisory and monitoring mechanism to oversee the said projects and file quarterly reports to Parliament on the status of the electricity sub-sector.
15. The Committee recommends that the Minister of Energy and Mineral Development should present to Parliament, within twelve months after the adoption of this report, the Electricity Amendment Bill to provide for among others, the following:
 - i) Repeal of the PERD Statute by transferring the ownership, management and supervision of UETCL, UEDCL and UEGCL to the Ministry of Energy.
 - ii) Expansion and enhancement of the legal and institutional mandate of ERA by transforming it into the Energy Commission of Uganda with UETCL, UEDCL and UEGCL being among its key departments.
 - iii) Elevation of the Rural Electrification Agency to an Authority with a much more distinct mandate and autonomy, other than its current status where the Permanent Secretary, Ministry of Energy is the Chairman and Accounting Officer.
16. Government should support promotion and development of sustainable management of the country's natural forests and woodlands for sustainable supply of wood including woodfuels.
17. Government should establish an institutional framework to enhance and coordinate woodfuel related activities as an integral part of the national energy development strategy.

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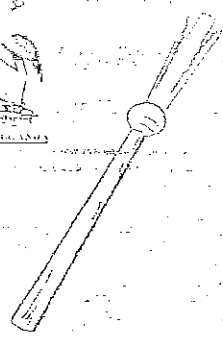

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18. Government should support capacity building programmes for the regulatory and the utility agencies.
19. Government through the ERA develop the necessary Renewable Energy Technology regulatory framework.
20. Government should support promotion and development of biomass for electricity generation from municipal garbage, logging and wood processing residues and agro fuels, as well as plantations.
21. Government should support and help local agencies tap the numerous available world wide funding from international donor facilities ("green credits") such as the Global Environment Facility and the Clean Development Mechanism.
22. Government should explore various options including decentralised and mini-grid systems for reducing the cost of supplying utility power to the rural communities.
23. Government should support Rural Electrification Agency/Authority and ERA to set up local energy advisory units in the district councils to advise consumers on energy efficient technologies and practices.
24. It is recommended that Government urgently develops an integrated and harmonized planning framework that will deal with least cost generation planning to forestall the possibility of commissioning costly energy sources in the supply mix.
25. Further investment in the rehabilitation of the power distribution network should be prioritized done in a bid to reduce energy losses, considering that energy losses have a significant bearing in the computation of the retail electricity tariffs.

ENDORSEMENT OF THE REPORT OF THE PARLIAMENTARY ADHOC COMMITTEE ON ENERGY

No.	NAME	PARTY	SIGNATURE
1.	Hon. Oboth M. Jacob	IND	
2.	Hon. Mulongo Simon	NRM	
3.	Hon. Dr. Eng. Ajedra Aridru	NRM	
4.	Hon. Lubega Sseggona Medard	DP	
5.	Hon. Nankabirwa Ann Maria	NRM	
6.	Hon. Okupa Elijah	FDC	
7.	Hon. Baryayanga Andrew Aja	IND	
8.	Hon. Amongi Betty Ongom	UPC	

APPENDIX I



PARLIAMENT OF UGANDA

PARLIAMENT HOUSE.

Speaker's Chambers.

P.O. BOX 7178
KAMPALA, UGANDA

Tel: +256-414-341 038
+256-414-377 100
+256-414-377 000
Fax: +256-414-231 296

AB 199/199/01

16th September 2011

The Chairperson and Members of
The Adhoc Committee on Energy
Parliament House
P. O. Box 7178
KAMPALA

RE: TERMS OF REFERENCE FOR THE COMMITTEE

This is to advise that your committee commences investigations w.e.f. 21st September 2011. The terms of reference are as follows:

The committee shall assess the performance of the energy sector and in particular:

1. Investigate matters related to power losses, tariffs, subsidies and power generation;
2. Scrutinize agreements between Government and independent power suppliers with a view of determining whether the terms are favourable to Government and consumers;
3. Establish the extent to which the recommendations of the report on the General Salim Saleh Commission of inquiry instituted in 2009 to investigate the energy sector has been implemented;
4. Investigate whether the management of the open tender system (OTS) on the purchase of oil products in Kenya has a bearing on

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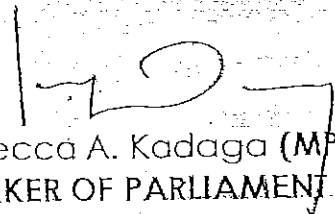
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production costs of generation of thermal electricity by the various power suppliers; and

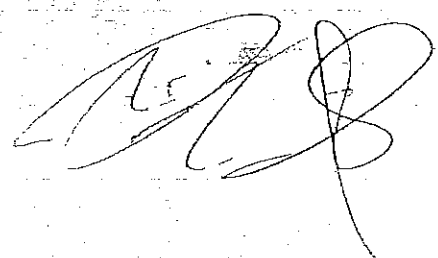
5. Make such recommendation as the Committee may consider appropriate and report back to Parliament within 60 days from the date of its appointment.



Rebecca A. Kadaga (MP)
SPEAKER OF PARLIAMENT

Cc: Rt. Hon. Deputy Speaker
Cc: The Government Chief Whip
Cc: Leader of the Opposition
Cc: Clerk to Parliament

Bank

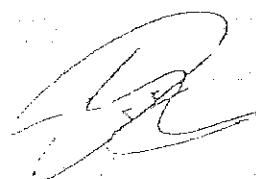


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APPENDIX II

LIST OF WITNESSES MET BY THE ADHOC COMMITTEE ON ENERGY

S/No	Name	Designation	Institution
1.	Hon. Irene Muloni	Minister	MEMD
2.	Hon. Hillary Onck	Minister	MoIA
3.	Hon. Aston Kajara	Minister of State	MFPED
4.	Hon. Du'janga Simon	Minister of State	MEMD
5.	Hon. Kamanda Bataringaya	Minister of State	MoES
6.	Hon. Fredrick Ruhindi	Deputy Attorney General	MoJCA
7.	Mr. J.R. Suuza	PSA	MoJCA
8.	Gen(Rtd) Akandwanaho Caleb(Salim Saleh)	Former Chairman	Interim Review of Electricity Tariff Committee
9.	Mr. Perez Bukumunhe	Former Chair-Technical	Interim Review of Electricity Tariff Committee
10.	Mr. Muyanja Mbabali	Former Vice Chairman	Interim Review of Electricity Tariff Committee
11.	Dr. Muhamed Serunjonji	Former Secretary	Interim Review of Electricity Tariff Committee
12.	Mr. Fred Kabagambe Kaliisa	Permanent Secretary	MEMD
13.	Mr. Ronald Ssegawa Gyagenda	Under Secretary	MEMD
14.	Eng. Moses Murengezi	Advisor to PS	MEMD
15.	Eng. Paul Mubiru	Director Energy	MEMD
16.	Mr. Joseph Odoi	Principal Accountant	MEMD
17.	Mr. David Ssebabi	Director	PU/MFPED
18.	Mr. Jim Mugunga	Spokesperson	PU/MFPED
19.	Mr. Moses Mwase	Head Legal	PU/MFPED
20.	Mr. Richard Apire Sant	Chairman Board	ERA
21.	Mrs. Fatumah Nsereko	Board Member	ERA
22.	Mr. Fabian Tibeita	Board Member	ERA
23.	Mr. Benon Mutambi	Ag. CEO	ERA
24.	Eng. Nobert Semitala	Director - Technical	ERA
25.	Mr. Patrick Mwesige	Director-Finance	ERA
26.	Mr. Julius Wandera	PRO	ERA
27.	Mr. Stephen Mwanda	Legal Counsel	ERA
28.	Mrs. Allen Kagina	Commissioner General	URA
29.	Mr. Moses Kajubi	Commissioner	URA



30.	Mr. John Walakira	Assistant Commissioner	URA
31.	Mr. Joseph Kateregga	Manager	URA
32.	Mrs. Cornelia Sabiiti	Executive Director	PPDA
33.	Mr. Milton Tumutegyereize	Director	PPDA
34.	Mr. Benon Turanye	Director	PPDA
35.	Ms. Patricia Asiimwe	Director	PPDA
36.	Mr. John Muwanga	Auditor General	OAG
37.	Mr. Francis Masuba	Director	OAG
38.	Ms. Caroline Bonabana	Legal Officer	OAG
39.	Mr. John Mugyenzi	Managing Director	UEGCL
40.	Mr. Emmanuel Lubandi	Manager-Finance	UEGCL
41.	Mr. Dan Mayanja	Manager-Technical	UEGCL
42.	Mr. Nicholas Ecimu	Legal Counsel	UEGCL
43.	Eng. Eriasi Kiyemba	Managing Director	UETCL
44.	Mr. Denis Makuba	Manager	UETCL
45.	Mr. Innocent Kihika	Manager	UETCL
46.	Mr. Valentine Katabira	Manager	UETCL
47.	Mr. Emmanuel Owiny	Ag. Manager	UETCL
48.	Mr. Joseph Katera	Managing Director	UEDCL
49.	Ms. Esther Mulyagonja	Company Secretary	UEDCL
50.	Mr. Godfrey Turyahikayo	Executive Director	REA
51.	Mr. Patrick Kyakulaga	Manager	REA
52.	Mr. Benon Bena	Manager	REA
53.	Ms. Deborah Nantume	Supervisor	REA
54.	Ms. Elizabeth Nakungu		MoJCA
55.	Eng. Dr. Sebbowa	Former CEO	ERA
56.	Mr. Johnson Kwesigabo	Former Counsel ERA	ERA
57.	Mr. Charles Chapman	Managing Director	UMEME
58.	Mr. Sam Zimbe	General Manager	UMEME
59.	Mr. Andrew Kasirye	Legal Counsel	UMEME
60.	Mr. Henry Rugamba	Head Communications	UMEME
61.	Mr. Selestine Babungi	Chief Finance Officer	UMEME
62.	Mr. Robert Kisubi	Stakeholder Manager	UMEME

63.	Ms. Florence Nsubuga	Chief Operations Officer	UMEME
64.	Mr. Dag MOEN	Managing Director	Jacobsen
65.	Mr. Roar Millenougen	Director	Jacobsen
66.	Mr. Herbert Dusabe	Company Secretary	Jacobsen
67.	Mr. Charles Muhumuza	CEO	Electro-Maxx
68.	Makenzie .S	Business Analyst	Electro-Maxx
69.	Ms. Nokwanda Mugeni	MD/CEO	Eskom
70.	Dr. Allan Shonubi	Legal Counsel	Eskom
71.	Ms. Elizabeth Ossiya	Director Finance	Eskom
72.	Mr. Peter Tentena	Ag. Director Technical	Eskom
73.	Eng. Mugisha Shillingi	Director	MoWE

MEME LOSSES

PROMINENT PERSONS

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- ① - SEE PAGES 27, 28, 29 of SALEM REIDAT
- ② - " PAGE 5 OF ONEK LETTER TO KALISA DATED 6-11-2006

NOTE ON THE HIGH LEVEL MEETING BETWEEN THE PS MINISTRY OF ENERGY AND UMEME OFFICIALS ON THE AMENDMENT DEFAULT THRESHOLDS OF LOSSES AND COLLECTIONS HELD IN THE MINISTRY BOARD ROOM AT AMBER HOUSE, ON 23RD NOVEMBER 2006

In attendance

Mr. Kabagambe Kaliisa	PS Ministry of Energy & Mineral Development
Mr. Luka Buljan	Director, UMEME Ltd.
Mr. Eriasi Kiyemba	Managing Director, UETCL
Mr. Paul Mare	Chief Executive Officer, UMEME Ltd.
Mr. Sam Zimbe	Chief Customer Service Manager
Mr. David Szabadi	Team Leader Utility Reform - MOFPED

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Introductory remarks by the Permanent Secretary

The Permanent Secretary opened the discussion with highlighting two outstanding issues of concern on the side of Government, on the proposed amendments to the UMEME concession. The first of which was the seemingly low default threshold targets on the Losses and Collections which was in GOU's view, unacceptable in light of the reforms and strategic direction of the sector. He pointed out that the 38% distribution loss threshold and the 20% non-collection threshold did not send the right signals; firstly politically and as well as especially in the context of the need for the highest level of efficiency during the ongoing energy supply crisis.

The PS requested for an understanding from UMEME, because the company was a private entity expected to have the muscle of reducing the losses and increasing collections. Government was therefore proposing that the loss and collection threshold of default be held at the current levels of 33% and 10%; twelve months after amendment, as this would provide enough time for UMEME to deal with them.

See support
agreement
12 months
adjustment
on 31/12/06

The second point of concern raised by the PS was that of the need to expedite negotiations on an agreed framework on how UMEME will cooperate with REA on the Rural Electrification Schemes. This remained a priority for Government and indeed it would be best that this matter is finalized by the middle of December 2006 to allow these schemes to proceed smoothly.

UMEME Response

In their response to the above, UMEME clarified that the default threshold of 38% and 20% were intended to cap the compensations of Government, they were an improvement from the previous position for the benefit of GOU, where potentially GOU was exposed to compensation liability without a ceiling. These thresholds were not meant to be the incentive for efficiency as it would seem to have been understood by Government. The real efficiency loss and collection targets were the regulatory ones, which are provided for in the amendments and are 1% below the level at the time of tariff adjustment for losses and the prevailing collection rate for the quarter ending before a tariff adjustment.

Appendix A

Umeme restructuring: Explanation of the mechanism for allowances of losses and non-collections during the Special Provision Period (The Energy Supply Crisis)

The retail electricity tariff provides allowances for losses and non-collection, which allow Umeme to recover their impact through the tariff. The decrease in these allowances present efficiency targets for Umeme as it improves the business.

	Before restructuring	During SPP	After SPP
Distribution losses			
Allowance for losses	Fixed profile from Schedule A-4 in Annex A to the Supply License ¹	Loss allowance is determined on the basis of actual losses experienced in the previous period minus 1% ²	New fixed profile to be agreed by ERA and Umeme
Impact of Umeme beating the allowance	Umeme keeps 100% of the benefit	Umeme keeps 75% of the benefit for the first five years, thereafter 50%	Umeme keeps 100% of the benefit
Impact of Umeme matching the allowance	Umeme's results are not impacted	Umeme loses money, as it starts the year by being 1% behind the allowance. In order to avoid the impact, Umeme needs to beat the allowance by 1% by the end of the year, i.e. arrive to 2% below the actual level of losses in the previous year.	Umeme's results are not impacted
Impact of Umeme falling behind the allowance	Umeme suffers 100% of the shortfall	Umeme loses the 1% of its revenue, which at today's tariff amounts to \$1.8 million. The rest of the impact is borne by GOU.	Umeme suffers 100% of the shortfall

	Before restructuring	During SPP	After SPP
Non-collection rates			
Allowance for	Fixed profile from	Loss allowance is	New fixed profile to be

¹ The license contained a loss reduction profile which went from 33% to 26% over the first seven years of the concession.

² Therefore, if actual losses experienced by the business in the year 1 were 33%, then the loss allowance in the year 2 will be 32%. The process of determining a new loss allowance is done once a year. Therefore, if by the end of year 2 actual losses experienced go down to 30%, then the loss allowance in year 3 would be 29%. This mechanism has the ability to transfer benefits of loss reductions very quickly to the customers in the form of a lower tariff.

A detailed explanation of the efficiency targets is attached hereto for information-
Appendix A.

UMEME also explained that under the amendments, a comprehensive Loss Reduction Plan has been submitted, and the plan clearly indicates what activities that will need to be done to further reduce losses. They however highlighted the need for Government to support them to implement this plan as a joint effort and welcomed the suggestion from the PS for a regular, preferably quarterly, forum between GOU officials and UMEME to exchange information on Losses and collections. The PS would constitute such a forum.

On the possibility of having local participation in the shareholding of UMEME, the representatives were very positive about, and indicated that this is a welcome development and UMEME would be willing to consider it.

Resolutions

Having heard the clarification from UMEME on the two issues, the meeting resolved the following:

1. That the threshold be maintained at 38% losses and 20% non-collection, however, it is important that the clarification of this being a threshold to cap the compensations as opposed to it being a regulatory efficiency target (which is the relevant incentive mechanism for UMEME to reduce losses) be clarified and explained to all stakeholders.
2. REA and UMEME had made substantial progress in agreeing to a workable framework of the Rural Electrification Schemes and were now on course to achieve the set December 15th Ministerial deadline for resolving the impediments.
3. UMEME would communicate a proposal on how to enhance local participation in the ownership of the Concession Company.
4. There is a need to have a regular forum, preferably on a quarterly basis, in which relevant officials from Government and UMEME will discuss the progress on the reduction of losses and increase in the collections.

non-collections	Schedule A-5 in Annex A to the Supply License ³	determined on the basis of actual non-collection experienced in the previous period	agreed by ERA and Umeme
Impact of Umeme beating the allowance	Umeme keeps 100% of the benefit	Umeme keeps 75% of the benefit for the first five years, thereafter 50%	Umeme keeps 100% of the benefit
Impact of Umeme matching the allowance	Umeme's results are not impacted	Umeme's results are not impacted	Umeme's results are not impacted
Impact of Umeme falling behind the allowance	Umeme suffers 100% of the shortfall	Umeme's results are not impacted - the impact is borne by GOU.	Umeme suffers 100% of the shortfall

³ The license contained a loss reduction profile which went from 25% to 7.5% over the first seven years of the concession.
⁴ Therefore, if actual non-collection experienced by the business in the year 1 was 11%, then the non-collection allowance in year 2 will be set again at 11%. The process of determining a new non-collection allowance is done once a year. Therefore, if by the end of year 2 actual non-collection experienced by the business went down to 9%, then the non-collection allowance in year 3 would be 9%. For non-collections there is no 1% reduction of targets as in losses, as there is a smaller margin to work from and as such it would be impossible for Umeme to deliver.

ANNEX 4 Appendix IV

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PLEASE QUOTE NO:



OFFICE OF THE MINISTER
MINISTRY OF ENERGY AND
MINERAL DEVELOPMENT
P. O. BOX 7278
KAMPALA - UGANDA

ESD/85/237/02

17th November 2006

Hon. Minister of Finance, Planning and Economic Development
Ministry of Finance, Planning and Economic Development
KAMPALA

Dear Colleague,

**RE: UGANDA ELECTRICITY DISTRIBUTION COMPANY LTD
(UEDCL)/UMEME CONCESSION RESTRUCTURING**

This follows mine ESD/567/01 of 30th October 2006 in which I agreed in principle to the restructuring of the UMEME concession subject to further information being availed to me.

Subsequently in a Policy Coordination Committee (PCC) meeting held on 15th November 2006 in which our colleague, the Minister in charge of Privatization participated, we further deliberated upon the restructuring of the UMEME Concession to our satisfaction.

This is to therefore grant our final approval to the restructuring of the UMEME concession – subject to the review of the default threshold for the Distribution Losses and the collection rate, currently set at 38% and 20% to a more acceptable level. Current figures for loss reduction of 33% and collection rates of 10% could be considered as acceptable benchmarks.

We would also wish to reiterate the importance of more active participation of UMEME in the Country's Rural Electrification schemes and shall insist on a workable framework to accelerate these schemes to be agreed between the concessionaire and the Rural Electrification Agency by mid December 2006.

Meantime we would like to propose that the idea of allowing the local population to take up shares in UMEME be given consideration. This will make UMEME more acceptable to the Ugandans since they will have a stake in it, but also they will be able to participate in modern business and to take advantage of the attendant benefits.

Yours,


Daudi Migereko [M.P.]

MINISTER OF ENERGY AND MINERAL DEVELOPMENT

c.c. Hon. Minister of State for Energy,
Ministry of Energy & Mineral Development

c.c. Hon. Minister of State for Finance, Planning and Economic
Development (Privatization)

c.c. The Permanent Secretary/Secretary to the Treasury

c.c. The Permanent Secretary,
Ministry of Energy and Mineral Development

c.c. The Deputy Secretary to the Treasury

c.c. The Chief Executive Officer Electricity Regulatory Authority

c.c. The Director, Privatization Unit

TELEGRAMS: ENERMIN
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MINISTRY OF ENERGY AND
MINERAL DEVELOPMENT
P. O. BOX 7270,
KAMPALA.

IN ANY CORRESPONDENCE ON
THIS SUBJECT PLEASE QUOTE NO:

ESD/85/237/02

28th November 2006

Hon. Dr Ezra Suruma
Minister of Finance, planning and Economic Development
Ministry of Finance, Planning and Economic Development
KAMPALA

Dear Colleague

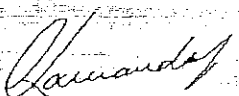
UGANDA ELECTRICITY DISTRIBUTION COMPANY LTD (UEDCL)/UMEME CONCESSION
RESTRUCTURING

Further to our letter referenced ESD/85/237/02 of 17th November 2006 in which we gave our final approval to the restructuring of the UMEME concession subject to the parties agreeing to a more acceptable threshold of losses/collections and resolving the framework for the implementation of Rural Electrification Schemes, I hereby wish to grant our no objection to the execution of the amendments.

Our no objection is granted after having been satisfied that the losses and collection threshold as set out in the proposed amendments are not the regulatory targets of performance, but rather are a mechanism of capping the Government compensation on increasing losses and reduced collections.

Secondly, we are also satisfied on the progress made on resolving the impediments of the implementation of the Rural Electrification Schemes, for which, according to our understanding, a workable framework will be in place by 15th December 2006.

Yours sincerely


Dr Cos Kamanda Bataringaya
MINISTER OF STATE FOR MINERAL DEVELOPMENT also HOLDING
THE PORTFOLIO OF MINISTER OF ENERGY AND MINERAL DEVELOPMENT

Cc The Minister of Energy and Mineral Development

Cc The Minister of State for Energy

Cc The Minister of State for Finance, Planning and Economic Development
(Privatization)

cc The Permanent Secretary, Ministry of Energy and Mineral Development

Cc The Permanent Secretary/Secretary to the Treasury

Cc The Deputy Secretary to the Treasury



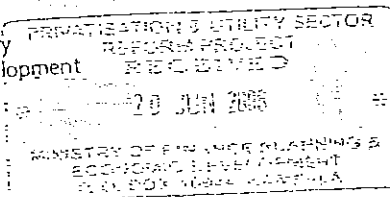
ELECTRICITY REGULATORY AUTHORITY

Promoting Quality and Sustainable Electricity Supply at Equitable Prices

June 16, 2006

Ref: MEMD/006/005-mdk

The Permanent Secretary/Secretary to the Treasury
Ministry of Finance, Planning and Economic Development
P.O. Box 8147
KAMPALA



Attn: Mr. Keith Muhakanizi

Dear Sir

RESTRUCTURING OF THE UGANDA ELECTRICITY DISTRIBUTION CONCESSION

We refer to your letter Ref EDP 49/258/02 of 12th June 2006 on the above subject matter.

You will be glad to know that ERA is a full member of the Project Transaction Committee (PTC) set up by the Utility Reform Unit (URU) and have very senior representation at most of its meetings.

The distribution losses remain a major enigma in the sector. ERA has recently sought some independent profession advise on these losses.

Through the support of the Norwegian Embassy, the Authority (with approval of Umeme Ltd) commissioned Norconsult AS an Oslo based energy consulting firm in April 2006 to address some of the issues raised in your letter. Their work with Umeme Ltd on losses is on-going. However, they recently submitted a draft report on the "Study on Establishing the Level and Cause of Distribution Losses", which although un-discussed by all parties seem to suggest that:

- The total distribution losses are at present estimated to be 34-35% //
- The technical losses are at present estimated to be 14-17%
- The commercial losses are at present estimated to be 16-19% //

Since the total is close to numbers presently reported by Umeme Ltd the split might also be close. One would on average take technical losses as 15.5% and commercial losses at 17.5%.

Our advice in the PTC on how to restructure issues around the losses has been:

a) Worsening Losses Scenario:

All parties to agree a present 35% total distribution losses. Umeme Ltd has full control over the technical component of the losses.

In case of any worsening of distribution losses above 35% Umeme should be only compensated up to a maximum of pro-rated commercial loss component i.e. 53% of the escalation in distribution losses above the 35%. For example, if total distribution losses were to shift from 35% to 37% Umeme should be allowed $(35 + 2 \times 53\%)$ i.e. 36.06% as the total distribution losses. The 0.94% would be a technical loss met by Umeme and would act as an incentive for Umeme Ltd to invest in loss reduction equipment/infrastructure.

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