# PROJECT INFORMATION DOCUMENT (PID)
## CONCEPT STAGE

Report No.: PIDC1290

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## I. Introduction and Context

### Country Context

Despite its numerous geographical disadvantages, as well as political unrest within and adjacent to its borders, Uganda has sustained one of the world’s highest per capita economic growth rates over two decades. In the late 1980s, Uganda was one of the first Sub-Saharan African countries to embark on liberalization and pro-market policies. Through the 1990s, the government maintained a stable macroeconomic environment and continued to undertake private-sector oriented reforms. By 2006, Uganda had graduated into a mature reformer, and had achieved an average annual GDP growth of 8.1% over the six year period from 2002/2003 through 2008/09. However, a succession of shocks including the global economic crisis, a prolonged drought, a surge of election related spending in 2010 and recent corruption cases affected the country’s macroeconomic stability. The rate of growth of GDP, which averaged 7% during the two previous decades declined to 5.9% in 2010 and to 3.4% in 2012. As a result of adopting corrective fiscal and monetary policies, the Government of Uganda (GoU) was able to stabilize the economy in 2012 and 2013. GDP growth is
expected to go up to about 5 percent in FY13, while the inflation rate has reverted to a single digit after exceeding 30 percent at the end of 2011.

Like any other country, an adequate and reliable supply of electricity is a necessary condition for sustainable growth and development in Uganda. Access to electricity enhances the socio-economic development of the population through better access to education, health care, and personal security. It also facilitates the development of small-scale industrial and commercial enterprises and provides an added incentive for larger-scale industrial and commercial investment in the country. So far, Uganda has failed to fulfill this need. Despite substantial power resources, its capacity to provide reliable, cost effective electricity supply has continuously lagged behind the demands of its growing economy.

In order to address the above and transform the Ugandan society from a peasant based agrarian society to a modern and prosperous country within 30 years, the GoU has articulated the “Uganda Vision 2040” that lays out broad policy directives and sets out a target of increasing access to electricity to 80 percent by 2040. In this context, the National Development Plan (NDP) of Uganda for the period FY11-15 focuses on increasing access and usage of electricity by investing in least cost power generation, promotion of renewable energy and energy efficiency in addition to the associated transmission and distribution infrastructure.

**Sectoral and Institutional Context**

The Uganda Electricity Board (UEB) was established in 1948 as a vertically integrated utility with responsibility for all aspects of power sector operations in the country. Despite concerted attempts, UEB had failed to improve its efficiency and performance. In the late 1990s, the GoU recognized that major efficiency improvements and expansion of access to electricity could be better accomplished through implementing a comprehensive power sector reform program which placed the power sector under private management operating on commercial principles. Since then, the sector has been unbundled, legal and regulatory reforms introduced, and operation of the main generation and distribution assets turned over to the private sector under long-term concession agreements. Three separate corporate entities were created through the unbundling of UEB to manage the generation, transmission and distribution aspects of the sector: Generation – Uganda Electricity Generation Company (UEGCL); Transmission - Uganda Electricity Transmission Company (UETCL); and Distribution - Uganda Electricity Distribution Company (UEDCL). For the purposes of introducing private sector efficiencies into management and operation, generation assets of UEGCL were contracted to Eskom (Uganda) Ltd and the distribution assets of UEDCL that only covered some parts of the country, were contracted out to six Licensed Distribution Companies (LDCs). In order to increase access to electricity in rural areas, a Rural Electrification Strategy and Plan (2001-2010)–RESP-1 along with a Rural Electrification Master Plan were developed. A Rural Electrification Board (REB) was established to oversee the operations of the Rural Electrification Agency (REA) which using funds made available by the Rural Electrification Fund (REF) was responsible for undertaking rural electrification investments and build the necessary facilities. These were then handed over to the LDCs under license to operate and maintain as a commercial utility. Within an existing concession area, consumer connection was left to increase on its natural course. Without any strategy for expanding the concession areas (aimed at improving commercial viability) or specific targets to increase access, the LDCs had little appetite to increase their consumer base and expand their business and revenue earnings.

During the period 2001-2010, the power sector faced several significant challenges. Chief among
these were: (i) a lack of adequate and reliable power supply - because of delays in the implementation of the Bujagali Hydropower Project (BHPP), which forced the GoU to introduce expensive rental-based thermal generation; (ii) weak sector finances resulting from inadequate tariffs and financing of expensive thermal generation that caused a significant drain on GoU’s budgetary resources; (iii) inadequate operational performance (such as high system losses of more than 30%) on account of weak enforcement of sector regulations; (iv) weak institutional set-up and capacity to deal with such issues as integrated least-cost system planning and increasing access. This was exacerbated by the lack of necessary coordination between some of the key sector players such as the MEMD, UETCL, REA and the LDCs.

The strategy undertaken by the GoU to address the above challenges has been to: (i) increase electricity supply through investments in renewable energy and improvements in energy efficiency – the BHPP (250 MW) was commissioned in August 2012. This improved the power supply situation significantly and reduced the dependence on expensive thermal generation options that had caused serious drains on budgetary resources. However, with an estimated growth in demand of about 15% per annum, shortages are expected to return around FY15 until new generation facilities at Karuma (600 MW), Isimba (180 MW) and Ayago (600 MW) are commissioned, expected within the next five or more years. In the interim, GoU is promoting the development of small hydro power plants and other renewable energy resources by the private sector; (ii) implement tariff adjustments – the last one was in January 2012 of about 50% and is close to being cost reflective. A combination of availability of power from BHPP along with much needed tariff increases had significantly reduced the budgetary support needed for sustainable operations of the sector; (iii) develop a more diversified generation mix, as well as a strong interconnected national grid with links to neighboring countries, for ensuring security of supply and increased potential for electricity trading between East African Community (EAC) countries; (iv) continue monitoring of sector entities that led to an improved operational performance (system losses are expected to be reduced to about 20% within the next five years under the recently approved regulatory review); and (v) continue developing the institutional framework and capacity of the key sector institutions.

All through this period, the World Bank Group played a major role in supporting the GoU initiatives. On generation, for the BHPP, financial support provided by the IFC was augmented by MIGA guarantee and an IDA supported PRG. Currently, a PRG is under preparation for the development of small-hydro plants. On the development of the national grid, the Bank is financing implementation of the 220-kV Kawanda-Masaka transmission line. On development of the distribution network, over the last eight years, the Bank has been supporting the concession of the public distribution infrastructure to a private investor (Umeme). Rural transformation is a priority in the GoU’s Poverty Eradication Action Plan (PEAP), which places a lot of emphasis on the provision of infrastructure and functioning social services to promote growth and reduce poverty. In November 2001, the Bank approved the Energy for Rural Transformation (ERT) program as a three-phase Adaptable Program Loan (APL). The purpose of the ERT program is to develop Uganda’s energy and information/communication technologies (ICT) sectors, so that they make a significant contribution in bringing about rural transformation, i.e., these sectors facilitate a significant improvement in the productivity of enterprises as well as the quality of life of households.

In the past, development of the rural electrification program was based on the RESP-1 which aimed at increasing access to electricity in rural areas from 1% in 2001 to 10% by 2010. Implementation of the RESP-1 started with support from the APL-ERT program. The first phase of the program
(ERT-1) covered the period 2001 through 2009 and was followed up by a second phase of the program (ERT-2) that is covering the period 2009 through 2016. However, implementation was carried out in a disaggregated manner with many players acting in ineffective coordination and often playing overlapping roles. As a result, the outcome of the RESP-1 was not satisfactory and access to electricity in rural areas at the end of 2010 is estimated at less than 4%; by mid-2013, this is reported to have reached 7%. In view of this low level of rural electricity access, the GoU attempted to increase the level of access for the rural population through a number of bilateral and multilateral funded programs that financed 33 kV distribution lines, transformer stations and low voltage reticulation lines. Despite this, connection rates remained at a low level, often ranging from about 10% to 20% of the targeted consumers. In brief, the main reasons for the unsatisfactory performance in increasing access can be attributed to: (i) unclear roles and responsibilities of the different agencies responsible for increasing access; (ii) disassociations of the investment in rural electrification from the existing operations and maintenance arrangements and lack of participation in network expansion design by the LDCs; (iii) lack of incentive within the LDCs to increase access particularly amongst the rural poor; (iv) inadequate funding for service connection materials; (v) high cost of service connections (starting from US$200 per connection) and the requirement for consumers to pay the cost of the connection upfront; and (vi) absence of any organized effort at consumer mobilization.

Based on findings of a study (financed by a DfID TF) under the Uganda Accelerated Rural Electrification Project (UAREP), a second Rural Electrification Strategy and Plan (RESP-2) was formulated for the period 2013 through 2022 to address these issues. This Policy document was approved by the Cabinet in July 2013. Under the RESP-2, a new business model has been developed that promotes a centralized planning and management of the RE sector and simplifies program implementation. The RESP-2 takes an area coverage approach, whereby the country is divided into 13 Service Territories (ST) each to be served by a Service Provider (SP) that will be responsible for all management, operational and maintenance activities within its dedicated/assigned Service Territory. Currently, there are six LDCs that operate as SPs covering eight STs. Thus, there are five STs that have no operators and until such time that permanent SPs selected through a transparent selection process are appointed, a proposal for having an interim operator for these five STs is under consideration. The selection will be based on a transparent tendering process that will be open for bidding for the private sector (including cooperatives). The map below shows the 13 Service Territories created through the RESP-2. The RESP-2 also proposes the conversion of the REA to an autonomous government entity along with the granting of sufficient policy and administrative decision making authority. Such proposals are expected to be formulated and submitted to the parliament for approval in 2014.

The RESP-2 attempts to address the issues mentioned earlier (para 9) in the following manner: (i) an institutional set-up/mecchanism is in place whereby the SPs will be directly responsible for increasing the access to electricity; (ii) centralized planning and management of the rural electrification sector will help in better coordination of all sector players; (iii) performance targets will be set between REA and the SPs and the performance of individual SPs will be measured against targets met. Adequate incentives will be included while setting up the agreed performance targets; these will include increases in areas of operation of individual SPs resulting in increased revenues through enlarged customer base/favorable consumer mix, adequate tariff to cover operating costs and agreed returns on any investments made in combination with discounted Bulk Supply Tariff if necessary; (iv) financing requirements for the RESP-2 implementation period has been identified enabling GoU to actively pursuing necessary funds required to implement the entire
program; (v) cost reductions for connections charges are under consideration, including options for eligible consumers to pay up for connections costs through installment arrangements; and (vi) consumer mobilization is being initiated and will be facilitated through retaining appropriate external services support.

The implementation of the RESP-2 and in particular, the design of the appropriate mechanisms to address the issues highlighted above will be supported under the proposed Project through Technical Assistance as necessary. Some of the specific actions such as those related to (iii), (v) and (vi) above will need to be accomplished within an agreed time frame during processing of the proposed Project.

The proposed Project is the third and last phase of the ERT Program, and is aimed at increasing access to energy in rural areas of Uganda that is expected to facilitate improvement in the productivity of enterprises and the quality of life of the households. The total program amount is currently at US$165.15 million, of which the first phase (ERT-1) was for US$49.15 million, and the second phase (ERT-2) was approved for US$75.0 million. The remaining US$41.0 million was earmarked for ERT-3. In order to meet the connection targets of the ERT-2, an Additional Financing for ERT-2 (AF-ERT-2) was approved for US$12.0 million in FY13. In view of the major transformational role that rural electrification plays and in response to the needs of “Vision 2040”, IDA allocation for the third and final phase has now been increased to US$100 million thereby raising the total IDA support for the program to US$236.15 million. Along with cofinancing (joint) from GEF, for US$30.02 million, the entire ERT program will be providing a total of US$266.17 million of WB Group support. Lately, additional cofinancing (parallel) from an Output Based Aid program for US$16.0 million (equivalent) comprising funds from the GPOBA (US$5.5 million), KfW (Euro 5.0 million) and the GoU (US$4.0 million) has been made available; this operation became effective in December 2012. As connecting households to the grid would eventually lead to emission reductions due to replacement of mostly fossil based lighting, possibilities are being explored of assessing other market-based instruments such as carbon finance, or other results-based finance instruments based on greenhouse gas emission reductions to improve the sustainability of providing energy access.

In terms of providing access to electricity, the ERT program aims at connecting households (HH) through both on-grid and off-grid connections, providing institutional connections to schools, health centers and water pumping stations. In addition, energy efficiency measures such as solar water heaters and power factor correction equipment are also financed.

During implementation of the ERT program, other donors have also participated in the development of the rural electrification sector. These were outside the ERT program and consisted of financing from KfW, Government of Norway, JICA, BADEA/SFD and the IsDB. In addition, new development partners (such as ADB and AFD) are currently engaged in discussing possible financial assistance to the sector. Total financing from other donors has so far been about US$150 million; in addition, funding for an additional amount of about US$93.5 million is under discussion with various donors. Despite this significant donor support, a major financing gap still needs to be filled in order to meet the overall financing needs of the sector which is estimated at about US$1.0 billion for the next ten year period (FY13-22).

Because of implementation delays, the Closing Date of ERT-2 was extended until June 30, 2016. Major reasons justifying this extension are: (a) while most components, other than the infrastructure
development, are expected to be completed by the end of December 2014, the rural infrastructure development component (mainly comprising construction of grid schemes) will need additional time to complete; (b) recent approvals for funding of service connections (GPOBA and AF-ERT-2) will require additional time for implementation and meet the connection targets for the ERT-2; (c) recent approval of the RESP-2 has provided a new policy directive that allows the access base to increase in a rapid and sustained manner. However, establishment of the new institutional arrangements will require additional time. Against the above back-drop, the proposed Project (expected to be effective by the end of August 2014) will facilitate implementation of the RESP-2 and provide the much needed impetus towards attainment of the connection targets for RESP-2 that will ultimately pave the way towards reaching the developmental goals of the “Vision 2040”. The timing of the ERT-3 is thus considered appropriate.

Relationship to CAS
The Country Assistance Strategy (CAS) for FY2011-2015 aims at reducing unmet demand for electricity and increasing access to electricity for the rural population, including through: grid extensions and the harnessing of renewable energy resources (on-grid and off-grid). In the context of increasing access to electricity (CAS Outcome number 2.1), the GoU has prepared the RESP-2 covering the period 2013-2022. The proposed Project is fully aligned with the CAS FY11-15 and is primarily dedicated to facilitating the implementation of the RESP-2 in a sustainable manner leading to achieving the targeted increase in electricity access.

II. Proposed Development Objective(s) / Global Environmental Objective(s)
A. Project Development Objective(s)
The program’s long-term objective of rural area transformation is retained in this project because it is as relevant now as it was when the program was first designed. It is also clear that some changes are needed in view of the implementation experience, changing conditions in the power and ICT sectors, and changes in the Ugandan economy.

The project development objective is to increase rural access to electricity.

B. Global Environmental Objective(s)
The GEF objective is to increase the use of renewable energy and promote energy efficiency. Energy efficiency was not originally included in the long-term program but was added during Phase I when Uganda’s unexpected shortage of power at peak times created an opportunity to initiate energy efficiency measures.

These objectives will be achieved by accelerated investments and shifting from the case-by-case approach of ERT-1 to processing projects through the institutional framework developed during implementation of ERT-2.

Key Results (From PCN)
The key results that would reflect and measure success in achieving the PDOs would include: (a) number of on-grid connections made; (b) number of households using Solar PV systems; (c) number of Health Centers with access to electricity using solar systems; (d) number of rural schools with access to electricity using solar systems; and (e) number of water pumping stations with access to electricity using solar systems.

III. Preliminary Description
The proposed Project will be designed in line with the 2001 description of the ERT Program as approved by the World Bank and the GEF Council with minor adjustments needed to reflect better the current country and sector context and requirements. It will provide US$100 million (eq.) in IDA funds (as a Credit) and US$8.9 million in GEF funds (as a Grant). The proposed components are shown below with initial cost estimates and an indicative financing plan. The GoU is preparing a “Project Summary” paper that will include a complete proposal on project components (including cost estimates) and their financing and implementation arrangements. These details are expected to be in line with discussions held during the last preparation mission (June 2013) and will be used for further processing of the proposed Project.

Component 1: Rural Energy Infrastructure: (US$95.4 million – US$82.3 million IDA, US$3.1 million GEF; US$10.0 million GoU). On-grid investments will finance all on-grid activities. Off-grid investments will include installation of fixed solar home systems (SHS). Possibilities are being explored to include financing of mobile solar systems as well on a pilot basis under collaboration with the Africa Lighting Initiative. All on-grid activities will be implemented by REA. For implementation of off-grid activities (SHS), the implementation arrangements are under discussion. Technical Assistance will be provided to finance the necessary consultancy services and training.

Component 2: Energy Development, Cross Sectoral Links and Impacts Monitoring: (US$17.4 million – US$13.0 million IDA, US$4.4 million GEF). This component will finance installation of solar PV systems for institutions such as schools, health centers and water pumping stations – as was done for the ERT-2, these will be implemented by the respective line ministries (i.e., MoH, MoE&S and MWE). The PSFU will continue with their successful investment components such as Power Factor Correction Equipment, Solar Water Heaters and Private Sector Small Hydropower Development etc. It could also include supporting the Efficient Cooking Stove initiative that is currently under discussion and funded by a Russian Trust Fund. Finally, the UECCC will utilize their portion of funds to facilitate local commercial finance by providing credit enhancement products such as partial risk guarantees, and other refinance facilities. Technical Assistance provided under this component will finance the necessary consultancy services, capacity building and operations costs as agreed.

Component 3: Renewable Energy Development: (US$ 6.1 million – US$4.7 million IDA, US$1.4 million GEF). This component will finance development of other renewable energy resources such as geothermal energy, studies for small hydropower development etc., and will be implemented by the MEMD. Technical Assistance provided under this component will finance the necessary consultancy services, capacity building and operations costs as agreed.

Changes in Project Design:
The proposed design and preliminary allocation of funds responds to the implementation experience of ERT-1 and ERT-2 as well as overall changes in Uganda’s economy and the power sector as described below.

Changes Based on Implementation Experience of ERT-1 and ERT-2
Based on implementation experience of ERT-1 and ERT-2, the most significant change in project design is to drop the Information and Communication Technology (ICT) component. Although, under the ERT-1, there was a general increase noted in the usage of mobile phones and internet
services in the project areas, there has been no conclusive evidence to attribute this to the project. Additionally, despite the slow implementation of the ICT component of the ERT-2, the ICT sector has steadily grown by about 30% mainly through private sector led investments implying irrelevance of any GoU financing through IDA/Donor support. However, this has started in the urban areas and is expected to expand and gradually cover the rural areas as well. In view of this, the GoU is considering not to borrow any further from IDA in support of the ICT sectoral development. On providing connections to agro-industries, other donors (such as the USAID) have shown interest in financing electricity connections for the agro-industry. This will be supplemented by GoU budgetary support to promote further growth of the industry. Consequently, no support to the Ministry of Agriculture, Animal Industries and Fisheries (MAIIF) has been considered under the proposed Project at this time. Finally, in terms of providing PV systems to schools, the Ministry of Education and Sports (MoE&S) has demonstrated satisfactory implementation capacity and will carry out these installations. As such, contrary to the ERT-2 design of supporting the capacity building of the MoLG through their implementation of PV systems for schools, the current project design will not require the Ministry of Local Government (MoLG) to implement any new PV systems for schools.

Changes Based on Sectoral Development

While the design of ERT-1 and ERT-2 was guided by the policy parameters of the RESP-1, the design of the proposed ERT-3 will be guided by the policy directives of the recently approved RESP-2. For each Service Territory, the relevant Service Provider will be accountable for increasing access, both on-grid and off-grid. Agreed targets will form a part of performance indicators and will be included in a “Lease Agreement” between REA and individual SPs. While capital financing for on-grid electrification shall be provided under a system of long-term leasing and financing contracts to be concluded with the SPs, off-grid electrification services comprised of other energy service technologies not dependent on grid electricity shall be planned, offered and supplied to eligible consumers in the STs in tandem with on-grid electrification services.

Changes Based on Implementation Arrangements

The recent approval of the RESP-2 will lead to significant changes in implementation arrangements for on-grid connections that are aligned with the principles developed under the AF-ERT-2. Unlike implementation of the RESP-1, where accountability for increasing access was not clearly defined, under the RESP-2, the SPs will be responsible for carrying out connections and increasing access. Given the overall financial weakness of the SPs, REA will procure service connections materials (that will be financed through the proposed Project) in bulk and have them delivered at the individual stores of the SPs. As a part of common utility practice, the SPs will finance consumer connections through advances paid by the consumers. Through special arrangements as stipulated in the legal agreements between REA and individual SPs, the recipient SPs will pay back REA the cost of materials received in a manner satisfactory to REA and individual SPs. These amounts will be deposited in a dedicated account managed by REA who will then reuse these funds for future procurement and supply of service connection materials. Thus, the recycling of funds – “Revolving Funds” will make additional funds available even after the project financing has ceased. Appropriate audit arrangements (non-consultancy services) will be in place to verify the connections made including adherence to technical standards. This will ease the shortage of funds somewhat (para.11) but more funds will still be needed to attain the target of “Vision 2040”. For development of off-grid electrification, on the solar home systems, implementation experience of the SHS under the ERT-2 through the Photo-Voltaic Targeted Market Approach (PVTMA) has not been satisfactory. During the four year period (2009-2013), only 6817 SHS were installed, that too
on a highly subsidized basis. This is very low compared with some of the better implementation experiences in other countries. As such, the GoU is considering several options that will aim at accelerating the installation of SHS including extending refinancing facilities to solar vendors on the basis of a declining subsidy regime leading to its ultimate removal.

Changes on Monitoring and Evaluation
Under ERT-2, overall, 109,000 new connections were expected to be made; of this, 52,000 connections were to be installed on newly built grid schemes within the project areas (new areas) and 57,000 connections were to be installed on the existing grid system outside the project areas (old areas). As explained earlier (para. 16), delays in implementation of new grid schemes had undermined any initiative to increase access in the new areas. Also, since the ERT-2 project design did not allocate any separate funds for procurement of connection materials, the project could not finance any new connections. However, during implementation of ERT-2, some connections were made outside the ERT program in the existing distribution networks (old areas) from sources other than the project (non-ERT program). Linkage of project performance to the availability of funds from sources other than the project (non-ERT program) and relevance of its monitoring and evaluation was discussed during preparation of the AF-ERT-2. This has been considered not reflective of the project’s implementation performance; as such connections made outside the ERT program could not be attributed as an output of the ERT-2. At the time of the original Closing Date of the ERT-2 (June 30, 2013), no connections had been made on account of the ERT program. In order to address this issue, financing for service connection materials was arranged and the GPOBA grant (US$5.5 million) and the AF-ERT-2 credit (US$12.0 million) – both linked to the ERT-2, were approved. Together, these will play a crucial role in increasing electricity access in rural areas and are expected to finance about 120,000 connections by project closing that has now been extended until the end of FY16. This will facilitate meeting the targets for the ERT-2 (109,000) and through scaling up (to 120,000 connections), accelerate the electricity access agenda.

Changes Based on National Developments
The RESP-1 did not meet all its intended objectives. Unlike the earlier RESP-1, where electricity access was expected to increase through targeting electrification such as in areas within one kilometer on either side of the distribution line (1-km foot print), the RESP-2 takes an area coverage approach, whereby the country is covered and divided into 13 STs each to be served by an SP that will be responsible for all management, operational and maintenance activities within its dedicated/assigned territory. Its design has also taken cognizance of the United Nations (UN) initiative on modern energy for all – Sustainable Energy for All (SE4ALL) which calls for all governments to ensure the availability of clean and affordable modern energy in all homes by 2030.

IV. Safeguard Policies that might apply

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VI. Contact point

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