I. Introduction and Context

Country Context

The Kyrgyz Republic, with a multi-ethnic population of around 5.5 million, is one of the two low income countries in the Europe and Central Asia region. The Kyrgyz economy has fluctuated widely over the past 5 years due to economic and political vulnerabilities. Growth has ranged from a strong 7.6 percent in 2008 to a recessionary -0.5 percent in 2010 following political and social disturbances in April and June of that year. This volatility has continued, with the economy expanding by 6 percent in 2011 and contracting by -0.9 percent in 2012, owing to a sharp drop in gold output.

Poor governance, especially corruption, and lack of voice in governing institutions was the fundamental cause of political upheavals in 2010. Improving the governance and enhancing...
transparency and accountability in the public sector are strongly demanded by the general public and are at the heart of the National Sustainable Development Strategy 2013-17 (NSDS) of the Government. Given the significant role of the energy (particularly power) sector in the Kyrgyz economy, improving the management in energy enterprises and enhancing transparency of their activities is a key reform area under the NSDS.

**Sectoral and Institutional Context**

The power sector of the Kyrgyz Republic is overwhelmingly publicly owned and operated by six Joint Stock Companies that are responsible for power generation, transmission and distribution. The companies consist of a generation company (the Electric Power Plants), a transmission company (the National Electricity System of Kyrgyzstan) and four regionally divided distribution companies (Severelectro, Vostokelectro, Oshelectro and Jalalabadelectro).

The power sector is relatively large and has significant growth potential. It accounts for about 4 percent of GDP and 16 percent of industrial production, and its performance is critical for the growth of the Kyrgyz economy. The sector has a significant unrealized potential for export. Other advantages of the power sector are relatively low cost of power generation, reliance on clean sources of energy, and the near universal access to power supply.

However, the sector is hobbled by lack of financial viability and poor service quality and reliability. Power tariffs are exceptionally low and do not allow the sector entities to recover even recurrent expenses. Thus, for 2007-11 the sector’s accrued expenses (not adjusted for under-spending on maintenance and financing costs for capital expenditure) were on average 35 percent higher than the average end user tariff. Consequently, the energy sector is a source of a substantial quasi fiscal deficit that accounted for about 2.5 percent of GDP in recent years. A major consequence of the sector’s poor financial condition is under-investment and under-spending on maintenance-perpetuating problems for supply reliability and service quality. In 2013, the four distribution companies reported that 28 percent of all power lines were in unsatisfactory or unserviceable condition, and Severelectro stated in 2012 that 85 percent of its distribution lines and electrical equipment was in urgent need of repair. As a result, from 2010-12, Severelectro alone recorded outages every hour in winter and every other hour on an annual basis. Unless some critical investments are implemented, the power sector may face fatal failures leading to extended outages, further impeding the country's economic development, and deteriorating quality of life for the population.

Underlying the sector challenges are the weak governance of the sector and the lack of transparency and accountability in its operations. The results of the weak governance and the poor operational and financial performance of power utilities are reflected in the high level of technical and commercial losses in the sector, which were 22 percent of net generation in 2012, one of the highest in the Europe and Central Asia region. At the sectoral level governance issues include the ambiguous regulatory environment, sub-optimal contractual arrangements between the power sector companies and payment mechanisms in the sector hindering the transparency of power and financial flows and undermining the incentives for good performance and sound management by the sector companies. At the company level, the manifestations of the poor governance include poor internal control systems, inadequate corporate resource management and customer information management systems, which are not integrated and most procedures are manual.

To address the serious challenges that the power sector faces, the Government developed a Power
Sector Development Strategy for 2012-2015. Measures in the strategy include: (a) further improvements in efficiency and transparency of the sector operations, (b) development and adoption of a medium-term tariff policy that would need to be accompanied by properly designed revisions of social protection schemes, and (c) a number of important energy investments. In addition, the Government adopted an Action Plan for Reforming the Energy Sector in 2013-14 to operationalize the implementation of the Strategy and coordinate donor support to the sector. The Government has implemented some modest governance related measures already. For example, it introduced an escrow account for power export proceeds in 2011. It also introduced the Fuel and Energy Sector Transparency Initiative in 2011 in an attempt to improve management and governance within the sector by ensuring greater public participation and transparency.

The Government has requested the Bank to allocate IDA funding for the Electricity Supply Accountability and Reliability Improvement Project (ESARIP) to reduce losses and revenue leakages in Severelectro OJSC. Severelectro is the largest distribution company, owning and operating the distribution grid for the city of Bishkek, Talas Oblast and the Tchui Valley. The company serves a total of about 462,000 households, representing approximately 45 percent of the total household consumers in the Kyrgyz Republic.

Relationship to CAS

The new Country Partnership Strategy (CPS) for 2013-2017 recognizes governance as the key development challenge. Specifically, it identifies maintaining scarce natural resources and physical infrastructure, including energy, as one of the three areas of focus for the CPS.

II. Proposed Development Objective(s)

Proposed Development Objective(s) (From PCN)

The proposed development objective is to improve the reliability of electricity supply in the project area and strengthen the governance of the company’s operations.

Key Results (From PCN)

The key results indicators include:

Indicator 1. Reduction of total losses - electricity injected into Severelectro that is not paid for by customers - in the service area of Serverelectro (based on Cash Recovery Index - CRI).

Indicator 2 (core sector indicator). Decrease in average interruption frequency per year in the project area (based on System Average Interruption Frequency Index – SAIFI).

Intermediate results indicators, including distribution lines rehabilitated under the project (core sector indicator) and other relevant indicators, will be developed for tracking project progress after the project scope is finalized.

III. Preliminary Description

Concept Description

The project will achieve the development objective through a holistic approach that integrates the following three components: (i) rehabilitation of select segments of distribution infrastructure, (ii) incorporation of Information Management Systems, and (iii) institutional strengthening.
Component 1 Infrastructure rehabilitation: This component will strengthen the distribution infrastructure of Severelectro by focusing on the sections of the infrastructure where losses are high and may jeopardize reliability of power supply. The investments may include replacement of meters, conductors, transformers, switchgear and other distribution assets. The scope of this component will be finalized based on the investment program that Severelectro is developing with the support from an international consultant and funded by the ECA Capacity Development Trust Fund Grant. The investment program will include a comprehensive set of investments aimed at reducing losses and improving reliability of power supply in the service area of Severelectro. Component 1 will finance priority investments (with highest potential for reducing losses and improving reliability of supply) identified in the investment program and will also complement the ongoing KfW financed Distribution Network Improvement Project for Bishkek.

The KfW financed project focuses on areas of Bishkek that do not have access to district heating and account for 40 percent of consumption in Severelectro’s service area. It includes replacement of 110,000 customer connections by new ones designed and built to prevent electricity theft, including advanced meters (with remote reading and remote disconnection/reconnection functionalities) installed in protected boxes; limited replacement of conventional (bare) conductors in low voltage networks by aerial bound conductors to prevent illegal connections; and establishment of metering data management system.

Component 2 Information Management Systems: This component will provide Severelectro with information tools for identification of losses and revenue leakages and for modern and efficient management of the services it provides to the customers. To that end, the component will finance supply, installation and commissioning of the information management systems (IMSs), as well as training to Severelectro employees to apply them. The IMSs will be set-up company wide and may include:

(a) Commercial Management System (CMS) that will be available in all customer service centers of Severelectro and allow: (i) integrated management of commercial cycle (metering, reading, billing, collection, and receivables accounting); (ii) on-line management of customer database; (iii) management of customer service orders, including registration of all the activities performed for each client (e.g. service interruption, reconnection, metering replacement, new connection, etc.); (iv) execution and monitoring of Severelectro’s energy balance, including evolution of losses. The CMS will enable detection of billing errors and fraudulent behavior, management of delinquent accounts, and facilitate quick and efficient response to the clients’ requests (e.g. general and account information requests, contracting, service requests, claims, etc.).

(b) Incidence Recording and Management System to be integrated with the CMS and allow Severelectro to better respond to client contingencies by automating the detection of distribution faults and ensuring the quality of power supply.

(c) Implementing a Corporate Resource Management System for Severelectro to complement the CMS by integrating the management of all the processes and resources (financial and management accounting, procurement, human resources management, etc.) of Severelectro under a single technological platform that eliminates erratic processes and unnecessary efforts.

The technical and functional specifications of the CMS and other IMSs will be finalized during the project preparation.
Component 3 Institutional Strengthening and Project Implementation Support. This component will provide technical assistance to Severelectro to enhance its institutional capacity, support project implementation and incremental operating expenses of the Project Implementation Unit (PIU) under Severelectro for the smooth implementation of the project and sustainability of project outcomes. The technical assistance will include support for: (i) project management, monitoring and evaluation; (ii) improving transparency, efficiency and accountability in procurement function; (iii) strengthening financial reporting and accountability mechanisms in the company; (iii) setting up systematic consumer feedback and social accountability measures in Severelectro to track whether project interventions lead to a perceived improvement in its services and overall client satisfaction, and ensure an iterative dialogue with consumers over the course of the project, and (iv) establishing a performance-based management system in the company.

IV. Safeguard Policies that might apply

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V. Financing (in USD Million)

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VI. Contact point

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