

SIGAR

**Special Inspector General for
Afghanistan Reconstruction**

SIGAR Audit 13-7

Afghanistan's National Power Utility: Commercialization Efforts Challenged by Expiring Subsidy and Poor USFOR-A and USAID Project Management



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SIGAR

Special Inspector General for Afghanistan Reconstruction

WHAT SIGAR REVIEWED

Since 2008, the Afghan government has identified improvements to its energy sector as a top priority, including increasing revenues and reducing losses from power generation through distribution. Collectively, these initiatives are referred to as commercialization. Since 2009, the U.S. government has obligated almost \$88 million to help the Afghan government commercialize Da Afghanistan Breshna Sherkat (DABS), its national power utility. DABS operates and manages electric power generation, import, transmission, and distribution services throughout Afghanistan. U.S. government projects funded by U.S. Forces-Afghanistan (USFOR-A) and the U.S. Agency for International Development (USAID) focus on helping DABS increase cost recovery, reduce losses, and build its capacity to manage, operate, and maintain a national power system. To date, USFOR-A and USAID have focused their efforts in Kabul, Kandahar, and Helmand provinces, and the first objective focuses on the self-sufficiency of DABS-Kabul because there is a lack of reliable, available data for other directorates—such as data on revenues and losses. This report is the second of two reports on U.S. efforts to assist in the commercialization of DABS. SIGAR evaluated (1) the extent to which U.S. assistance contributed to DABS-Kabul's goal of becoming self-sufficient and (2) USFOR-A and USAID management of commercialization projects.

WHAT SIGAR RECOMMENDS

SIGAR recommends that the Commanding General for USFOR-A Regional Command-Southwest work with DABS to finalize the installation schedule for the equipment. SIGAR also recommends that the USAID Mission Director for Afghanistan require that USAID-funded systems are coordinated with DABS Corporate and consistent nationwide. In commenting on a draft of this report, USFOR-A concurred with the recommendation. USAID also concurred, but disagreed with some findings. The U.S. Army Corps of Engineers provided technical comments. Agency comments are reproduced in appendices III and IV.

April 2013

Afghanistan's National Power Utility: Commercialization Efforts Challenged by Expiring Subsidy and Poor USFOR-A and USAID Project Management

SIGAR AUDIT 13-7

WHAT SIGAR FOUND

Although USAID investments resulted in some commercialization successes for DABS-Kabul in recent years, it is not able to pay its bills without an Afghan government subsidy set to expire in 2014. For example, with the assistance of a \$53 million project funded by USAID to assist in the commercialization of DABS-Kabul, cash collections increased by nearly 60 percent. However, DABS-Kabul—one of the best performing electricity directorates in all of Afghanistan—is still operating at a financial loss.

Further, USFOR-A and USAID have provided nearly \$88 million to assist in the commercialization of DABS in Kabul, Kandahar, and Helmand, but poor management of commercialization projects by the agencies hindered U.S. efforts. For example, USFOR-A approved eight Commander's Emergency Response Program projects intended to help DABS decrease losses and increase revenues from electricity sold; these projects were designed to procure urgently needed electricity distribution equipment for Kandahar and Helmand. As identified in an interim report in December 2012, almost \$12.8 million of the equipment purchased by USACE-TAS—on behalf of USFOR-A—as part of Kandahar commercialization efforts was sitting unused in U.S. government-controlled storage. SIGAR also found no clear plans for the equipment's installation. Although this equipment approved and funded by USFOR-A arrived without an installation plan and was placed in storage, USFOR-A continued to approve projects for similar equipment without an installation plan. As a result, \$10.2 million of additional equipment for Helmand remains in storage without an approved plan for installation.

Moreover, USAID's decision to approve an expanded scope of work on a sole source basis may have inappropriately limited competition because there may have been other technically capable bidders. Finally, although USAID required its contractor to implement a billing system in Kandahar that was consistent and coordinated with systems in Kabul, USAID did not enforce these contractual requirements, allowing a different system to be installed in Kandahar that was later deemed a failure by USAID and DABS. As a result, USAID wasted nearly \$700,000 to implement the system in Kandahar, which will ultimately be replaced by the same system originally installed in Kabul.



SIGAR

**Office of the Special Inspector General
for Afghanistan Reconstruction**

April 18, 2013

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Dr. S. Ken Yamashita
USAID Mission Director for Afghanistan

This draft report discusses the results of an audit of the U.S. government's \$88 million dollar effort to assist in the commercialization of Afghanistan's national power utility, Da Afghanistan Breshna Sherkat (DABS). In general, we found that U.S. Agency for International Development (USAID) assistance made improvements at DABS-Kabul, but an expiring Afghan government subsidy makes the goal of realizing self-sufficiency uncertain. Additionally, poor management by U.S. Forces-Afghanistan (USFOR-A) and USAID hampered commercialization efforts.

The report makes two recommendations: (1) that the Commanding General, USFOR-A Regional Command-Southwest, work with stakeholders to finalize the installation schedule for \$10.2 million in equipment that currently remains in storage and (2) that the USAID Mission Director for Afghanistan require that USAID-funded systems are coordinated with DABS Corporate and consistent nationwide.

In commenting on a draft of this report, USFOR-A concurred with our recommendation. USAID also concurred, but disagreed with some of our findings. USFOR-A and USAID's comments are reproduced in appendices III and IV. The U.S. Army Corps of Engineers also provided technical comments, which we incorporated, as appropriate. SIGAR conducted this work under the authority of Public Law 110-181, as amended, and the Inspector General Act of 1978, as amended; and in accordance with generally accepted government auditing standards.

A handwritten signature in blue ink, appearing to read "John F. Sopko".

John F. Sopko
Special Inspector General
for Afghanistan Reconstruction

CC: The Honorable John Kerry, Secretary of State; The Honorable Chuck Hagel, Secretary of Defense; The Honorable James B. Cunningham, U.S. Ambassador to Afghanistan; General Lloyd J. Austin III, Commander, U.S. Central Command

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ABBREVIATIONS & ACRONYMS

CERP	Commander's Emergency Response Program
DABS	Da Afghanistan Breshna Sherkat
DABM	Da Afghanistan Breshna Moassasa
KESIP	Kabul Electricity Services Improvement Program
LBG/B&V	Louis Berger Group Inc/Black & Veatch Special Projects Corp Joint Venture
PTEC	Power Transmission Expansion and Connectivity
TO 22	Task Order 22
USACE-TAS	U.S. Army Corps of Engineers–Afghanistan Engineer District South
USAID	U.S. Agency for International Development
USFOR-A	U.S. Forces–Afghanistan

Since 2008, the Afghan government has identified improvements to its energy sector as a top priority and, for that reason, has developed strategies and goals to increase its electrical sector efficiencies.¹ To accomplish these goals, the Afghan government set targets to increase revenues and reduce its losses from power generation through distribution. Collectively, these initiatives are referred to as commercialization. In support of these initiatives, the U.S. government has obligated almost \$88 million since 2009 to help the Afghan government commercialize its national power utility, Da Afghanistan Breshna Sherkat (DABS).² DABS operates and manages electric power generation, import, transmission, and distribution services throughout Afghanistan. The U.S. government's commercialization efforts focus on assisting DABS to increase cost recovery, reduce losses,³ and build its capacity to manage, operate, and maintain a national power system. U.S. Forces-Afghanistan (USFOR-A) and the U.S. Agency for International Development's (USAID) have implemented U.S. government commercialization efforts, and, to date, have focused their efforts in Kabul, Kandahar, and Helmand provinces.⁴

The objectives of this audit were to evaluate

- the extent to which U.S. assistance contributed to the DABS-Kabul goal of becoming self-sufficient, and
- USFOR-A and USAID management of commercialization projects.

We conducted our audit work in Kabul and Kandahar, Afghanistan, and Washington, D.C., from July 2012 to March 2013, in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. This audit was performed by SIGAR under the authority of Public Law 110-181, as amended, and the Inspector General Act of 1978, as amended. A discussion of our scope and methodology is included in appendix I.

BACKGROUND

According to Afghanistan's National Priority Program, DABS' mission is to acquire, operate, and maintain the equipment and systems needed to finance, generate, supply, and expand electricity to all areas of Afghanistan.⁵ DABS is an independent, but still government-controlled, corporate entity created in 2009 from Da Afghanistan Breshna Moassasa (DABM), which was the national utility within the Ministry of Energy and

¹The 2008 Afghanistan National Development Strategy emphasized operational efficiency as the number one priority in the energy sector. Developed by the Government of Afghanistan, the document lays out a 5-year plan to address major development challenges facing the country. The Afghanistan National Development Strategy sets the following issue area priorities: agriculture, security, education, governance, health, private sector, roads, infrastructure (energy and water), and social protection.

²For our audit, we defined "commercialization" as U.S. government efforts to assist DABS to increase revenues, decrease losses, and become a self-sustaining entity.

³Commercialization includes efforts to reduce technical and commercial losses in the distribution process; throughout the report, we use "losses" to refer to both types. Technical losses refer to differences in the amount of energy purchased by a utility and the amount of energy consumed or stored by the utility; these losses often occur as a result of poorly maintained or aging equipment/infrastructure and overloading. Examples of commercial (or non-technical) losses include differences in the amount of energy consumed and the amount billed (unbilled energy), and energy billed and energy paid (unpaid energy).

⁴Our first objective focuses on the self-sufficiency of DABS-Kabul because there is a lack of reliable, available data for other directorates—such as data on revenues and losses.

⁵Government of Afghanistan, National Priority Programs, Economic and Infrastructure Development Cluster, July 2010.

Water.⁶ DABS' headquarters (DABS Corporate) is located in Kabul and it maintains regional departments in Kabul, Parwan, Kunduz, Balkh, Herat, Nangarhar, and Kandahar provinces, as well as 10 sub-regional offices, including an office in Helmand. Since 2009, the U.S. government has focused its commercialization efforts primarily in Kabul and, to a lesser extent, Kandahar and Helmand.

The goal of commercialization is to create an independently sustainable national power utility. A December 2008 World Bank⁷ report states that because investments made in Afghanistan's energy sector through 2008 focused primarily on emergency rehabilitation to meet basic needs, it was unreasonable to expect that resources had been efficiently utilized.⁸ Since 2008, however, the Afghan government has developed strategies and set goals to improve the energy sector. The 2008 Afghanistan National Development Strategy Energy Sub-sector Strategy emphasized operational efficiency as the number one priority and identified commercialization, investments in transmission and distribution, and repair and maintenance of all power assets as areas for improvements.⁹ As illustrated in table 1, short-term goals for the energy sub-sector include reducing technical losses to 27.5 percent and increasing revenue collections to 70 percent between 2010 and 2013. For 2013 through 2018, the goal is to further reduce technical losses to 20 percent and increase revenue collection to 85 percent.

Table 1 - Short-term and Intermediate-term Commercialization Goals for Energy Sub-sector

Issue	Short-Term ^a (2010-2013)	Intermediate-Term (2013-2018)
Corporate Governance	DABM operating on commercial basis; some areas in private hands	Management Contract for DABM (in whole or in parts)
Technical Losses	27.5%	20%
Collections	70% collection to billed ^b	85% collection to billed
DABM Commercialization	Complete commercialization; improve metering, billing & collection; implement management performance contract	Unbundle & privatize ^c

Source: SIGAR analysis of Afghanistan National Development Strategy, Energy Sector Strategy, February 2008.

Notes:

^aThe goals for the energy subsector were established in 2008, one year before DABS replaced DABM as Afghanistan's national power utility.

^bCollection to billed refers to energy revenue collections compared to energy billed to customers.

^cAccording to the Afghanistan National Development Strategy, unbundling is the separation of the utility into different operating units and privatization by sale of one or more of those units.

⁶DABS replaced DABM as the national power utility; DABM is no longer an entity within the Ministry of Energy and Water.

⁷The World Bank awarded a contract to MVV Consulting in October 2005 to assist in the restructuring of DABM—the national utility within the Ministry of Energy and Water—and to legally establish DABS as an independent, but still government-controlled, corporate entity. The project was completed on December 15, 2008.

⁸*Technical Assistance for Restructuring and Commercialization of Da Afghan Breshna Moassassa, Completion Report, Volume I – Main Report*, MVV Consulting, December 7, 2008.

⁹The Afghanistan National Development Strategy is a five-year strategy document developed by the Government of Afghanistan to address major development challenges facing Afghanistan. The Afghanistan National Development Strategy sets the following issue area priorities: agriculture, security, education, governance, health, private sector, roads, and infrastructure (energy and water) and social protection.

To help DABS achieve these goals, the U.S. government has obligated nearly \$88 million on commercialization projects since September 2009.¹⁰ Of this amount, the USAID obligated almost \$61 million in Economic Support Funds on two contract task orders and one grant for commercialization efforts in Kabul and Kandahar.¹¹ For Kabul-based efforts, USAID awarded a \$53 million dollar task order to support commercialization of DABS-Kabul through the Kabul Electricity Services Improvement Project (KESIP)¹² and a grant to Etisalat for more than \$670,000 to support DABS-Kabul's revenue collections via mobile bill payment.¹³ For Kandahar-based efforts, USAID awarded Task Order 22 (TO 22) to Louis Berger Group Inc/Black & Veatch Special Projects Corp Joint Venture (LBG/B&V) for more than \$6.8 million to support various commercialization activities—such as developing a customer meter installation plan, installing boundary meters, and performing baseline studies related to revenues and losses—for DABS-Kandahar.

These three commercialization projects have been completed and USAID is not currently funding any commercialization projects in Afghanistan. However, USAID plans to provide \$157 million to DABS in direct assistance between 2013 and 2016—as part of its 3-year \$814 million Power Transmission Expansion and Connectivity (PTEC) program—to assist in commercialization and capacity building. According to USAID officials, KESIP will be used as a model under the PTEC project to build on achievements in Kabul and apply them to other regions of Afghanistan. The Electricity Commercialization Program under PTEC will be a 3-year program that will include continued commercialization activities in Kabul and Kandahar, and begin activities in Jalalabad, Mazar-e Sharif, and Herat.

In addition to USAID commercialization projects, USFOR-A has obligated \$27.3 million in Commander's Emergency Response Program (CERP) funds to purchase equipment needed to rebuild, repair, and expand current electrical distribution grids for areas in Kandahar and Helmand. The U.S. Army Corps of Engineers-Afghanistan Engineer District South (USACE-TAS) implements these projects for USFOR-A. Table 2 shows the three completed USAID commercialization projects funded by the Economic Support Fund and the eight USFOR-A commercialization projects funded with CERP.

Table 2 - DABS Commercialization Projects

Funding Agency	Project	Location (Province)	Description	Period of Performance	Obligated Amount
USAID	KESIP	Kabul	Commercialization activities	5/5/2009-3/31/12	\$53,025,290
USAID	Kandahar Commercialization (Task Order 22) ^a	Kandahar		5/10/09-12/31/11	\$6,875,436

¹⁰Not all contracts discussed in this report have been closed out and invoices are still being paid. Therefore, to ensure consistency in language we only identify dollars obligated by each agency for each project, rather than total dollars spent.

¹¹The Economic Support Fund promotes the economic and political foreign policy interests of the United States by providing assistance to allies and countries in transition to democracy, supporting the Middle East peace negotiations, and financing economic stabilization programs, frequently in a multi-donor context. USAID, with overall foreign policy guidance from the Department of State, implements most Economic Support Fund programs.

¹²Tetra Tech ES, Inc. (Tetra Tech) performed the work required under KESIP.

¹³Etisalat is a telecommunications company with operations in many countries throughout the world, including Afghanistan.

Table 2 - DABS Commercialization Projects

Funding Agency	Project	Location (Province)	Description	Period of Performance	Obligated Amount
USAID	Etisalat Afghanistan	Kabul ^b	Support Etisalat in mobile electricity bill payment	12/1/11-12/31/12	\$676,110
USFOR-A	Kandahar City Starter Kit 1	Kandahar	The near term increase and improved reliability of electrical power in the Kandahar area.	8/13/10-3/25/12	\$7,446,712 ^c
	Kandahar City Starter Kit 2			7/20/11-3/19/12	
USFOR-A	Pashmul Completion Kits	Kandahar	Purchase materials for new digital, individual metered connections to homes and businesses.	9/29/11-11/30/12	\$2,843,564 ^c
USFOR-A	Maiwand Completion Kits	Kandahar	Purchase materials for new digital, individual metered connections to homes and businesses.	9/29/11-11/30/12	\$2,704,128 ^c
USFOR-A	Spin Boldak Completion Kits	Kandahar			\$3,232,527 ^c
USFOR-A	Sangin Completion Kits	Helmand		9/28/11-12/30/12	\$2,843,564 ^c
USFOR-A	Musa Qa'leh Completion Kits	Helmand			\$2,704,128 ^c
USFOR-A	Hyderabad Completion Kits	Helmand			\$2,704,128 ^c
USFOR-A	Tangi Completion Kits	Helmand			\$2,843,564 ^c
Total					\$87,899,151

Source: SIGAR analysis of USFOR-A, USACE-TAS, and USAID data.

Notes:

^aThe initial task order scope of work cites providing technical assistance, training, and contract advisory support to DABS-Corporate. Modification 1 to the Task Order changed the scope of work to providing technical assistance to DABS-Kandahar.

^bThe initial grant cites supporting Etisalat in mobile electricity bill payment in Kandahar. Modification 1 to the grant changed the implementation area from Kandahar to Kabul.

^cRepresents amount of CERP funds transferred from USFOR-A to USACE-TAS through a Military Interdepartmental Purchase Request (MIPR), rather than amount obligated to the contracts by USACE-TAS.

In the course of fieldwork for this audit, we identified two issues that warranted immediate attention. First, we identified in an earlier report that almost \$12.8 million of the equipment purchased by USACE-TAS, for USFOR-A, as part of Kandahar commercialization efforts was sitting unused in U.S. government controlled storage. We also found no clear plans for the equipment's installation. Additionally, we found that USAID paid a contractor the full allowable fee on a task order, despite the contractor's failure to complete 26 of the 34 required

deliverables. As a result, we issued an interim report in December 2012 notifying USFOR-A Commanders, and the USAID Mission Director for Afghanistan of our findings.¹⁴ In that report, we recommended that USFOR-A determine whether \$12.8 million of equipment procured for Kandahar can and should be installed in Kandahar. If so, we recommended that USFOR-A develop a plan for the equipment's installation. If not, we recommended that USFOR-A should determine other uses for the equipment. We also recommended that USAID complete a comprehensive assessment of task order deliverables and contractor performance and, using results of this assessment, negotiate the appropriate fixed fee and seek reimbursement for any fee paid in excess of the negotiated amount. Both USFOR-A and USAID concurred with our recommendations and are taking steps to address them.

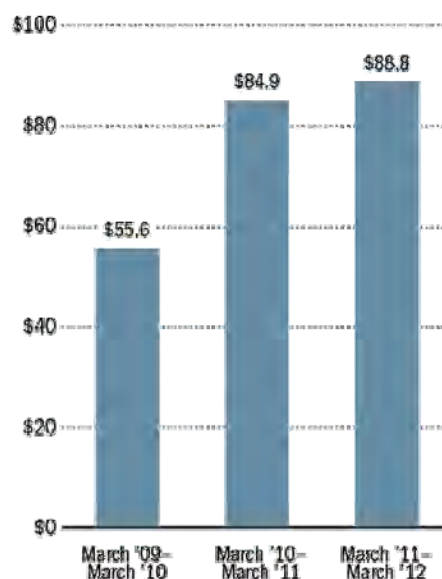
Additionally, in the course of our work we brought an issue to USACE-TAS' attention which resulted in the return of more than \$1 million in unspent funds to USFOR-A. USFOR-A transferred approximately \$7.4 million in CERP funds to USACE-TAS to buy equipment needed for a project in Kandahar. USFOR-A used a Military Interdepartmental Purchase Request¹⁵ to transfer the funds to USACE-TAS. However, the final invoice for the project from the contractor showed that USACE-TAS only paid approximately \$6.2 million for the equipment. We brought this to USACE-TAS' attention and, as a result, it returned \$1.16 million to USFOR-A on December 20, 2012. In addition to the \$1.16 million already returned, up to an additional \$3.14 million for 7 remaining projects in other areas of Kandahar and Helmand may be returned to USFOR-A because USACE-TAS did not require the funds to complete the remaining projects. USACE-TAS officials indicated that they are waiting to pay final invoices before returning these funds.

USAID ASSISTANCE LED TO IMPROVEMENTS TO DABS-KABUL BUT EXPIRING SUBSIDY MAKES SELF-SUFFICIENCY UNCERTAIN

USAID assistance to DABS-Kabul helped the directorate reduce its losses and increase revenues, yet DABS-Kabul still cannot sustain itself without an Afghan government subsidy set to expire in 2014. Indeed, USAID's efforts to commercialize DABS-Kabul—through the \$53 million KESIP—improved revenue collection by nearly 60 percent, from approximately \$56 million to nearly \$89 million. Figure 1 shows the annual increase in cumulative cash collections from March 2009 to March 2012.

Tetra Tech—the contractor for KESIP—coordinated the installation of approximately 50,000 customer meters

Figure 1 - DABS-Kabul Cumulative Cash Collection (in millions)



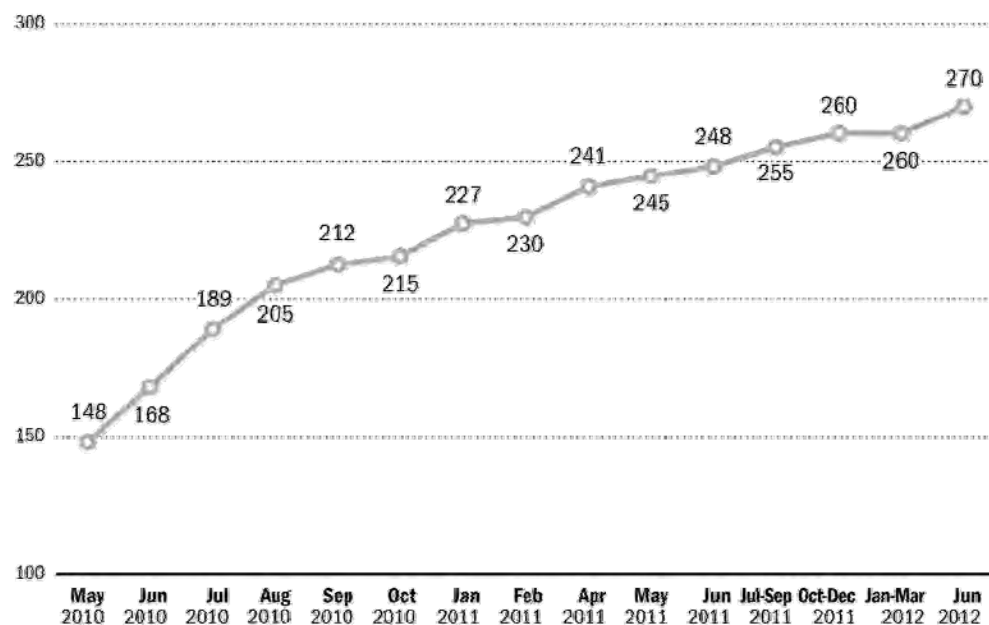
Source: SIGAR analysis of Kabul Electricity Service Improvement Program Final Report, Tetra Tech ES, Inc, June 1, 2012

¹⁴SIGAR 13-2, *Afghanistan's National Power Utility: \$12.8 Million in DOD-Purchased Equipment Sits Unused and USAID Paid a Contractor for Incomplete Work*, December 2012.

¹⁵A Military Interdepartmental Purchase Request is used by a requesting agency, in this case USFOR-A, to place an order for supplies or non-personal services with a servicing agency, in this case USACE-TAS. Two kinds of Military Interdepartmental Purchase Requests are available, Category I and II. All eight of the CERP projects approved to purchase electrical equipment are in Category I.

used for billing energy use, and worked with DABS-Kabul to design and implement a program to enumerate DABS-Kabul customers into a computerized billing system. As shown in Figure 2, from May 2010 to June 2012, DABS-Kabul increased the number of enumerated customers to a total of 270,000.

Figure 2 - DABS-Kabul Customers Enumerated Into Computerized Billing System (in thousands)



Source: SIGAR analysis of KESIP monthly reports, quarterly reports, and final report

Despite these improvements, data shows that DABS-Kabul is not a self-sufficient power utility. For example, a preliminary financial statement developed for DABS-Kabul showed that the directorate operated at a financial loss; however, as a result of the Afghan government subsidy, DABS-Kabul's financial statement shows a positive cash flow.¹⁶ The financial statement states that the subsidy is scheduled to expire at the end of March 2014, and without the subsidy, DABS-Kabul will be unable to pay its bills.¹⁷

In response to a draft of this report, USAID stated that phasing out fuel subsidies was part of the agreement between the Ministry of Finance and DABS from DABS's inception and has been a part of its operational planning process. To fill the revenue gap left by the planned reduction in subsidies, USAID also stated that increasing customer rates for energy consumption as well as further decreasing losses will eventually bring revenue in line with operational costs. While such efforts may result in revenue/cost alignment, whether they occur in time to offset the expiring subsidy remains questionable.

¹⁶Tetra Tech completed this assessment in January 2012, and notes that the financial statement was an internal exercise, and that DABS was not yet at a stage where it was ready to prepare 'pro forma' financials.

¹⁷The Government of Afghanistan's 1390 budget cites \$63.4 million allocated to DABS.

Further, DABS-Kabul's technical and commercial losses remain at about 38 percent. According to a USAID energy sector specialist, losses by a utility exceeding 20 percent indicate problems such as theft and lack of funds for maintenance. Similarly, a report prepared for the World Bank links losses exceeding 30 percent with poor operational and financial performance.¹⁸

POOR PROJECT MANAGEMENT HAMPERED COMMERCIALIZATION EFFORTS

Poor project management by USFOR-A and USAID hampered their efforts to help commercialize DABS in Helmand, Kandahar and Kabul. Specifically, USFOR-A purchased equipment for use in Helmand without an installation plan, and the equipment was placed in storage, despite its previous purchase of similar equipment—also approved without an installation plan—that was already in storage in Kandahar. Additionally, USAID's poor project management resulted in a sole-source award that may have inappropriately limited competition, and USAID failed to enforce a key contractual requirement that resulted in almost \$700,000 in wasted funds.

USFOR-A Purchased \$10.2 Million in Equipment that Remains Unused in Helmand

In addition to the \$61 million that USAID provided for its three commercialization projects, USFOR-A provided \$27.3 million in CERP funds for urgently needed electricity distribution equipment, including starter kits and completion kits for eight projects in Kandahar and Helmand.¹⁹ USFOR-A requested that USACE-TAS execute the contracts to purchase the equipment. USACE-TAS procured the equipment from a contractor, Jubaili Brothers, at a total cost of about \$23 million. Approximately \$12.8 million was used to buy starter and completion kits for projects in Kandahar and almost \$10.2 million was used to buy kits for projects in Helmand. According to USACE-TAS, it received all of the equipment for Kandahar and Helmand.

While all of the equipment was delivered, it was immediately placed in storage—and remained there, as of December 2012—because neither USFOR-A nor DABS completed a finalized plan for installation and DABS lacked the capacity to install and manage the equipment. USFOR-A approved the first project for Kandahar starter kits in April 2010 and USACE-TAS awarded the first contract four months later. The contract required the equipment to arrive no later

Donor Coordination in the Afghanistan Energy Sector

The Inter-Ministerial Commission on Energy was created by Afghan presidential decree in November 2006 to provide oversight for Afghanistan's energy sector policy and infrastructure. In the commission's role of coordinating international support, participants from Afghan ministries, the U.S. government, the World Bank, the Asian Development Bank, and other international donors met on a monthly basis. Both SIGAR and the U.S. Government Accountability Office found the commission to be an effective coordination body and a potential model for enhancing U.S. reconstruction effort coordination while it was active. However, in mid-2012, the commission stopped meeting, leaving energy sector coordination reliant upon ad-hoc efforts. The Afghan government has requested funding from the Asian Development Bank to reassemble the commission, and the Bank anticipates providing two years of funding beginning in early 2013.

¹⁸*Reducing Technical and Non-Technical Losses in the Power Sector: Background Paper for the World Bank Group Energy Sector Strategy*, July 2009, pg 8.

¹⁹Starter kits and completion kits are made up of equipment to improve the electricity distribution infrastructure. According to USACE-TAS officials, and based on our review of the required equipment, the two kits are virtually identical in content and include items such as meters, transformers, poles, and trucks.

than December 2010.²⁰ However, as we previously reported,²¹ neither USFOR-A nor DABS-Kandahar completed an installation plan prior to the purchase, and DABS-Kandahar lacked the capacity to install the equipment.²² As a result, the \$12.8 million of equipment remains in storage at USACE-TAS' Shorandam Industrial Park.²³ Yet, while the starter kits sat in storage in Kandahar, USFOR-A approved seven additional purchases of similar equipment for Kandahar and Helmand without requiring an achievable plan for installation. Figure 3 shows the timeline of the continued approval of CERP projects for equipment that did not have an installation plan.

Figure 3 - Timeline of CERP Equipment Purchases



Source: SIGAR analysis of CERP approval documentation and USACE-TAS contract award documentation.

Similar to what we identified in our interim report for equipment in Kandahar, none of the \$10.2 million in equipment has been installed in Helmand, and no final installation plan exists. USACE-TAS received about 90 percent of the equipment for Helmand and turned it over to DABS-Helmand in September 2012.²⁴ According to USFOR-A officials, the Helmand Provincial Reconstruction Team is in discussion with DABS-Helmand to develop an installation schedule.²⁵ The Helmand Provincial Reconstruction Team developed a draft schedule after the turnover of the equipment, with a more “refined” schedule expected in early 2013.²⁶ According to Helmand Provincial Reconstruction Team officials, senior DABS-Helmand officials have assured USFOR-A that DABS-Helmand has the capability to manage and install the completion kits at their intended locations. A

²⁰The contract allowed additional time - up to 240 days - for some long lead items.

²¹SIGAR 13-2.

²²USAID and Asian Development Bank officials independently verified this assessment.

²³Shorandam Industrial Park is a U.S. facility housing a power plant supplying electricity, and is located just outside of Kandahar City. According to USACE, the facility will be turned over to the Government of Afghanistan in December 2014. SIGAR auditors and an engineer inspected the equipment in storage in September 2012. The equipment appeared to be well-maintained within the storage facility and USACE-TAS had a process and internal controls for approving requests and issuing equipment to DABS-Kandahar on an as-needed basis.

²⁴In its formal comments to this report, USACE-TAS stated that all of the equipment has been received and turned over to DABS-Helmand.

²⁵The Helmand Provincial Reconstruction Team is led by the United Kingdom and is supported by the United States, United Kingdom, Denmark, and Estonia in helping the Afghan government deliver governance and improved development across Helmand province. The Helmand Provincial Reconstruction Team has an embedded representative from USFOR-A that works directly with DABS-Helmand.

²⁶According to the draft schedule, installation was to commence in December 2012 and will be completed in March 2014.

Memorandum of Sustainment dated June 28, 2011 between the Commander of USFOR-A Regional Command-Southwest²⁷ and the Director of DABS-Helmand states:

“The Director of DABS-Helmand agrees to be responsible for the operation and maintenance of the Musa Qal’eh, Sangin, Hyderabad, and Tangi Completion kits. The operation and maintenance will begin once the Completion Kits are transferred to [DABS-Helmand] and will include staffing, routine maintenance, and supplies for the kits.”

However, DABS-Helmand requested training from USFOR-A and USACE-TAS to increase technical capacity required for installation, and USFOR-A and USACE-TAS intend to provide lineman training, training on use of completion kit vehicles, surveying, and project management.

Further, as we previously reported, the meters procured as part of the eight starter and completion kits have a warranty of 26 months from the date of dispatch from the manufacturer.²⁸ Given the amount of time that has already lapsed, if the meters are found to be faulty following their eventual installation, the warranty may have expired, potentially making it more difficult to obtain replacements from the manufacturer without incurring additional expense.

USAID Issued a Sole Source Award that May Have Inappropriately Limited Competition

USAID awarded TO 22 to the LBG/B&V on May 10, 2009²⁹ to provide expert technical assistance, training, and contract advisory support to DABS Corporate in Kabul. TO 22 was initially valued at \$3.4 million and had a period of performance of May 10, 2009 to May 9, 2011. However, in August 2009, 3 months after TO 22 was awarded, USAID’s Office of Infrastructure, Engineering, and Energy requested that the task order be expanded and modified to include commercialization efforts in Kandahar.³⁰

The Federal Acquisition Regulation generally requires contracting officers to allow for full and open competition for government acquisitions. However, both federal regulations and the USAID Acquisition Regulation allow for some exceptions. For example, USAID allows exceptions when the contracting officer determines that full and open competition would impair or otherwise have an adverse effect on programs conducted for the purposes of foreign aid, relief, and rehabilitation.³¹ In order to use this “foreign impairment” exception and limit competition, the contract file must include appropriate explanation and support justifying the award without full and open competition. To justify the modification of TO 22 for the inclusion of additional commercialization work in Kandahar without full and open competition, USAID’s Office of Infrastructure, Engineering, and Energy prepared a Justification for Other than Full and Open Competition. The Justification cited the foreign impairment exception and stated that the additional work for DABS-Kandahar was a direct extension of work already underway at DABS-Kabul under TO 22. The Justification further stated that the proposed work at DABS-Kandahar “will expand the same commercialization concepts...and will take advantage of staff and processes that are already in place.” USAID officials in the acquisitions, program, and legal offices subsequently

²⁷The area of responsibility for Regional Command-Southwest is Helmand and Nimroz provinces.

²⁸SIGAR 13-2.

²⁹In August 2006, USAID awarded a 5-year, single source indefinite quantity contract with a \$1.405 billion ceiling to the LBG/B&V to implement the Infrastructure and Rehabilitation Program in Afghanistan. Between August 25, 2006 and August 24, 2011, USAID issued 27 cost-plus-fixed fee task orders under the contract to LBG/B&V, including TO 22 (contract number 306-I-22-06-00517-00).

³⁰This office is now known as the Office of Economic Growth and Infrastructure.

³¹USAID Acquisition Regulation 706.302-70.

approved the sole source justification and expanded scope of work, allowing LBG/B&V to implement Kandahar commercialization under Modification 1 to TO 22. As a result, the value of TO 22 increased by \$940,000 to more than \$4.3 million.

Although USAID officials justified the expanded scope of work for TO 22 by stating that the work was an extension of existing work by LBG/B&V in Kabul, an analysis of the original scope of work for TO 22 found that it did not include Kabul commercialization support services. Rather, TO 22 originally called for expert technical assistance and contract advisory support to DABS Corporate for the potential award of a management contract to run DABS-Kabul.³² In fact, another contractor, Tetra Tech ES, Inc. (Tetra Tech), was actually providing Kabul commercialization services under USAID's KESIP at that time.³³ Additionally, the USAID Justification for Other than Full and Open Competition stated that using a sole source procurement would allow the contractor to take advantage of staff and processes already in place; however, LBG/B&V did not have the staff in place to immediately begin Kandahar commercialization activities. In fact, LBG/B&V did not even conduct a "kick-off" meeting with DABS-Kandahar managers until late August 2010—a year after the modification to TO 22 that added Kandahar commercialization activities. Similarly, although LBG/B&V hired a Task Order Manager in early December 2010, he did not arrive in Kandahar until August 2011, 2 years after the modification.

Additionally, even when the foreign impairment exception is used, USAID requires contracting officers to seek bids from as many potential offerors as is practicable. However, despite the existence of other potential technically capable bidders—for reasons contained in the sole source justification discussed above—USAID did not seek offers from these bidders, including the USAID contractor already performing commercialization activities for DABS in Kabul. Specifically, in May 2009—only 3 months prior to the modification of TO 22 to include Kandahar commercialization activities—USAID awarded very similar work for commercialization activities in Kabul under an existing contract vehicle in which five contractors were allowed to compete for the work. Two offerors responded to the solicitation, neither of which were LBG/B&V. As the Government Accountability Office reported in July 2010, competition is a critical tool for achieving the best return on the government's investment.³⁴ Although at least two other potential offerors existed, USAID officials requested and approved Kandahar commercialization activities on a sole source basis through a modification to TO 22.

Poor Planning and USAID's Failure to Enforce a Key Contractual Requirement Resulted in Nearly \$700,000 in Wasted Funds

A sustainable energy distribution business requires reliable and integrated billing and collection systems. These systems are key to improving revenues, reducing costs, and ensuring accurate reporting. To assist with the development of such systems in Afghanistan, USAID required Tetra Tech (the contractor for KESIP) to implement billing and collection systems in Kabul, and LBG/B&V (the contractor for TO 22) to implement "systems, procedures and management operations [that] are consistent between Kabul and Kandahar."³⁵ Beyond calling for consistent systems, the statements of work for KESIP and TO 22 did not specify what billing systems should be used in either of the two provinces.

³²Documentation cited in this report often used the term 'Kabul Electricity Directorate.' However, we use 'DABS-Kabul' throughout to convey that we are referring to the DABS regional office in Kabul.

³³Although PA Government Services was originally awarded the contract, a Novation Agreement changed the contractor to Tetra Tech in November 2010.

³⁴U.S. Government Accountability Office, GAO 10-833, *Opportunities Exist to Increase Competition and Assess Reasons When Only One Offer is Received*, July 2010.

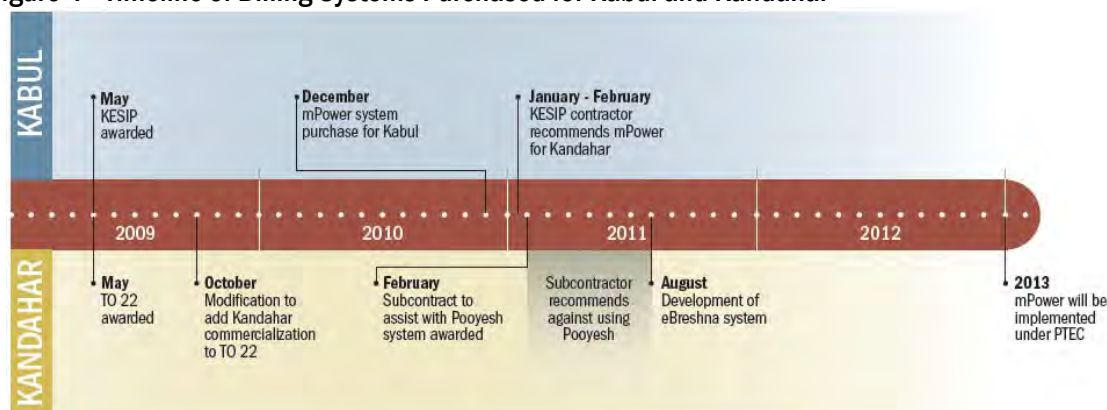
³⁵This requirement was deleted in Modification 3. However, Modification 3 was signed in October 2011, only 2 months before the end of the task order.

Despite the requirement that billing systems be consistent between the two projects, Tetra Tech and LBG/B&V installed inconsistent systems in Kabul and Kandahar. Shortly after USAID awarded TO 22, LBG/B&V informed USAID that an existing Farsi-language system,³⁶ the “Pooyesh” billing system,³⁷ had most of the basic functionality needed in a billing and collection system and that the system could improve short-term billing and collection efforts and possibly longer-term improvements with minimum programming effort. Based on these statements, LBG/B&V advised USAID that the Pooyesh system should be used in Kandahar.³⁸ Subsequently, USAID funded the purchase of the equipment, and LBG/B&V installed the Pooyesh system in Kandahar.³⁹

At the same time, Tetra Tech had purchased and began implementing a different billing system, “mPower,” for DABS-Kabul. According to Tetra Tech officials, they recommended that LBG/B&V use the same system in Kandahar that was already purchased and being installed in Kabul. However, USAID and LBG/B&V decided not to implement mPower in Kandahar despite the recommendation and the contractual requirement that all new systems implemented in Kandahar be coordinated with Kabul.

After installing the Pooyesh system in Kandahar, LBG/B&V and USAID later found the billing system to be inadequate, antiquated, and incompatible with other billing systems. The subcontractor responsible for the installation of the Pooyesh system recommended replacing it and developing an entirely new system. USAID approved the replacement and the subcontractor ultimately began development and installation of a new system, called the “eBreshna,” in August 2011, at a cost of more than \$690,000.⁴⁰ However, USAID officials stated that the eBreshna system was never fully developed, and officials from DABS Corporate also highlighted problems with the eBreshna system in Kandahar, while touting the success of the mPower system in Kabul. Figure 4 shows the timeline of the purchase of billing systems in Kabul and Kandahar under KESIP and TO 22.

Figure 4 - Timeline of Billing Systems Purchased for Kabul and Kandahar



Source: SIGAR analysis of KESIP and TO 22 contract documentation and USAID planning documentation.

³⁶The two official languages of Afghanistan are Dari and Pashto; Farsi is the official language spoken in Iran. Pashto is spoken by approximately 50 percent of the Afghan population, most of whom are concentrated in southern and eastern Afghanistan, including Kandahar. Because Pooyesh is Iranian-based software, it utilizes a Farsi interface that is not compatible with the Pashto-speaking south.

³⁷Pooyesh, a billing and applications system written in Farsi, was in limited use by DABS in Afghanistan, but was not used in Kandahar.

³⁸Prior to 2011, the billing and collection system for DABS-Kandahar was not automated and billing and collection functions were manually performed. Under this paper based system, meter readers would log a reading into a customer log book, who would then take the log book to the bank to pay the bill to a DABS envoy, who would then issue a receipt.

³⁹LBG/B&V awarded a subcontract in February 2011 to assist with the required improvements to the Pooyesh system.

⁴⁰\$627,500 for the subcontract plus \$62,775 for the General & Administrative (G&A) and fee.

Because USAID did not enforce contractual requirements for the development and installation of consistent billing systems across locations, and more than 2 years after the mPower system was purchased for use in Kabul, USAID now plans to implement the mPower system in Kandahar under the PTEC program in fiscal year 2013. These actions resulted in the waste of nearly \$700,000 and delayed improvements that are critical to DABS becoming a self-sufficient entity. USAID also plans to implement the mPower system in Herat, Kunduz, Balkh, and Nangarhar Provinces as part of PTEC.

CONCLUSION

Since replacing DABM in 2009, DABS has made significant commercialization progress through increased revenues and decreased losses, particularly in Kabul as a result of USAID's \$53 million KESIP assistance. However, despite these gains, even DABS-Kabul—one of the highest performing provinces—cannot sustain itself without an annual Afghan government subsidy, set to expire in 2014. To achieve self-sufficiency, DABS must build on the gains made by DABS-Kabul under KESIP and expand successful and standardized commercialization efforts to other key areas. USFOR-A and USAID have executed projects and programs to assist DABS in areas outside of Kabul, but so far those efforts have been marred by a lack of planning and poor contract management that resulted in wasted U.S. funds. If the U.S. government follows through on its plan to invest an additional \$157 million in DABS commercialization efforts nationwide through its PTEC program—in addition to the hundreds of millions it plans to spend over the next several years to build critical energy sector infrastructure—it must ensure proper planning, decision making, and management when implementing efforts and that U.S. funds are effectively contributing to the creation of a self-sufficient DABS.

RECOMMENDATIONS

To ensure that purchased electrical equipment will be used to repair and expand electrical distribution grids, we recommend that the Commanding General for USFOR-A Regional Command-Southwest

- 1. work with DABS to finalize the installation schedule for the Helmand equipment, within the warranty period, if possible.**

This recommendation should be performed in coordination with USACE-TAS and the Helmand Provincial Reconstruction Team.

To ensure that U.S.-funded billing systems are consistent across Afghanistan, we recommend that the USAID Mission Director for Afghanistan

- 2. require that any system funded by the PTEC program is coordinated with DABS Corporate and consistent nationwide, wherever possible.**

AGENCY COMMENTS

We received written comments on a draft of this report from USFOR-A, USAID, and USACE and made revisions to the report, as appropriate.

USFOR-A concurred with our recommendation that it should work with DABS to finalize the installation schedule for the Helmand equipment within the warranty period. USFOR-A described the actions it is taking or plans to take to address the recommendation. USFOR-A's comments are presented in appendix III.

In commenting on the draft of this report, USAID disagreed with several of our statements. Most notably, USAID disagreed with our statement that DABS-Kabul self-sufficiency is uncertain because of expiring subsidies. USAID stated that phasing out the subsidies was part of the agreement with the Ministry of Finance and DABS

from inception, and removing the subsidies in favor of commercial viability is the goal of its partnership with DABS. To fill the revenue gap left by the planned reduction in subsidies, USAID also stated that increasing customer rates for energy consumption as well as further decreasing losses will eventually bring revenue in line with operational costs. While such efforts may result in revenue/costs alignment, we question whether those positive results can occur before the subsidies expire in 2014 and, therefore, believe that our finding that the self-sufficiency of DABS is questionable remains valid.

USAID concurred with our recommendation that it should require any system funded by the PTEC program to be coordinated with DABS Corporate and consistent nationwide. USAID provided a copy of the “Request for Proposal” for DABS commercialization, which stated that mPower will be the billing system used as USAID expands commercialization efforts into Herat, Kandahar, Nangarhar, and Balkh. With appropriate contract management and USAID’s assurance that any additional expansion includes similar requirements, USAID’s actions will meet the intent of our recommendation.

USAID’s comments and our responses are presented in appendix IV.

We also considered technical comments provided by the U.S. Army Corps of Engineers when finalizing the report, which we incorporated, as appropriate.

APPENDIX I - SCOPE AND METHODOLOGY

In July 2012, the Special Inspector General for Afghanistan Reconstruction (SIGAR) initiated an audit of U.S. government efforts to assist in the commercialization of Da Afghanistan Breshna Sherkat (DABS). Specifically, SIGAR evaluated (1) the extent to which U.S. assistance contributed to DABS-Kabul's goal of becoming self-sufficient and (2) USFOR-A and USAID management of commercialization projects. SIGAR issued an interim report in December 2012 to highlight issues related to DABS commercialization requiring immediate consideration prior to issuing this final audit report on the results of SIGAR's review.

To evaluate the extent to which U.S. assistance contributed to DABS-Kabul's goal of becoming self sufficient, we reviewed contract documentation and contractor deliverables for the Kabul Electricity Services Improvement Program (KESIP) and the Afghanistan National Development Strategy.

To evaluate USFOR-A and USAID management of commercialization projects, we reviewed relevant guidance, including the Federal Acquisition Regulation and the current Money as a Weapon System Afghanistan, dated March 2012. We reviewed contract documentation and disbursement and obligation data for KESIP, Task Order 22 (TO 22), and the eight Commander's Emergency Response Program (CERP) projects. We performed data reliability tests to determine the accuracy and completeness of the computer-processed data in the report by comparing CERP project files to Military Interdepartmental Purchase Request data provided by U.S. Forces-Afghanistan (USFOR-A) and U.S. Army Corps of Engineers-Afghanistan Engineer District South (USACE-TAS). We also compared U.S. Agency for International Development (USAID) disbursement and obligation data to TO 22 and KESIP contract and modification documentation. We determined that the data were sufficiently reliable for the purposes of the audit objectives. We reviewed USFOR-A's internal controls over CERP project files to determine whether CERP project documentation in the Combined Information Data Network Exchange database was complete. We reviewed documents in the period between July 2012 and January 2013.

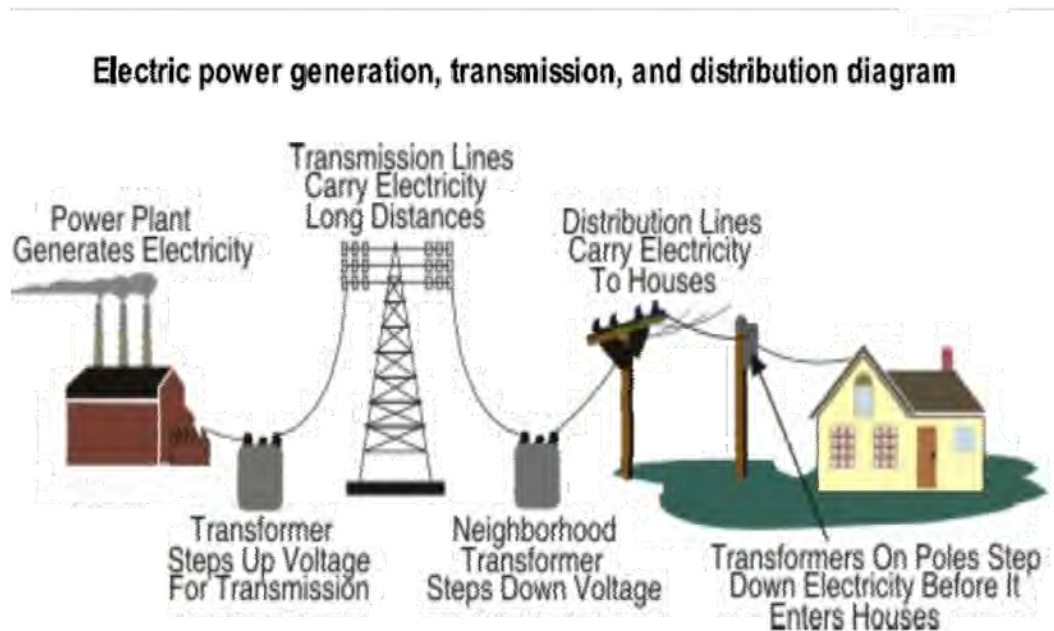
For both objectives, we interviewed officials at USAID Offices of Financial Management, Acquisition and Assistance, Economic Growth and Infrastructure, and Program and Project Development; Department of Defense Offices USFOR-A J9, USFOR-A J8, USFOR-A Regional Command-South, USFOR-A Regional Command-Southwest, USFOR-A Inspector General, and USACE-TAS. We also interviewed representatives from the World Bank, the Asian Development Bank, DABS Corporate, Tetra Tech ES, Inc., and current and former in-country Louis Berger Group Inc./Black & Veatch Special Projects Corp staff. We also viewed the equipment purchased by USACE-TAS with USFOR-A funds stored at the Shorandam Industrial Park outside of Kandahar City.

We conducted our audit work in Kabul and Kandahar, Afghanistan, and Washington, D.C., from July 2012 to January 2013, in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives. This audit was performed by SIGAR under the authority of Public Law 110-181, as amended, and the Inspector General Act of 1978, as amended.

APPENDIX II - LOSSES IN ENERGY DISTRIBUTION

The majority of energy losses occur in the distribution phase of energy flow to customers. Figure I shows how energy flows from generation to transmission and distribution.

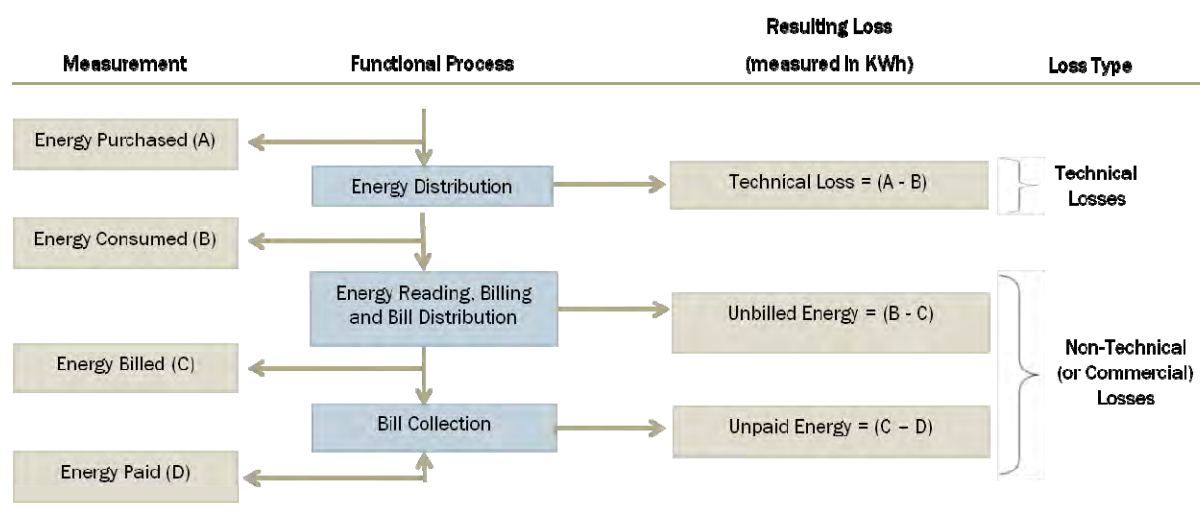
Figure I - Energy Flow from Generation to Distribution



Source: National Energy Education Development Project (Public Domain).

Losses in the distribution of energy occur for technical and non-technical (or commercial) reasons, and utilities must address both types simultaneously (not one or the other) to increase revenues and achieve full cost recovery. Figure 2 demonstrates where technical and non-technical losses occur in the distribution system.

Figure II - Losses in the Distribution System



Source: USAID document for the South Asia Regional Initiative for Energy

APPENDIX III - U.S. FORCES-AFGHANISTAN COMMENTS



HEADQUARTERS
UNITED STATES FORCES-AFGHANISTAN
KABUL, AFGHANISTAN
APO AE 09356

USFOR-A J9

28 March 2013

MEMORANDUM FOR Special Inspector General for Afghanistan Reconstruction (SIGAR),
2530 Crystal Drive, Arlington, Virginia 22202-3940

SUBJECT: SIGAR Audit 13-7, AFGHANISTAN'S NATIONAL POWER UTILITY;
COMMERCIALIZATION EFFORTS THREATENED BY EXPIRING SUBSIDY AND POOR
USFOR-A AND USAID PROJECT MANAGEMENT

1. USFOR-A concurs with SIGAR recommendation found on page 14 of this report: To ensure that purchased electrical equipment will be used to repair and expand electrical distribution grids, we recommend that the Commanding General for USFOR-A Regional Command Southwest work with DABS to finalize the installation schedule for Helmand equipment, within the warranty period, if possible. This recommendation should be performed in coordination with USACE-TAS and the Helmand Provincial Reconstruction Team.
2. The Deputy Commanding General for Support, USFOR-A, hosted a "Power Summit" on 12 March 2013 in Kabul to discuss USG support to DABS. At this meeting senior executives from DABS discussed their efforts to achieve commercial viability. USAID also briefed its plans to assist DABS achieve viability. The USFOR-A Joint Program Integration Office (JPIO) and USACE also participated in these discussions. This is just one instance of the ongoing efforts of USFOR-A and USAID to rectify this situation.
3. On 2 April 2013, the Deputy Commanding General of Regional Command Southwest will host a meeting of representatives from USFOR-A, USAID, JPIO, and USACE to further explore ways in which to rectify this situation (uninstalled completion kits in Helmand) and otherwise advance the commercialization of DABS.


BRYAN GROVES
COL, CA
USFOR-A J9

APPENDIX IV - U.S. AGENCY FOR INTERNATIONAL DEVELOPMENT COMMENTS



MEMORANDUM

April 13, 2013

TO: John F. Sopko
Special Inspector General for
Afghanistan Reconstruction (SIGAR)

FROM: Brooke Isham, Acting Mission Director

SUBJECT: Draft SIGAR Report titled, "Afghanistan's National Power Utility: Commercialization Efforts Threatened by Expiring Subsidy and Poor USFOR-A and USAID Project Management" (SIGAR Audit 13-7)

REFERENCE: SIGAR Transmittal email dated 03/22/2013

Thank you for providing USAID with the opportunity to review the subject draft audit report. Discussed below are our comments on the findings and recommendations in the report.

PART I: USAID'S GENERAL COMMENTS ON THE DRAFT REPORT

In four years, DABS has achieved impressive progress in both capacity and revenue generation leading to self-sustainability. DABS increased revenues by 68% between 2010 and 2012 and reduced electricity losses in Kabul from 60% to below 35%. These improvements, along with an adjustment in tariff rates, have increased DABS collected revenue from \$137 million in 2010 to \$204 million in 2012. This represents hundreds of millions of dollars saved in subsidies from US taxpayers and other donors - a remarkable achievement and impressive return on investment. It also represents a major step towards sustainability and full Afghan financing of their energy system. Continuing at this rate, and with appropriate continued support, DABS could reach commercial viability in three years.

Therefore, USAID strenuously objects to the title of this audit and a number of its findings. As we demonstrate below, DABS' success in commercialization is tied to, rather than threatened by expiring subsidy, and is a direct result of USAID's successful program management.

SIGAR
Comment 1

U.S. Agency for International Development
Great Massoud Road
Kabul, Afghanistan

Tel: 202-216-6288 / 0700-108-001
Email: kabulusaidinformation@usaid.gov
<http://afghanistan.usaid.gov>

Indeed, removing subsidy in favor of commercial viability is precisely the goal of our partnership with DABS. The establishment of a national utility and its continued progress toward full commercial viability within a few years would be viewed as a success story in any nation in which USAID works. That DABS has followed this trajectory in Afghanistan is particularly striking, given the well documented challenges USAID, other donors, and Afghan officials face.

The report fails to accurately assess its first objective: *"evaluate the extent to which U.S. Assistance contributed to DABS-Kabul goal of becoming self-sufficient."* Through Kabul Electrical Services Improvement Project (KESIP), USAID sought to help Kabul Electricity Directorate (KED) -- DABS' Kabul branch, called "DABS Kabul" in the SIGAR report -- improve its commercial operations so it could become a key part of a larger, commercially viable DABS.

SIGAR
Comment 2

KED is the largest single unit in DABS and accounted for 55% of overall DABS cash collections from electricity sales in fiscal year ending in March 2012. It has shown solid commercialization improvement and in 2012 had a collection rate over 85%, far exceeding the level of accomplishment laid out in the strategy referenced in the SIGAR report. The goal of this three year program was never full self-sufficiency, and KESIP's goal was successfully achieved. As a result, the report's assertion that KED is overly reliant on Afghanistan government subsidy to pay its bills is unsupported.

SIGAR
Comment 3

SIGAR
Comment 4

DABS already has demonstrated its growing capacity to manage projects. It has been working with the ADB's Program Management Unit within DABS to manage a transmission line project. In 2012, DABS used its own funds to finance and manage \$14.3 million of improvements to distribution systems in Uruzgan, Ghazni, and Kabul; upgrade of the transmission line from Sar-e-pul to Sheberghan, and procure 200,000 digital meters.

As the report documents, in just four short years, KED saw significant improvements in its commercial performance, in large part due to KESIP. Further deepening these accomplishments and extending them to other parts of DABS is key to ensuring their long-term sustainability that will require them to:

- a) Put in place corporate management and governance structures that ensure effective technical, financial, and investment planning to

expand and extend the system and improve quality of service to customers;

- b) Continue to reduce losses and improve metering, billing and collections to increase commercial performance toward international best practice; and
- c) Ensure that tariffs are adjusted to reflect full cost recovery, so improved commercial performance will ensure the financial resources required to support the planned investments in physical and human resources to increase supply and improve quality of service.

All of these priorities will be addressed in the course of implementing USAID's upcoming on-budget commercialization and capacity-building activity, a component of the larger Power Transmission Expansion and Connectivity (PTEC) project over the next three to four years.

Changing tariff rates is a gradual process that relies on economic analysis, political will, and public education. DABS did adjust the current multi-tiered tariff rate structure for 2012, a change that has led to a 10% increase in the weighted average charge per kWh billed to 10.8 cents. Ongoing and planned efforts focus exactly on this challenge, as DABS develops a full and accurate accounting of all its assets, including those received from the Ministry of Energy and Water.

USAID agrees that DABS faces significant challenges to ensure long-term sustainability as a modern, effective public electric utility. Nevertheless, it has made significant strides in addressing the complex set of challenges inherent in defining and ensuring that sustainability. The next stage of USAID assistance -- the planned \$157 million on-budget DABS commercialization and corporate capacity component of the PTEC program -- has been designed in close collaboration with DABS to continue fostering the creation of a self-sufficient organization.

A key feature of USAID's on-budget assistance approach is the direct link between DABS corporate governance and the conditions of assistance. Effective corporate governance is essential to addressing problems of weak corporate management systems, high losses, low revenues and widespread corruption in the sector identified in earlier years and is crucial to sustainability.

USAID's assistance to DABS (though KESIP) ended in April 2012, but their management consistently and effectively has continued to implement and extend the improved commercial operations initiated under that program. This development resulted in a 61% increase in

collected revenue nationwide for the first eight months of the Afghan fiscal year ending in March 2013, when contrasted to the same period the prior year.

DABS has made significant positive accomplishments in the four years since it was established, but building a modern electricity utility and ensuring its sustainability will take many more years. It is inaccurate to suggest that KED “. . . is not able to pay its bills without an Afghan government subsidy set to expire in 2014.” The planned declining subsidy was not used by KED at all in 2012 -- KED successfully maintained and improved the quality of service in Kabul in 2012 while operating without the subsidy, ahead of schedule.

SIGAR
Comment 5

PART II: COMMENTS ON SIGAR'S RECOMMENDATION

To ensure that U.S.-funded billing systems are consistent across Afghanistan, we recommend that the USAID Mission Director for Afghanistan require that any system funded by the PTEC program is coordinated with DABS Corporate and consistent nationwide, wherever possible.

USAID Comments:

The Mission concurs with this recommendation and already has taken steps to ensure systems funded by the PTEC program are coordinated with DABS Corporate and consistently implemented nationwide. This requirement is specifically contained in the Request for Proposals for the On-budget DABS Commercialization Program Part 1 for Distribution, issued by DABS on March 9, 2013 (Attachment 1). Therefore, USAID requests the recommendation be closed upon report issuance.

SIGAR
Comment 6

SIGAR Response to USAID Comments of April 13, 2013

1. In response to USAID's comments, we revised the title of the report to more accurately reflect the challenges associated with making DABS self-sufficient. As noted in the report, DABS must continue and expand the gains it made in Kabul as a result of USAID's \$53 million commercialization efforts. Further, as identified in multiple USFOR-A and USAID documents, to reach financial viability DABS will require continued support for reconstruction at a cost of well over a billion dollars in U.S. energy-sector assistance (including USAID's planned PTEC work and projects under the Afghanistan Infrastructure Program funded by the Afghanistan Infrastructure Fund).
2. We disagree. Pages 7-9 of the report evaluate the extent to which USAID's commercialization efforts in Kabul assisted DABS-Kabul increase revenues, decrease losses, and become self-sufficient.
3. USAID's memorandum mischaracterizes the data in our report. The report gives credit to USAID for assisting DABS-Kabul in increasing its revenues by nearly 60 percent and reducing its technical and commercial losses to 38 percent; the report does not discuss collection rates in the same manner as the USAID memorandum.
4. USAID's comments to the draft of the report mischaracterize the objectives and expectations for KESIP. The contract between USAID and Tetrattech for KESIP clearly states, "The purpose of the Commercialization Contract is to reduce electricity losses in Kabul, and to rebuild KED's technical, commercial and human resource systems. At the end of the Commercialization Contract, KED is expected to be able to operate on a full cost recovery basis."
5. The pro forma income statement does not support USAID's assertion that DABS-Kabul [KED] did not receive a subsidy. In fact, the pro forma clearly states that DABS-Kabul received 37 percent of DABS' 1,500,000,000 Afs per year subsidy—more than \$2.9 million in the first quarter of solar year 1390 alone. Additionally, the contractor that developed the statement provided an explanation that painted a dire picture for the future of DABS-Kabul. According to the contractor, the cash flow situation is "serious" and "headed in the wrong direction," and DABS-Kabul will be "unable to pay its bills" as subsidies are phased out.
6. With appropriate contract management, and USAID's assurance that any additional expansion includes similar requirements, USAID's actions will meet the intent of our recommendation.

APPENDIX V - ACKNOWLEDGEMENTS

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