

Sad Saga of the Financial Fraud of South Carolina's Two Failed Nuclear Power Plants

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In February 2006, SCANA and Santee Cooper announced plans to build two nuclear reactors at SCANA's V.C. Summer facility in Fairfield County, South Carolina. Once S.C. legislators passed the Base Load Review Act, SCANA and Santee Cooper reached an agreement with Toshiba-owned Westinghouse Electric Company to complete the twin power plants with a deadline of December 31, 2020, to obtain funding from future federal nuclear power tax credits. As early as April 2015, the company's nuclear team felt there was little possibility of completing the power plant on time to obtain the necessary tax credits. This study covers the false and misleading statements and steps taken by SCANA executives to hide the truth. On July 31, 2017, SCANA and Santee Cooper announced abandonment of the \$9 billion project after eight years of work. Ironically, seven months later Congress passed, and President Donald Trump signed into law an amendment allowing new nuclear reactors placed into service after December 31, 2020, to qualify for the nuclear production credit.

Parties to the Financial Fraud

The parties to this fraud and material misstatement in financial statements are the parent companies SCANA Corporation and its subsidiary South Carolina Electric & Gas (SCE&G), but now known as Dominion Energy after a merger on January 2, 2019. SCANA was a regulated monopoly in South Carolina. The other colluding partner was South Carolina Public Service Authority (also known as Santee Cooper Power & Navigation Project). Throughout his article, we refer to the parent and subsidiary as SCANA and the Public Service Commission as Santee Cooper.

SCE&G is a regulated public utility engaged in the generation, transmission, distribution, and sale of electricity in South Carolina to approximately 720,000 customers. The external auditor Deloitte maintained an office at SCANA's corporate office in Cayce, S.C.

Toshiba-owned Westinghouse Electric Company, headquartered in Pennsylvania, was the lead contractor (engineering) to build the two V.C. Summer nuclear reactors in Jenkinsville, S.C., along with two unrelated Georgia Vogtle nuclear plants #3 and #4 in Waynesboro. Westinghouse was a U.S. based nuclear power company formed in 1999 from the nuclear power division of the original Westinghouse Electrical Company. Westinghouse was acquired by Toshiba for \$5.4 billion on October 16, 2006. Toshiba, who in 2015 had major accounting problems, in 2016 wrote down the Westinghouse investment by \$2.5 billion, and on March 29, 2017, Westinghouse filed for bankruptcy, mostly because of losses on the two South Carolina power plants. Toshiba cited a yearly loss for the S.C. reactors exceeding \$9 billion. PricewaterhouseCoopers issued a qualified opinion of Toshiba's financial results for the year ending March 2017 and an adverse opinion on the firm's internal controls (Othman, 2020).

The Nuclear Regulatory Commission (NRC) was an important variable in SCANA's long learning curve and slow construction progress. The NRC, created in 1974, regulates commercial nuclear power plants and other uses of nuclear materials (e.g., nuclear medicine). The NRC forced Westinghouse to make many design changes to meet new standards after they applied for approval of their new P1000 design. For example, NRC demanded they strengthen the shield building so it would withstand a crash by a commercial jet. Then the NRC questioned whether the new design would withstand an earthquake or tornado. These major changes were not approved until 2011.

Shaw Nuclear Services Group, a Baton Rouge company, owned a 20 percent interest in Westinghouse, so Westinghouse selected Shaw's nuclear sister company, Shaw Modular Solutions, located in Lake Charles, Louisiana to build the modules for the AP 1000 pressurized water reactors to be shipped to South Carolina and Georgia. Christopher Hart, nuclear procurement quality assurance manager for Shaw, said that the Lake Charles fabrication plant was clueless as to the complex geometry of nuclear welds, the nuclear supply chain and the need for a nuclear safety culture (Korman, 2017). The Nuclear Regulatory Commission would inspect the parts and mistakes would have to be corrected. Hals and Flitter (2017) indicate that not until June 2015 was the Lake Charles facility building acceptable modules. By then, Shaw

was purchased by Chicago Bridge & Iron. For example, missing and illegible paperwork (e.g., a missing signature) could delay the work on one of the 72 modules longer than constructing it (they then were to be fused together on location). One unit could weigh 2.2 million pounds (Hals and Flitter, 2017).

Major characters in this scandal include Kevin B. Marsh, who joined SCANA in 1984 and over 27 years held various officer positions. From December 2011 until December 2017, he was CEO of SCANA Corporation and SCE&G as well as Chairman of the SCANA Corporation and SCE&G Board of Directors. With a B.B.A. degree in accounting from the University of Georgia, Marsh's responsibilities included overseeing the nuclear expansion project at V.C. Summer. His substantial compensation and bonuses were tied partly to his oversight of the two nuclear projects (*SEC v. SCANA*, 2020). Research suggests that CEO and Chairman of the Board positions should be separated to avoid fraud (Beasley, 1996; Zhao and Chen, 2008). Marsh also was a former employee of Deloitte (SCANA's external auditors) which is often a precursor to the failure to detect financial fraud. SCANA announced on October 31, 2017, that Marsh was retiring as CEO effective January 1, 2018, and on December 21, 2017, SCANA stated that he would resign as a director as of December 31, 2018.

Stephen A. Byrne joined SCE&G in 1995, as the Plant Manager of the V.C. Summer plant, but later he became the company's Chief Nuclear Officer. From 2012 until January 2018, Byrne was an Executive Vice President of SCANA and President of Generation and Transmissions and COO of SCANA, overseeing all nuclear construction of the two nuclear units. He had a B.S. degree in Chemical Engineering from Wayne State University. The SEC brought a civil action suit against Marsh and Byrne for three counts of fraud, one count of aiding and abetting fraud, reporting provision violations, and false certifications on February 27, 2020 (*SEC v. SCANA*, 2020). Both Byrne and Marsh stepped down from the company in January 2018.

Deloitte acted as a feeder of executives for the company. Walsh was a former employee of Deloitte, along with CFO Jimmy Allison (eventually CEO) and Vice-President and Controller James Swan IV. Also, Gregory Aliff, Deloitte's U.S. Energy and Resources Industry leader served as a board of directors' member of SCANA as well as the chairman of the Audit Committee. Aliff is co-author of *Accounting for Public Utilities*, annually updated by Matthew Bender.

An auditing red flag is when too many executives are hired from the same audit firm (e.g., HealthSouth) that is currently auditing them (Marchesi and Emby, 2018). They tend to know how the auditors audit, may have a more favorable influence on the auditors, reduce their skepticism, and result in inattentional blindness (Othman and Laswad, 2019). Inattentional blindness is the phenomenon of not being able to see things that are actually there (Kleinman and Anandarajan, 2011). The SEC requires a cooling off period of one year before a lead partner, the consulting partners, and other members of the engagement team can be hired by that company, but some believe that period is too short (Kotb, Halabi, and Ebstein, 2018; Marchesi and Emby, 2018).

Deloitte became SCANA's independent auditor in 1945 and continues to be Dominion Energy's auditor (after the merger). Did Deloitte increase their audit fees since research indicates a higher level of audit fees for peer firms when serious misreporting by other firms in the same industry (Guo, Kubick, and Masli, 2018)? They were paid almost \$10 million in audit fees from SCANA for years 2015, 2016, and 2017 (International Brotherhood, 2020). The two audit engagement partners at Deloitte were Eileen Foody Little, CPA and Sean M. Bird, CPA. Little was the Audit Engagement Partner for SCANA and SCE&G for 2014, 2015, and 2016 engagements. She was the engagement partner when Deloitte performed a special audit of the construction costs in 2015. Little joined Deloitte as a staff auditor in the Atlanta office in 1992 and became an audit partner in 2011. She worked for Arthur Andersen before its fall and then joined Deloitte, becoming a partner in three years (*Floyd v. Deloitte*, 2020).

Sean M. Bird, CPA, joined Deloitte as a staff accountant in May 1997 and was admitted as an audit partner in 2012. With a B.S. degree in accounting from Pennsylvania State University, he was the Audit Engagement Partner for SCANA and SCE&G for the 2017 and 2018 audit engagements. SCANA Jimmy Addison in deposition said that Bird was the Audit Engagement Partner that informed him that Deloitte's local, as well as national offices, had reviewed their audit work in disclosures, post-abandonment of the project, and did not find "any gaps" in the disclosures made in the financial statements (*Floyd, III v. Deloitte*, 2020).

A minor character at SCANA was Carlette Walker, Vice President of Nuclear Finance Administration and lead accountant, who admitted she was complicit in sharing misinformation with the PSC. She indicated she was coerced to submit false testimony about the project's estimated costs (Judy and Korman, 2019). She maintained that her CEO put her

on special medical leave over her complaints. Also, engineer Kenneth Browne also said he started telling his bosses at the public utility that the project was in trouble in 2012, around four years after the nuclear project was started (ABV, 2018).

Other minor characters were Jimmy E. Addison and James E. Swan IV, who became executives at SCANA or Santee Cooper after working at Deloitte. Addison became SCANA's CFO in April 2006 and was promoted to Executive Vice President in January 2012. He replaced Kevin Marsh as SCANA's CEO on January 1, 2018. Addison was not indicted by the SEC, and in an October 3, 2018, deposition, he testified that he was not aware of the critical Bechtel Reports but relied on Deloitte as to disclosure of the Bechtel findings in SCANA's financial statements and filings with the SEC (*Floyd III v. Deloitte*, 2020).

Financing the Two Nuclear Power Plants

With only around 720,000 customers, SCANA did not have the means to build two new nuclear power plants in Fairfield County in South Carolina. There are large up-front capital requirements, construction difficulties, and cost escalations in constructing a reactor (as experienced by SCANA). SCANA had four legs to their financial plan.

Leg One. So, for leg one, SCANA split ownership of the expansion project to build two 1,117-megawatt AP1000 Advanced Passive Power plants as part of their V.C. Summer Nuclear Station located in Jenkinsville, S.C. SCANA took a 55 percent ownership stake, and Santee Cooper took the remaining 45 percent share. As majority owner, SCANA had control of the daily operations and management of the expansion project. SCANA already had a nuclear power Unit 1 in operation at V.C. Summer, so the new units became known as Unit #2 and Unit #3.

The nuclear power project was originally to cost \$9.8 billion with SCANA's share to be about \$4.5 billion. This amount was more than two times their total market capitalization at that time. A Wachovia analyst on September 12, 2008, said that "management readily admits that it is 'betting the farm' on the project" (International Brotherhood, 2020).

Leg Two. The second leg of the financial business plan for the expansion were the Federal Nuclear Production Credits. The 2005 Energy Policy Act created a production tax credit of 1.8 cents per kilowatt-hour electricity produced during the first eight years of operation by advanced nuclear power facilities. IRC Section 45J allows a maximum credit up to 6,000 megawatts of advanced nuclear generating capacity nationwide on a first come-first-serve basis. A megawatt hour is 1,000 kilowatts. The hitch in this part of the financial plan was the expansion had to be completed by January 1, 2021, to obtain the federal credits. Construction on Unit 2 officially began March 9, 2013, and Unit 3 on November 2, 2013.

Ironically, Congress passed and President Donald Trump signed an extension of the nuclear tax credit on February 9, 2018, which will benefit the two Georgia Vogtle reactors and the Utah NuScale Power project. This extension allows new nuclear reactors placed into service after December 31, 2020, to qualify. Georgia's two nuclear power projects were financed by debt and equity. They applied for \$12.03 billion of federal loan guarantees from the Department of Energy. Georgia Power had around 2.5 million customers. But like SCANA, they also were hindered by Toshiba- owned Westinghouse's bankruptcy and the problem of getting appropriate modules from Lake Charles, Louisiana to build the plants. Eventually, Georgia Power hired Bechtel Engineering to replace Westinghouse.

Both the South Carolina and Georgia plants were hampered by the erroneous "short, 36-month construction schedule" from first concrete to core load tests (Korman, 2017). The power plants were to be put together with modules like a kid playing with LEGOs—but much, much larger. The two Georgia nuclear plants will probably be finished because of their stronger financial plan and the extension of the IRC Section 48J tax credit.

The construction process lacked logical sense because Westinghouse did not have engineers at the offices of both Shaw and Westinghouse. Also, the NRC did not have inspectors on site or near Lake Charles or Westinghouse's Cranberry Township office near Pittsburgh. Richard Korman (2017) explains this communication problem which often took months:

Westinghouse would issue drawings to Shaw Nuclear in Charlotte. When Shaw reviewed the drawings and asked Westinghouse to correct a detail, problems ensued. The work processes were unnecessarily complicated by the separation of the team members. Giving an example of how the process got out of hand, Hartz says that if a design called for a 3/8-in.-wide, 12-in.-long fillet weld, the welder might make it 14 in. long. "Instead of having Westinghouse right there saying, 'That's no problem,'" recalls Hartz, "we had to write a nonconformance report that was processed and reviewed by Shaw and then sent to Westinghouse for disposition. It was insane. From Lake Charles to Pittsburgh to Charlotte

then back to Shaw Modular before the red nonconformance tag could be taken off, saying it's OK now."

The Department of Energy received 19 applications from 17 electric companies requesting loan guarantees in 2008. Apparently, SCANA Energy, Southern Company, UniStar Nuclear Energy, and NAG Energy were the final contenders for the loan guarantees (NA, 2010). On February 16, 2010, the Obama Administration announced the first conditional loan guarantees to Southern Company for the Vogtle site (Office of Nuclear Energy, 2010).

SCANA decided to avoid the loan program indicating these reasons for no interest in the government-backed loans (Adams, 2014):

'Everything we offer is oversubscribed,' Mr. Byrne said. 'Getting a government loan guarantee requires extensive financial disclosures to the federal government, and paying fees. I'm not sure why I'd want to,' he said.

Apparently, they wanted direct federal aid, not loan guarantee. This decision alone was probably fatal to the V.C. Summer Project.

The timing of completion was critical because once the plants had been built, there would be at least one year of government testing before the units could begin to sell electricity. The federal government works slowly. Of course, in hindsight, the extension of the federal tax credits would have saved SCANA if they had received the loan guarantees and not abandoned the project.

CFO Jimmy Addison (who was not indicted by the SEC) also stated that SCANA did not necessarily see a need for the DOE loan guarantee for the nuclear project. Instead, they touted their decision to buy a portion of interest from their partner Santee Cooper for \$500 million. The much stronger Duke Energy had told Santee that they were not interested in purchasing any portion of the V.C. Summer project (Barber, 2014).

Leg Three. The third leg in SCANA's financial roadmap was the S.C. Base Load Review Act (BLRA) passed in 2017. The BLRA was designed to allow utility companies to recoup "prudently incurred" capital and operating costs for a base load generating power plant during its construction rather than after its completion and start of operations. But if SCANA had material and adverse deviations from the approved schedule, the Commission could disallow any additional capital costs. Also, the utility could not recover costs after abandonment if the utility could have anticipated, minimized, or prevented these costs. Tony Bartelme (2017) explains BLRA with this analogy: "It was like paying a grocer as it builds its store—with the hope that groceries might be a little cheaper when it opens."

The special feature in the Base Load law is known as Construction Work in Progress (CWIP) or advanced cost recovery which is illegal in many states. Under CWIP, SCANA could add interest on debt and a return on investor's equity (e.g., carrying costs) in its electric rates while the nuclear project was under construction. Carrying costs are called "allowance for funds used during construction (AFUDC), which is what a power company can add to its rates. Entry wise, a noncurrent asset CWIP is debited, and cash or accounts payable is credited. Eventually, CWIP would be credited and the appropriate Property, Plant & Equipment account is debited. Basically, CWIP allows utilities to convert electrical customers into involuntary investors.

Rather than showing the construction costs as a liability on the balance sheet, they were shown on the balance sheet as an asset. They were being presented to the public as costs to be recovered in future rates as an operating generating plant. Both the balance sheets and income statements were given unqualified opinions by Deloitte. In reality, SCANA ended with a partially completed, abandoned nuclear plants with no value (with a huge liability to demolish the plants). Deloitte audited cost submissions each year and also in a special expense audit in 2015 (Floyd III complaint, 2019).

The S.C. Base Load Review Act did include the "prudently incurred" principle. However, CNO Stephen Byrne seemed to believe that the prudent principle was not necessary under the S.C. BLRA, since they only had to provide quarterly reports.

When SCANA and Santee Cooper abandoned their nuclear power project, they had spent approximately \$9 billion with only one-third being completed. Estimates were that the two plants would eventually cost more than \$23 billion (double the original estimate). Electrical customers had already paid \$1.4 billion (15.6 percent) as a result of nine different rate increases. Trigaux (2017) indicated that these projects would never have seen the light of day if state laws had not been

changed to allow the financial risk of expenses from the power company shareholders to be shifted to rate payers. The base load rate of around \$27 per bill was a large part of the average bills SCANA sent to customers. Eventually, Dominion Energy agreed to refund \$2 billion back to customers.

The BLRA and the federal tax credits were about one-half of the originally budgeted costs of SCANA's share of the project. An argument can be made that once SCANA (and Deloitte) knew that the deadline could not be met, the prudent rule would cause the previous rate increases not to be revenue. This knowledge probably occurred in the middle of 2015. Thus, the rate increase shown as income overstated the net income of SCANA. Certainly, at a minimum there were large contingent liabilities. SCANA commissioned Deloitte to perform a special audit of construction costs in early 2015 (Floyd III, 2019). The special audit was discovered in the sworn answers to interrogatories in *Lightsey et al. v. Westinghouse Electric Company*.

Leg Four. The fourth leg of the SCANA financial survival roadmap was to issue \$500 million in First Mortgage Bonds around May 19, 2015, because the company needed additional funds to continue the nuclear project. Incorporated by reference was the company's misleading Form 10-Q and its updated petition with the PSC. These documents were misleading regarding the construction schedule and the likelihood that they would qualify for the federal nuclear production tax credit.

On June 8, 2016, SCANA issued another \$500 million in First Mortgage Bonds, \$425 million with an interest rate of 4.10 percent and \$75 million with an interest rate of 4.50 percent. The SEC Complaint (2020) said that CFO Stephen Byrne's misleading presentation to Fitch the week before had the desired effect because SCANA was able to sell all \$500 million First Mortgage Bonds at amazing interest rates.

The Bechtel Reports

San Francisco Bechtel Engineering was hired by SCANA to assess the progress of Westinghouse on the nuclear project on August 10, 2015. The 130-page report was finalized on October 22, 2015 (but not made public). The Delmater and Speicher (2017) class action lawsuit complaint indicated these inadequacies and deficiencies of SCANA and Santee Cooper in the Bechtel Report:

- a. Contractors' construction plans were not specific to the Reactor project and, thus, could not serve as a firm basis to calculate the Reactor project's cost or completion date;
- b. At one point, the number of supervisors was "quite high" when compared to the 800 craft workers on the Reactor project;
- c. Contractors' designs needed "significant" changes before construction;
- d. Reactor project managers had not planned far enough ahead to adapt to the need for design changes;
- e. Turnover among non-manual workers was high;
- f. Productivity dipped because of bad designs, sustained overtime, complicated work packages, and an aging workforce;
- g. Employees worked too many hours for an extended period of time;
- h. SCANA and/or Santee Cooper should hire an experienced management company instead of relying on their own staffs; and/or
- i. SCANA and Santee Cooper should sit down with its contractors to reassess the Reactor project goals and realistically forecast its remaining cost and completion date.

The SEC complaint indicates that a SCANA nuclear construction manager stated that

"Basically, not a single schedule mitigation has worked." Another manager said that "it would take 22 years to complete the plants "at the current rate of progress (International Brotherhood, 2020, p. 63). Ron Jones, Vice- President of New Nuclear Operation said at a meeting in late 2016, that Westinghouse would need another seven years to finish the reactors if construction progress did not substantially improve (Brown and Moore, 2018).

Bechtel's one-million-dollar conclusion was that SCANA could not secure the federal tax credits over eight years after completion of the project. Lawyer George Wenick sent a letter to Deloitte's Tarah Schulz dated May 15, 2015 (referring to a February 17, 2015, letter) indicating that a partner had been hired to address the cause of and responsibility for the anticipated delay in the completion of the project. This letter stated that "nothing had occurred since our previous letter as

being material or as otherwise requiring disclosure.” Both the May 15, 2015, and February 17, 2015, letters involved the December 31, 2014, financial year (Floyd III, 2019).

An email from James E. Swan IV dated September 21, 2015, to Mark Sparks (SCANA) and Keith Coffey indicates how the SCANA executives tried to shield the critical Bechtel Report from investors and Deloitte:

FYI—Deloitte will be asking about whether (or why not) we mention the Bechtel consulting engagement in our discussion of NND in the next 10-Q. If Santee ends up mentioning it, they may feel strongly that we should too. The initial thinking, I believe is that we will not mention it, since the scope of their work is so limited [only a \$1 million study]. Stay tuned.

Also, they may ask about whether we ought to say anything about the ORS’ engagement of a CPA firm to consider the value/cost of the BLRA. I do not know what we would say about that, and I do not advocate talking about it. But it is public anyway, so if Deloitte presses and is willing to offer up some idea on language, I am open to it, I guess.

SCANA convinced their public utility partner Santee Cooper not to disclose the document for two years before the project was abandoned (Brown and Moore, 2018). The one million-dollar Bechtel Report’s best-case scenario indicated that Unit 2 would not be completed until between December 2020 and August 2021 and Unit 3 until between June 2022 and June 2023. Thus, at a minimum one-half of the important nuclear production tax credits would be lost.

Five days after Bechtel issued their initial report stating that the nuclear project would be delayed by at least three years, SCANA announced on October 27, 2015, in a press release and Form 8-K that it had amended the EPC Amendment delaying the completion of the reactors by two months. At this time SCANA needed to have a 3 percent monthly construction progress, but they were averaging only 0.5. Thus, they needed to improve their progress rate by 600 percent. (International Brotherhood, 2020, p. 66).

Even with this knowledge of the slow construction progress, in November 2015, SCANA told the PSC that the guaranteed substantial completion date (GSCD) would be met well in advance of the January 1, 2020, tax credit deadline (International Brotherhood, 2020, p. 69). There was a second Bechtel Report on February 5, 2016, with similar dire warnings, but SCANA did not change their optimistic reporting externally (Post and Courier, 2017). Their public statements after October 2015 differed materially from Bechtel’s undisclosed report (International Brotherhood, 2020, p. 72).

When Did the Parties Know?

The major question is when did the executives at SCANA know that the ticking time bomb was about to explode – the loss of the federal nuclear production tax credits on January 1, 2021. Keep in mind that the tax credits were only available for eight years after the reactors were producing electricity, not necessarily when the construction was finished.

In the *SEC v. SCANA* complaint (2020), the SEC uses the terms “fake and misleading” 38 times in 87 pages. They use the term “false” 48 times, “misleading” 50 times, “unreliable” 24 times, “misleadingly” 22 times, and “delays” 36 times. The SEC mentions “falsely” the earliest on SCANA’s second quarter earnings’ call on July 28, 2016.

SCANA executives were aware of Westinghouse’s repeated failure to meet critical milestones and various performance metrics, such as overall construction complete, the monthly percent complete, and the construction site efficiency metrics. The construction site efficiency metric constantly showed that the construction would not be completed in time to obtain the nuclear tax credits. Westinghouse would have to meet a performance factor of 1.15 each year to finish the project on time, but they never achieved the metric that high during the years working on the project (International Brotherhood, 2020).

In an executive meeting on March 6, 2015, the executives discussed the metrics showing that the current schedule was not credible or achievable (*SEC v. SCANA*, 2020). Yet SCANA continued petitioning the PSC for rate increases stating that the construction schedule represented a reasonable and prudent schedule for completing the project on time.

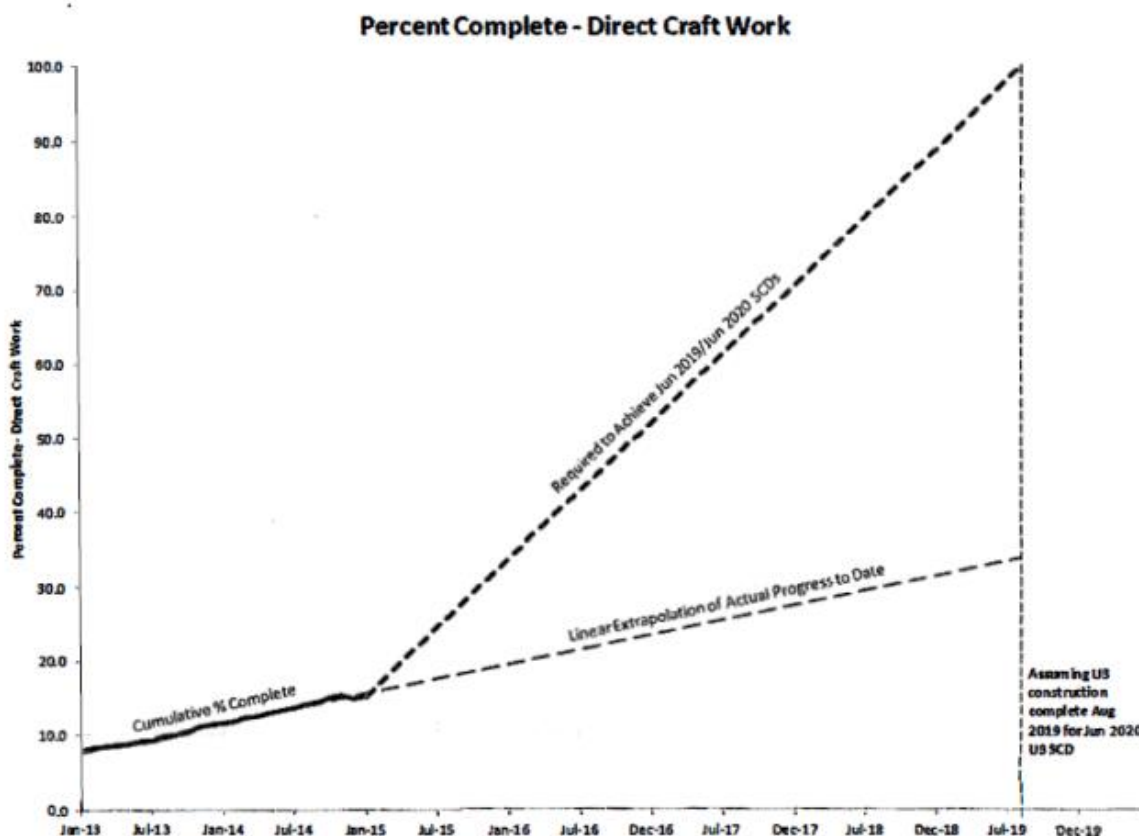
After the second Bechtel Report, in February 2016, Santee Cooper prepared a Bechtel Report Action Plan memorandum which indicated “what mitigation effort is required to defend potential shareholder problems—now that SCE&G is specifically aware of problems in [the] report; failure to act may result in O&D [Officers’ and Directors’] liability” (International Brotherhood, 2020, p. 71).

Yet on February 26, 2016, SCANA filed Form 10-K for 2015 and stated, “based on the guaranteed substantial completion dates [August 2019 and 2020], both new units are expected to be operational and to qualify for the nuclear production tax credits” (International Brotherhood, 2020, p. 72). Basically, SCANA rejected many of the Bechtel’s and Santee Cooper’s recommendations (International Brotherhood, 2020).

By the end of June 2016, the completion metrics had not improved as shown by this chart prepared by Westinghouse, being far below the needed 3% percentage (International Brotherhood, 2020, p. 84).

MONTH	EXPECTED PERCENT COMPLETE	ACTUAL PERCENT COMPLETE
January 2016	3%	0.3%
February 2016	3%	0.5%
March 2016	3%	0.6%
April 2016	3%	0.6%
May 2016	3%	0.7%
June 2016	3%	0.8%
TOTAL	18%	3.5%

One obvious smoking gun was an email discussed at a March 6, 2015, meeting which included several charts that visually depicted the lack of progress on the project. One chart showed that only around 15 percent of the project had been completed and at the current rate of progress only 30 percent would be completed by July 2019. One chart reflected that the new reactors would not be finished by the dates that SCANA was announcing:



The e-mail explained “that, in terms of costs, the attachments did not include a ‘total cost curve’ chart because based on the ‘actual numbers recorded on the project over the 5-month period (Sept. 2014–Jan. 2015),’ such a curve ‘would be off the chart’” (*SEC v. SCANA*, 2020). The chart demonstrated that Unit # 2 would not reach 35 percent completion by their July 2019 purported completion date.

One example of many false and misleading statements made by executives at SCANA was the May 26, 2015, written testimony from senior executives to the S.C. Public Service Commission. While testifying to the PSC in support of an upcoming petition, Kevin Marsh falsely testified that

In every case, both the cost and construction schedules presented and approved have been anticipated schedules for completing the Units ... The current schedules [submitted in this update petition] reflect the best information available about the anticipated costs and construction timetables for completing the project ... [SCANA] has ‘approved’ these updated schedules in the sense that it recognizes them to be the most accurate and dependable statements available of the anticipated construction schedule for completing the Units and the anticipated schedule of capital costs for completing the Units ... [SCANA] has carefully reviewed the data provided by [Westinghouse] and verified its reasonableness (*SEC v. SCANA*, 2020).

Marsh also falsely testified about their receipt of the important production tax credits:

In 2008, [SCANA] anticipated its total benefit would be \$1.06 billion gross of tax. Now it appears that there will be a smaller number of competing utilities so that [SCANA] will receive a larger amount of credits. Assuming that the current completion dates can be

maintained, [SCANA's] forecasted benefit has increased by approximately \$1.2 billion in future dollars since 2008 (SEC v. SCANA, 2020).

At the same time Stephen Byrne falsely testified about the status of the nuclear expansion project and the reliability of the construction schedule (SEC v. SCANA, 2020):

SCANA “determined in March 2015 that the cost and construction schedules as updated by [Westinghouse] through that time were in fact the anticipated schedules for completion of the project as envisioned by the BLRA.” Byrne went on to say, falsely, that the schedules “are reasonable and prudent schedules for completing the project [and] [t]hey should be approved. I can affirm that these schedules represent the best and most definitive forecast of the anticipated costs and construction schedule required to complete this project that is available as of the date of this filing of the testimony. These updated costs are not in any way the result of imprudent management of the project by” SCANA.

The SEC conclusion was that the current schedules before the PCS did not reflect the “best” or “most definitive” information available. According to the SEC complaint, on January 4, 2016, a member of SCANA's nuclear team informed Marsh that she “did not want to be involved in any of the SEC reporting because she was scared of [SCANA's] disclosures (SEC v. SCANA, 2020, p. 29).

The motive for this financial deception could have been that the total compensation for the SCANA executives almost doubled over 10 years by the end of 2017. Many companies indicted by the SEC after Enron had one thing in common: CEOs were making about 75 percent above their peers (Langley 2003), which creates pressure to manipulate earnings. Furthermore, Marsh and two other executives had golden parachute agreements if SCANA was purchased. Marsh's golden parachute payment was \$28 million, and two other executives had similar agreements of \$12 million each (Wilks, 2017). Of course, when Marsh and Byrne resigned, the SCANA board did not give them these special benefits. But Marsh has pension benefits of around \$3 million and Byrne \$1.4 million (Moore, 2018).

Class Action Lawsuits

Once a company is suspected of fraud or earnings management, securities class action lawsuits are brought against the company on behalf of investors who incur an economic loss on their stock or security. The appropriate damage group consists of investors who suffered a financial loss because they purchased the company's stock during the period when the fraud occurred. For example, if SCANA artificially inflated the price of their stock, only the individuals who purchased the stock during the class period and suffered a loss are automatically part of the class (Cheng and Crumbley, 2016).

Often there are a number of plaintiff lawyers, so the court approves a Lead Plaintiff. The Lead Plaintiff often has the largest financial interest, but a large class action lawsuit may have a Co-Lead Plaintiff. In order to bring a claim under the federal laws a plaintiff must prove a misrepresentation or omission of a material fact, reliance thereon, loss causation, damages (economic loss), scienter, and that the harm or economic damages claimed is directly connected with the purchase or sale of a security (Section 10(b); Cheng and Crumbley, 2016).

A number of class action lawsuits were filed against SCANA and Santee Cooper. Two South Carolina residents filed a suit on September 22, 2017, and another one was filed on November 10, 2017. By July 26, 2018, at least 19 lawsuits had been filed against SCANA. A legal action against Santee Cooper was back into state court on January 26, 2020. One lawsuit filed in August 2018, asked for \$453.3 million in damages. Pete Strom, lead attorney, indicated this huge amount was improperly received from customers attributable to nuclear construction from July 31, 2017, to August 6, 2018. Strom argued that SCANA was “not statutorily authorized to continue its collection of advance financing construction costs ... following its voluntary abandonment of the V.C. Summer Project on July 31, 2017 (FITS News, 2018).

By March 17, 2020, there was a settlement of a lawsuit against Santee Cooper for \$520 million, with around \$78 million going to attorneys (about 15 percent). The per residential ratepayer would get only around \$200.

Previously, on November 24, 2018, SCANA and SCE&G agreed to a \$2 billion settlement with plaintiffs in numerous class action lawsuits re electrical customers. The utility agreed to a Common Benefit Fund, with the following amounts to be distributed to the class members:

- A credit of up to \$2 billion in future electric rate relief will inure to the benefit of the Common Benefit Fund in favor of class members over a period of time established in the proceeding pending before the Public Service Commission of South Carolina (the PSC); and
- A cash payment of \$115,000,000.00, which will include the full value of the SCANA rabbi trust funded in January 2018 that was created in whole or in part for executive change in control payments (Gaither, 2018).

On March 7, 2020, a civil fraud lawsuit by shareholders was headed toward a \$192 million settlement. This settlement was composed of \$160 million in cash and \$32.5 million in stock of Dominion Energy. Dominion was the Virginia-based utility that merged with SCANA on January 2, 2019 (Monk, 2020). The typical monthly bill for a SCE&G electric customer using 1,000 kilowatt-hours had risen to at least \$147 by the time the reactors' construction was stopped (WLTX Staff, 2019).

SEC Aftermath and Prison Sentences

On February 27, 2020, the SEC charged SCANA Corporation, S.C. Electric Gas Company, and two former executives, Kevin Marsh and Stephen Byrne, with defrauding investors with their false and misleading statements about the construction of two nuclear power plants. The SEC claims the parties deceived investors by claiming that the projects were on schedule even though they knew the projects were far behind and would not qualify for federal nuclear power tax credits over eight years (once the project was completed and certified).

The SEC's Litigation Release No. 24751 states that executives flew around the U.S. showing the same construction photos from different angles and playing their fiddles while the two reactors were going up in flames. These false statements and omissions allowed SCANA to increase their stock price, sell more than \$1 billion of bonds, and obtain regulatory approval to increase ratepayers' rates to finance the two reactors. The SEC sought a permanent injunction, disgorgement of alleged ill-gotten gains with prejudgment interest, along with financial penalties for all defendants. The SEC wanted to bar Kevin Marsh and Stephen Byrne from ever being an officer or director of a publicly traded company in the future. The SEC lawsuit was a civil enforcement action and not a criminal trial.

The parties were criminally charged in South Carolina Federal Court with violating the antifraud provisions of Section 17(a) of the Securities Act of 1934 and Rule 10B-5 and Section 17(a) of the 1933 Securities Act. The parties also were charged with violating financial reporting provisions. Kevin Marsh was charged with aiding and abetting these violations.

On December 3, 2020, the SEC announced that SCANA agreed to pay a \$25 million civil penalty, and SCANA and S.C. Electric & Gas Company agreed to pay \$112.5 million in disgorgement plus prejudgment interest. Litigation Release No. 24976 indicates that without admitting or denying any allegations, the companies also agreed to a permanent injunction. The SEC litigation against Marsh and Byrne is still ongoing.

Penalties, of course, are not deductible under Code Section 162(f) and disgorgement payments were nondeductible before the *Liu v. SEC* (2020) Supreme Court decision. Here the Supreme Court held that for purposes of the SEC's remedial powers, disgorgement is not a penalty, but more like a restitution. Thus, the IRS may change their mind and allow SEC disgorgements to be deductible.

With respect to the criminal trials, Steven Byrne plead guilty on July 23, 2020, to conspiracy of mail and wire fraud. He cooperated with authorities over the previous year.

On November 24, 2020, former CEO Kevin Marsh agreed to plead guilty, go to prison for at least 18 to 36 months, and pay \$5 million fine.

There may be accounting malpractice charges against Deloitte & Touché by the SEC in the future. Only time will tell. The shareholder lawsuit is ongoing, but a settlement is likely.

Going Concern and Emphasis of Matter Paragraphs

A basic principle of financial accounting is the going concern assumption, which means that entities must continue in operation and meet their obligations within a reasonable time, not to exceed one year beyond the date of the financial statements. AU Section 341.03 states that if auditors believe there is substantial doubt the entity will operate without the threat of liquidation, they must obtain information about management's plans to mitigate the effect of such conditions and events and assess the likelihood that such plans can be effectively implemented.

If there is substantial doubt of a going concern, auditors must consider adding an explanatory paragraph after the opinion in the audit report to reflect substantial doubt. But auditors are not responsible for predicting future events or conditions. AU Section 341.06 indicates that some negative trends are “recurring operating losses, working capital deficiencies, negative cash flow from operating activities, and adverse key financial ratios.” Section 341.14 states that if auditors determine that the company’s disclosures with respect to their ability to continue as a going concern are inadequate, a departure from GAAPs exist and either a qualified or adverse opinion is appropriate.

A less severe indication is an “Emphasis-of-Matter” paragraph that is included in the auditor’s report that “refers to a matter appropriately presented or disclosed in the financial statements” which is so important that it is fundamental to the users understanding of the financial statements (AU-C Section 706.07).

In their 2017, financial statements SCANA reported a loss of \$119 million, with an impairment loss of \$1.118 billion (\$690 million net of tax). Deloitte issued an unqualified opinion for 2017 (on February 27, 2018), with a one sentence Emphasis-of-Matter statement:

As discussed in Note 10 to the financial statements, the abandoned Nuclear Project has led to legal, legislative, and regulatory matters that may result in material impacts to results and the liquidity of the company.

In Note 10 entitled Commitments and Contingencies, the abandonment of the nuclear project is mentioned along with an unrecovered Nuclear Project cost of \$3.976 billion. At the point of the issuance of the 2017 annual report, Deloitte also knew the following:

- Kevin Marsh and Stephen Byrne had resigned from SCANA in January 2018.
- Class action lawsuits against SCANA (September 27 and November 10, 2017).
- South Carolina Attorney General requests the State Law Enforcement Division to conduct a criminal investigation.
- S.C. Attorney General forces release of the Bechtel Report (September 4, 2017).
- Announcement of the abandonment of the nuclear project (July 31, 2017).
- Westinghouse files for Chapter 11, citing a \$9 billion loss in March 2017.

Why did Deloitte issue an unqualified opinion for 2017? A “Material of Uncertainty Related to Going Concern” should have been issued. Emphasis-of-Matter should not be used for material uncertainties related to a going concern. An unbiased, skeptical auditor should have issued a going concern paragraph.

Deloitte also issued an unqualified audit opinion of SCANA’s 2016 financial statements on February 24, 2017, stating they “present fairly in all material respects the information set forth therein.” At the point of the issuance of the 2016 annual report the auditor knew the following:

- The so-called “asset” on the balance sheet called “Construction in Progress” had grown to \$4.813 billion.
- There was only total net income of \$513 million without any deduction for construction costs.
- Toshiba announced the possibility of selling all or some of its stake in Westinghouse and take a \$6.3 million write-down related to nuclear projects on February 14, 2017.
- December 26, 2016, Toshiba announces an estimated impairment of several billion dollars due to cost overruns and missed deadlines on nuclear projects.
- On July 16, 2016, S.C. Public Service Commission announces there would be no more rate increases until the project was completed.
- In Note 10 of the 2015 annual report, the estimated construction costs were to be \$7.1 billion with completion dates of June 2019 for Unit 2 and June 2020 for Unit 3.
- They had knowledge that the loss of federal production tax credits expired on January 1, 2021. The second Bechtel Report on February 5, 2016, had dire warnings of the slow construction progress.
- Deloitte audited cost submissions each year and did a special expense audit in early 2015 (Floyd III complaint, 2019).

With the above knowledge, an unbiased and skeptical audit should have issued an Emphasis-of-Matter paragraph on their 2016 audit opinion, rather than this statement hidden in Note 10:

Although progress on the project was seen in December 2016 and January 2017, including the placement of the first of Unit 2's two steam generators, significant risks and uncertainties remain concerning WEC's [Westinghouse] ability to improve work force efficiency and productivity performance and to continue to fulfill its performance and financial commitments and Toshiba's ability to perform under its payment guaranty with respect to the project. In particular, there can be no assurance that their creditors will continue to provide support or that other sources of liquidity will emerge or continue to be available. In the event that WEC were to fail to complete the project in breach of its obligations under the EPC Contract, its payment obligations for damages would increase substantially above the amount of the liquidated damages described above, but would still be subject to limitations.

If the Construction in Progress account is treated as a liability, SCANA would have had a negative \$1,867 billion (411,278 - \$7,673 - \$5,472) retained earnings rather than \$3 million.

Conclusion

Much of the necessary capital SCANA needed was to be obtained from federal nuclear production tax credits that were scheduled to expire January 1, 2021. The credits were available only after the reactors were producing electricity and not when the actual construction was finished. This study follows the tortuous and flawed construction progress leading to the financial fraud by the officers of the company trying to salvage eight years of nuclear tax credits and wasting \$9 billion on the failed nuclear project. Management and the auditors knew that the project would not be completed in time to obtain the tax credits.

President Biden's Build Back Better Act would extend the credits through 2026. Georgia Power has two nuclear power projects in construction, with Unit 3 expected to be online in the third quarter of 2022 and Unit 4 to be online in the second quarter of 2023.

The implications for auditors are they not only must understand accounting and auditing, but also cost accounting and taxation. Deloitte is currently fighting an accounting malpractice lawsuit for not finding the fraud of showing construction costs as an asset rather than a liability and issuing unqualified opinions.

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Appendix I

Selected Timeline of V.C. Summer Nuclear Projects

February 2006—SCANA and Santee Cooper announce plan to construct two nuclear reactors at SCANA's V.C. Summer facility in Fairfield County.

April 19, 2007—South Carolina passes the Base Loan Review Act making it easier for utilities to raise rates to pay for nuclear reactors while under construction.

May 27, 2008—SCE&G and Santee Cooper reach agreement with Toshiba—owned Westinghouse Electric Company to construct two nuclear power plants (#2 and #3).

March 9, 2013—Construction on Unit #2 officially began.

November 3, 2013—Construction on Unit #3 officially began.

October 2014—SCANA and Santee Cooper announce one-year delay and \$1.2 billion extra project costs.

Early 2015—SCANA and Santee Cooper commission the San Francisco Bechtel Corporation through attorney George Wenick to review the struggling V.C. Summer project to outline Westinghouse failures. Attorney used possibly to protect the report under attorney-client privilege. SEC says August 6, 2015.

March 15, 2015—SCANA files false petition to PSC.

April 6, 2015—SCANA made false statements and omitted material information in their 1st quarter earnings call and Form 10-Q filing.

April 28, 2015—Memo by SCANA nuclear team: Westinghouse has no credibility for developing a realistic schedule, and we have no confidence they can complete No. 3 by the end of 2020 and the production tax credits are in jeopardy for that unit.

May 19, 2015—SCANA issues \$500 million in First Mortgage Bonds, with materially misleading construction schedule, omitting the likelihood that they would not get production tax credits.

October 15, 2015—\$1 million Bechtel Report, best case scenario Unit 2 would not be completed until between December 2020 and August 2021; Unit 3 until June 2022 and June 2023. Therefore, loss of some or all tax credits.

November 2015—Marsh and Byrne testified before the PSC giving false completion dates.

December 31, 2015—Deloitte issues a qualified opinion. Note 10: Estimated costs to be \$7.1 billion and completion dates of Unit 2, June 2019 and Unit 3, June 2020.

January 2016—SCE&G approved another round of salary raises for five executives, making \$937,000 more in total compensation than in 2015.

February 26, 2016—SCANA issues 2015 Annual Report with Deloitte's unqualified opinion.

June 8, 2016—SCANA issues another \$500 million in First Mortgage Bonds.

June 2016—SCE&G asks PSC to approve another rate increase.

July 2016—SCE&G asks for last of nine rate increases. Increase approved but S.C.P.S.C. negotiates no more increases until project is completed.

December 26, 2016—Toshiba announces an estimated impairment of several billion dollars due to the cost overruns and missed deadlines on nuclear projects.

February 2017—Westinghouse provides SCE&G with revised in-service dates of April 2020 for Unit #2 and December 2020 (Unit #3).

February 14, 2017—Toshiba announces the possibility of selling all or some of its stake in Westinghouse and take a \$6.3 million write-down related to the nuclear projects.

February 24, 2017—The 2016 annual report was issued by SCANA with a Deloitte unqualified opinion.

- March 2017—Westinghouse files for Chapter 11, citing \$9 billion in losses.
- July 28, 2017—SCE&G and Santee Cooper reached agreement with Toshiba Corp. to receive \$2.168 billion as guaranty of obligation for Westinghouse Electric Co., \$1.192 billion to SCE&G and \$0.929 billion to Santee Cooper.
- July 31, 2017—SCANA and Santee Cooper announce abandoning the \$9 billion project. After eight years of work.
- September 4, 2017—S.C. Attorney General forces the release of the Bechtel Report.
- September 22, 2017—S.C. Attorney General requests the State Law Enforcement Division to conduct a criminal investigation.
- September 22, 2017—Two S.C. residents file class action lawsuits against SCANA.
- September 28, 2017—SCANA and Santee Cooper sell their settlement payments from Toshiba Corp. to Citibank for \$1.847 billion (discount of 14.8 percent).
- November 10, 2017—Another class action lawsuit against SCANA.
- January 2018—Kevin Marsh and Stephen Byrne resign from SCANA.
- February 12, 2018—Congress passes and President Trump signs extension of the nuclear production tax credit allowing new reactors placed into service after December 31, 2020, to qualify.
- February 27, 2018—Deloitte expressed an unqualified opinion for year 2017. ICOFR: Company maintained, in all material respect, effective internal control over financial reporting. Emphasis of matter paragraph: Unrecovered Nuclear Project Costs, \$3,976 million.
- March 2018—Judge allows class action lawsuits to proceed against SCANA.
- May 10, 2018—S.C. Senate votes to repeal the Base Load Review Act.
- July 31, 2018—Shareholders vote to merge company with Dominion Energy. Merged January 2, 2019.
- November 24, 2018—SCANA and SCE&G agreed to a class -action \$2 billion settlement with S.C. customers and turns over \$115 million golden parachute payments due to the executives in a rabbi trust.
- November 26, 2019—Class action lawsuit against Deloitte re audit failure at SCANA.
- January 26, 2020—Legal action against Santee Cooper back in state court.
- February 18, 2020—Court appointed Int. Brotherhood of Electrical Workers Local 98 Pension Fund as lead plaintiff in the Deloitte class action lawsuit.
- February 27, 2020—U.S. SEC bring fraud action against SCANA Corporation, Dominion Energy South, SCE&G, Kevin B. Marsh, and Stephen A. Byrne.
- March 7, 2020—A civil lawsuit heads for settlement for shareholders for \$192 million (\$160 million cash and \$32.5 million in Dominion Energy stock).
- March 13, 2020—Santee Cooper, 45 percent partner of failed twin reactors, approves class action lawsuit to pay \$200 million in cash over 3 years and freezes utility rates for four years.
- July 23, 2020—Stephen A. Byrne agreed to plead guilty to criminal conspiracy fraud charges in U.S. District Court in Columbia. The document indicates that Byrne and others through intentional and material misrepresentations and omissions deceived regulators and customers to maintain financing for the nuclear project and to financially benefit SCANA.
- July 20, 2020—Deloitte asked the S. C. federal court to dismiss the thinly substantiated shareholder lawsuit, because the 200-page complaint only made two specific auditing statements that Deloitte violated the Securities Act.
- November 17, 2020—Judge Margaret B. Seymour denied Deloitte's motion to dismiss the shareholder lawsuit.
- November 24, 2020—Kevin Marsh agreed to plead guilty to fraud, to pay \$5 million, and go to prison from 18 to 36 months. The agreement must be accepted by the U.S. District Court judge.

December 2, 2020—SCANA agreed to pay the SEC a \$25 million penalty, and SCANA and S.C. Electric & Gas Co. agreed to pay \$112.5 million in disgorgement plus prejudgment interest.

December 24, 2020—Kevin Marsh plead guilty to conspiracy of mail and wire fraud in one courtroom and went to a Richland County courtroom to plead guilty to obtaining property under false pretenses.

February 24, 2021—Ex-SCANA CEO Kevin Marsh pleads guilty to conspiracy, agreeing to a two-year prison sentence and ordered to pay \$5 million in restitution to low-income rate payers.

June 10, 2021—Key Westinghouse executive Carl Churchman pleads guilty in S.C. nuclear scandal for lying to an FBI agent. He claimed that he was unaware that Westinghouse told SCANA executives certain completion dates of the S.C. nuclear projects.

October 11, 2021—Kevin Marsh was the first SCANA executive sentenced to two years in prison (reduced from 10 years due to a negotiated plea agreement), followed by a three-year term of court-ordered supervision. A \$200,000 fine was imposed upon him.