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Financial woes of Westinghouse parent company worry US nuclear industry

US nuclear companies are closely watching developments at Japan's Toshiba, both for their impact on four reactors under construction in the Southeast as well as for any potential impact on Westinghouse, the largest US-based reactor vendor.

"This is a critical moment in the US nuclear industry," considering that Westinghouse has long been "a top-tier reactor designer and builder," Edward Davis, President and CEO of Pegasus Group, said in a February 6 interview.

A Toshiba executive said January 27 the company is reviewing whether it will continue to be involved in nuclear construction outside Japan following the announcement in December that it expects to report a multi-billion-dollar loss in connection with construction of AP1000 projects in the US. Details are expected to be announced when Toshiba reports fiscal third-quarter financial results February 14.

Davis said the Pittsburgh-based company "always envisioned itself as a one-stop shop, a company that would bid not only for the manufacturing scope of the [nuclear power plant] project, but the construction and engineering, too."

Davis said it is unknown whether Westinghouse will continue to offer such "full scope" services in the future, based on its parent company's potential decision to exit the nuclear construction business.

The US nuclear industry is watching developments closely because of the key role played by Westinghouse in providing not only new reactors but services and components to existing plants, many of which it designed, industry officials said.

Exelon Generation, the largest US nuclear operator, is "monitoring developments in this case and will be ready, as always, with prepared contingencies to adapt safely and effectively to any change in industry vendors and suppliers," the company said in an email statement February 7.

Tennessee Valley Authority CEO Bill Johnson told reporters in Washington February 1 that "the entire nuclear industry" is concerned about the impact on Westinghouse from Toshiba's financial woes. Westinghouse is a key supplier to many US nuclear utilities, he said.

"We've had a reduction in the number of vendors and service providers over the last decades," Johnson said. "We're watching it really closely."

Davis said he does not see such a Toshiba decision, assuming it occurs, significantly affecting construction schedules of two Westinghouse AP1000 units each at the Georgia Vogtle and South Carolina Summer sites.

Davis said that “Southern has a virtually bullet-proof, fully-wrapped contract [with Westinghouse] that is very strong, which significantly insulates Southern from further cost overruns” in Vogtle’s construction. Davis said he believes Summer “is in a similar position” on cost overrun protection.

EPC contracts revised

Contracts for the two plants were revised at the end of 2015, when Westinghouse acquired Chicago Bridge & Iron’s Stone & Webster business, which had been managing construction efforts at Vogtle and Summer. Executives of Southern Co., whose subsidiary Georgia Power is the largest single owner of the Vogtle expansion, have always said their original 2008 EPC contract effectively fixed the vast majority of costs, meaning their expenses from delays were limited to their own costs. When the contract was revised as part of a court settlement in October 2015, Southern Co. CEO Tom Fanning said even more costs were made fixed rather than variable, and Westinghouse became responsible for penalties of \$10 million a month if Vogtle-3 did not load fuel by December 2018.

The new AP1000 units at Vogtle are scheduled to begin commercial operation in June 2019 and June 2020, respectively, although independent monitors for the state Public Service Commission have said those dates are not likely to be met.

The contract with South Carolina Electric & Gas to supply Summer-2 and -3 initially had fewer fixed-price elements, company officials have said, but in May SCE&G opted for a fixed-price option in the revised EPC contract that it said would cost the company more money up front but would protect it from delays and cost overruns.

Delays in construction threaten the ability of Georgia Power to receive production tax credits of \$18 per megawatt-hour from the federal government for the first eight years of operation. Those credits are contingent on the units being in commercial operation no later than the end of 2020, the Georgia PSC’s independent construction monitors have said.

For unit 4, the date “can only be achieved if all mitigation is successfully implemented as planned and no additional delays occur to future activities, which we believe to be highly unlikely,” they said in a report last year.

The credits, established in federal legislation in 2005 to spur new nuclear plant construction, are worth up to \$125 million annually per gigawatt of new capacity for eight years.

Edward Kee, CEO of Nuclear Economics Consulting Group, also said in a February 6 interview he does not foresee any shift in the Toshiba-Westinghouse corporate landscape adversely affecting the four US AP1000 units’ construction, noting that Fluor has taken over this responsibility.

“The big issue that is unknown is whether Westinghouse will continue to supply equipment for the AP1000 even after Toshiba-Westinghouse stop construction services,” Kee said.

Fluor was brought in as a subcontractor managing construction on the Vogtle and Summer projects in January 2016.

Needing partners

A critical issue, Kee said, is that should Westinghouse transition to become solely an AP1000 unit supplier, it is imperative the company team up with one or more other companies that would do the additional engineering, procurement, and construction, and sell this as “a package.”

“No utility is going to merely buy a reactor, and this is the reason Toshiba and Westinghouse are in the business together now, so they can wrap up all services and sell an entire package,” he said.

For example, Kee noted that Nuclear Power Corp. of India Ltd. has built nuclear power plants utilizing Russian-made reactors, and NPCIL built the balance of the plant.

In addition, he noted that Chinese companies are building the AP1000 units purchased from Westinghouse.

Margaret Harding, president of consulting firm 4 Factor Consulting, said in a February 6 interview it is likely Toshiba will look to sell Westinghouse. Harding, who was a General Electric nuclear executive in 2006 when that company and Toshiba bid to buy Westinghouse, said the Japanese company “kept bidding up the price and the feeling at GE was that [Toshiba] bought Westinghouse for twice what it was worth.” The deal closed for \$5.4 billion, Platts reported.

“The nuclear renaissance Toshiba believed was about to occur never did and all the new [US] units they expected to be built never were,” she said. “Then Fukushima came along [in March 2011] and with few prospects for new [reactor] builds, Toshiba’s stock took a beating.”

She said it will “not be easy” for Toshiba to find a buyer for Westinghouse, noting the “most likely” buyer would be one of several Chinese nuclear power companies.

However, Harding said this could be a “tough sell,” noting if a Chinese company wanted to buy Westinghouse “the US government would take a hard and long look at the proposal, given all of the nuclear technology owned by Westinghouse.

Westinghouse spokeswoman did not respond to a request for comment.

Credit rating impact

Moody’s Investors Service said in a report January 4, after Toshiba announced the potential for a major loss on the US nuclear business, that the situation for the company was negative for the credit rating of Georgia Power and SCE&G.

Under the contracts for the new units, Toshiba is the guarantor “of certain Westinghouse obligations under the the EPC contracts,” Moody’s said.

One concern is that the Toshiba loss could result in a breach of the company’s bank debt requirements, Moody’s said.

Georgia Power and its partners in the Vogtle project have protected themselves from the near-term impact of the loss because they required Westinghouse to provide them with letters of credit totaling \$920 million when Toshiba’s credit rating was cut in January 2016, Moody’s said.

SCE&G and the Summer co-owner Santee Cooper are less protected because they were to receive letters of credit from Westinghouse for \$100 million, Moody's said.

Toshiba's exit from the nuclear business, or potential sale of portions of it, "could have adverse consequences for the Vogtle and VC Summer projects by potentially introducing a new party into the process while two projects are less than 50% constructed," Moody's said.

"Even if Toshiba decides to keep its US nuclear business, a financially constrained Toshiba parent company could make any additional costs and/or disputes with Westinghouse more difficult to resolve, or could result in additional project delays if there are insufficient funds available to maintain the currently agreed project schedules," Moody's said.

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