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PUBLIC UTILITIES FORTNIGHTLY

"In the Public Interest"

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Energy's Spend and Workplace Diversity

Tracey Woods, Paula Glover, Pauline St. Cyr, Aaron Cope at American Association of Blacks in Energy

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Cover photography: From left to right, American Association of Blacks in Energy VP-Operations Tracey Woods, CEO Paula Glover, assistant Pauline St. Cyr and administrative analyst Aaron Cope. Photographer: PUF staff.

In Diversity There is Energy

Woodwinds, Brass, Percussion. Glorious Additions to the Strings

BY STEVE MITNICK

During the first decade of my career in utility regulation and policy, industry leaders were mostly old men with a serious demeanor and similar ancestry, experience and lifestyle. They were pretty intimidating, even for this white guy. My dissimilar accent, religion and look didn't help.

During the second decade of my career, among the industry's leaders were a few characters with more colorful personalities. A consequence of an increased need to connect with constituencies of all complexions. A handful of the leaders were men and women with different ancestry, experience and lifestyle. The first African-American to CEO an investor-owned utility emerged in these years.

> Diverse teams tend to be more curious, dynamic, creative. Groupthink is less likely, anticipating the unanticipated, more likely.

During the third decade of my career, you began to see women as leaders in the utilities industry, and more men and women from a broader background.

The first woman to CEO an investor-owned utility emerged in these years.

During this, the fourth decade of my career, diversity became commonplace. And, the trend clearly accelerated in the last couple of years.

Consider this. A woman has chaired the Edison Electric Institute since last June. She's the first to do so. Yet a second will take her gavel for the year starting this June.

Women are now CEOs at many investor-owned utilities including two of the very largest, Duke Energy and PG&E. That woman leading PG&E is Hispanic American. As is the man leading the other California mega-utility, Edison International.

This is not just happening at the top. Some of the brightest stars of today's industry are African American, Hispanic American and Asian American, both men and women, at Duke Energy, Edison International, Entergy, Exelon, PG&E, Southern Company and on and on. I know; I'm leaving out a bunch of others.

And, this stands out. The differences with their predecessors of the seventies and eighties are not just in ancestry, experience and lifestyle. These days, most of those at the top, and most of those heading there – the white guys too – are personable, remarkably open and well, colorful.

Why did this happen? That is, why has our industry put the pedal to the metal on diversity?

Some say it's due to the recognition that the leaders of utilities – and the workforce overall – should have a composition matching the communities they serve. I suppose so. The public naturally relates better to companies that feel like they're us rather than they're them.

Some say it's due to the response »

Steve Mitnick is Editor-in-Chief of *Public Utilities Fortnightly* and author of the book "Lines Down: How We Pay, Use, Value Grid Electricity Amid the Storm."

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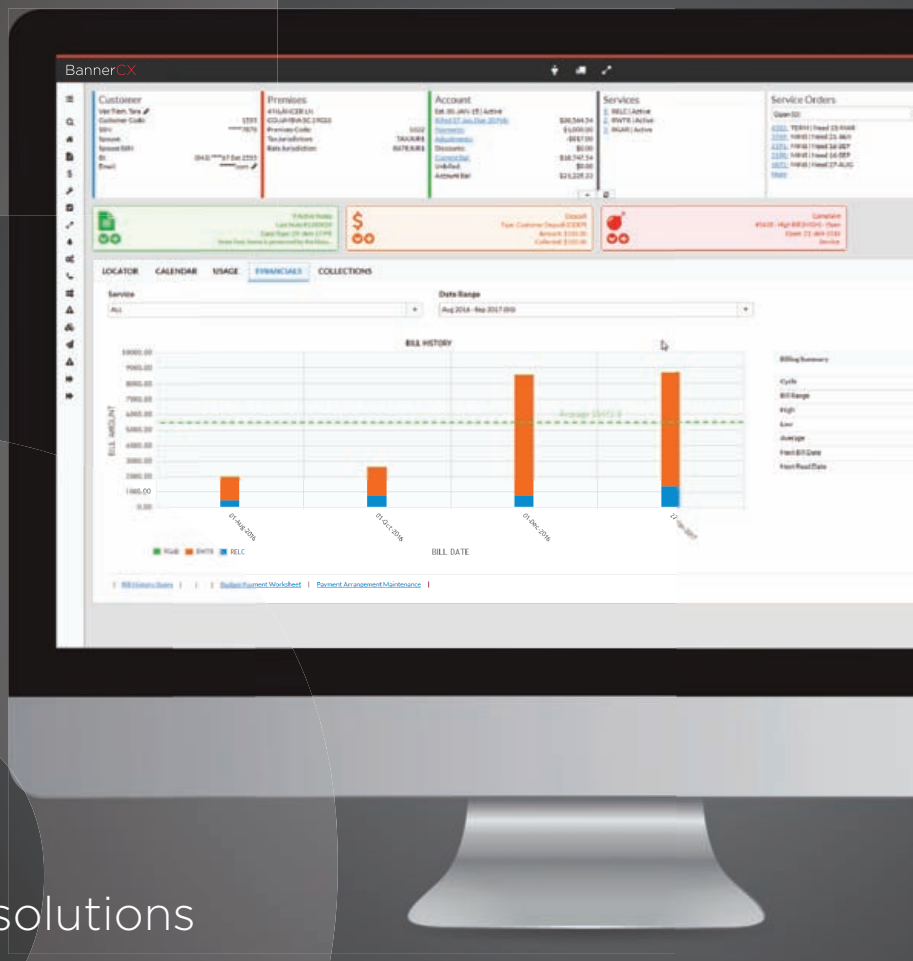

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to political and cultural pressures demanding diversity. Again, I suppose so. No company wants to swim against the tide.

My explanation differs. It's about a fast-growing realization among today's CEOs, that diversity imbues energy in energy companies.

It has become apparent that diverse teams tend to be more curious, dynamic, creative. In diverse teams, groupthink is less likely. Anticipating the unanticipated, that is more likely.

Makes sense, doesn't it? It's been proven again and again by our armed forces. Put the city tough, farm boy and backwoodsman into the same rifle company. With their multiple skills and perspectives devoted to a single cause, they become a mean fighting machine.

In some ways, diverse teams are more difficult. They're tougher to put together, tougher than recruiting from the neighborhood. They're tougher to keep together, tougher than hanging out with the regulars.

You have to be intentional. That's what she said in one of my interviews for this issue of *Public Utilities Fortnightly*. What she meant was, it takes work, hard work. It doesn't come naturally. Out with the old, "it's who you know." In with the new, "it's who you need."

Can it feel forced? Sure. It may feel like a mandate from up high. It may not feel like it's your will from inside.

Diversity imbues energy in the suppliers of energy companies as well.

But we surely want a lot of different instruments to play a masterpiece together. Though we always favored the strings section, let's imagine, though our buddies are mainly the string players, we really must seek out the woodwinds, brass and percussion. Those players aren't quite like us. But without them, the orchestra is one-dimensional and boring.

I learned so much in these interviews. While diversity in our leaderships and in the workforce does bring great energy to the good old energy company, you can't leave out the workforce beyond the workforce. The utilities industry contracts out, a lot. For every employee of a utility there are two employees at our vendors, suppliers, contractors, advisors, etc. So, the purpose of the diversity spend movement is to ensure those partner organizations are complete orchestras too.

Especially as diversity spend moves along the value chain from commodity providers such as janitorial and security services to intellectual capital providers such as engineering and financial services. Diversity imbues energy in the suppliers of energy companies as well.

I don't want to talk the talk, just, and not walk the walk. The *Public Utilities Fortnightly* team is working hard to involve authors and interviewees of all stripes. Or shall I say, all parts of the orchestra, be it woodwinds, brass or percussion, as glorious additions to the strings. PUF

Pinnacle West's CEO Don Brandt

Leadership Lyceum's Podcast Summary, hosted by Tom Linquist

I joined Don Brandt, CEO of Pinnacle West, under azure Phoenix skies in early March. With three and a half billion in revenue, Pinnacle West Capital Corporation is based in Phoenix, Arizona.

It has consolidated assets of about seventeen billion, about sixty-two hundred megawatts of generating capacity and sixty-three hundred employees in Arizona and New Mexico. Through its principal subsidiary, Arizona Public Service, the company provides retail electricity service to nearly 1.2 million Arizona homes and businesses.

Arizona Public Service has a storied past. Natural and man-made infrastructure were key to the settlement of the western U.S. and provide the dramatic context for Wild West legend and lore.

Railroad access, river crossings, mining, water resources, and power generation were important conditions for statehood in the west. Arizona Public Service was founded five years after the infamous gunfight at the O.K. Corral and a quarter century before Arizona became a state. The company has served Arizona for more than a hundred and twenty-five years.

Leadership Lyceum (LL): Don, your origins here at APS were storied as well. You orchestrated a turnaround coming into the company. Take us back to the situation you found yourself in when you came into the company in the 2002-2003 time frame.

Pinnacle West's Don Brandt: I came here to interview in October of 2002. Between my interview and when I came on board sixty days later, the company's credit ratings had been downgraded one more notch, approaching non-investment grade.

The company hadn't filed a rate case in ten years. The company was in dire need of one. The Palo Verde Nuclear Generating Station-related rate increases that were implemented in the early '90s had sustained the company and had worked well, until we got to the point where we needed additional revenue.

LL: How did the Palo Verde rate increases sustain the company over the ten years up to that point?

Don Brandt: We had gone ten years because the Palo Verde units came on in the late '80s and early '90s. We were basically displacing higher-priced coal and natural gas with nuclear fuel. We had the capital for the plant in the rate base, but as the units came on and the growth of our customer base continued, we were supplying the growth with the marginal cost of nuclear. Nuclear was half a cent per kilowatt-hour compared to natural gas at about five cents at that time. So, you're replacing five-cent fuel with half-cent fuel.

LL: You faced a pent-up need for a rate case, with not a lot of institutional memory of how to execute one. But let's provide a broader context for your setting.

It was 2002. We had the Enron bankruptcy. We had Dynegy teetering on the brink of bankruptcy. Any stability at the time was coming from the regulated utilities, and not from the diversified investments that so many had put money into.

Don Brandt: Exactly. To complicate it even more, at that time we had been ordered by the Arizona Corporation Commission, our public service commission here, to divest our generating assets into a competitive subsidiary.

Between my interview and when I came on board sixty days later, the company's credit ratings had been downgraded one more notch.

We were experiencing rapid growth in our customer base, on the order of four to six percent a year, so we were building power plants in the unregulated subsidiary to serve the growth. Redhawk One, Redhawk Two, big combined-cycle plants and a couple smaller ones.

Then when California blew up with the energy crisis out there, the commission said, "Whoa, stop. This doesn't look to be too brilliant an idea, put it all back together again."

We had to put it back together under the regulated utility and then pursue that much needed rate increase. This presented some people challenges and regulatory challenges, among other things.

LL: Putting that all back together and having to value those assets in a regulated context. That strikes me as a major challenge.

Don Brandt: Yes, you're not going to come out of that whole. We ended up writing off about a hundred and thirty million out of about a billion that was transferred back into the regulated utility. In addition, we really didn't get much of a rate increase. If my memory serves me right, it was somewhere around the two percent level.

LL: To give a sense of the magnitude of growth, in 1990 the Greater Phoenix Area population was 2,130,000. By 2006 it was 3,793,000. A growth of about 1.6 million or seventy-eight percent over that time period. Those are gold rush proportions. After ten years under the old rate, with the population growing at that magnitude.

Don Brandt: Exactly. That was very inadequate. As a consequence, a few months later we filed what out here we call an emergency rate increase, where I was the only witness. And unlike

APS supports veterans throughout the state of Arizona through programs and activities, including its annual event celebrating the Grand Marshals of Phoenix's Veterans Day Parade. Each year, the program features well-known political and military leaders as keynote speakers. Sen. John McCain, pictured here with Don Brandt, the Grand Marshals and APS employees, spoke at the 2014 event.

the typical rate case format, where you file all this testimony, it was a long-winded affidavit from me describing the situation from the standpoint of our company.

I was explaining that at the level we're growing, and we're investing a billion to a billion and a half a year to meet that growth, if we go to non-investment grade, forget it.

It's a situation you don't want to have to deal with. We have an elected commission here and there are pros and cons to elected versus appointed. But nevertheless, their reaction was, well, we're not going to raise customer rates just because Standard & Poor's thinks we need to.

I like to use the analogy that a credit rating agency is like the umpire of a baseball game. They're really not rooting for either team. If it's in the strike zone, it's a strike. If it's not, it's a ball. That's it. They're just calling 'em as they see 'em.

I was on the witness stand for days. I was not so much testifying, as I was educating. Day after day going through it. We ended up with about a six and a half percent increase after that.

At the time, we didn't have a fuel clause here in Arizona and we were successful getting that put in place. And with every rate case after that, we made some incremental improvements in the regulatory process. We had a rate case every two or three years.

LL: With your population growth, it seems like you had to go back on a more frequent basis.

Don Brandt: Yes. And at the time, the traditional rate case, not the emergency, but the traditional, was lasting about twenty-four months. We were the fastest growing utility in the United States, investing over a billion dollars a year, with an historic test year and twenty-four months to process a rate case. You're two to four billion dollars behind the eight-ball by the time that you get the last one done.

We sat down and developed what I thought was a pretty constructive relationship with the Commission staff. Since about ninety-five percent of the data requests we get over the course of a rate case are identical to the last one, much of it is just rote.

We could streamline many of the routine parts of the process. With the first case where we implemented that new approach, we got it done in a little over twelve months, which essentially cut the time in half. Now we have it down to under twelve months.

As a result, we stopped the credit downgrades and now we have one of the strongest balance sheets in the industry. We're in the business of working for our shareholders.

Our return on equity has improved. Our allowed returns were a little higher then, but they've come off a little bit with interest rates. Now they're ten percent.

During that troubled period, we were only actually earning about six and a half percent on equity. I just wrote my annual shareholder's letter for the annual report. Our 2017 consolidated earned return on average common equity was 9.96 percent. On a consolidated basis we are right there against our allowed return.

LL: About as close as you can get.

Don Brandt: Exactly, without causing problems.

LL: What about your diversified investments?

Don Brandt: Yes, I noticed very early on that we were in a lot of other businesses. We had a separate real estate subsidiary that did all kinds of real estate from residential to commercial, from some light industrial to condo building development. It was relatively small, but it took unbelievable amounts of time from senior executives.

We had an energy efficiency business. We had the district cooling loop here in downtown Phoenix and downtown Tucson. It was originally built to supply chilled air to the ballpark where the Arizona Diamondbacks play. It had been expanded and a number of buildings used this chilled water system.

Don Brandt speaks at an event of the Employer Support of the Guard and Reserve (ESGR) in Phoenix. APS has been recognized for its contributions to ESGR in Arizona.

It was a continual cash drain because you had to continue to expand it and then try to add the customers. We wouldn't expand it unless we knew there were customers coming with additional buildings, but there was a huge delay in that. And that wasn't a regulated business. We never really made any money at it, either.

When I became CEO in April 2009, one of the first things we did was decide to get out of the real estate business. It was in decline with the great recession, and we had never been all that successful in it.

I think the very first two weeks after I became CEO, we announced we were getting out of the real estate business and took a five hundred-million-dollar charge. And our stock went up fifteen percent.

LL: That underscores your investor sentiment for your real estate business.

Don Brandt: They were thrilled. Our biggest outcome from the real estate business was the tax loss we got out of it. When we announced the five hundred million charge, we made very public the fact that the associated tax benefit would enable us to defer an equity issuance for another two years. We were out of the real estate business that the analyst community never really understood. And we put off an equity issuance.

LL: We've covered a lot of the external factors with the turnaround. What about the internal components and company culture? What was required there?

Don Brandt: That is a big key. It's one thing to talk about the regulatory process, but it's another to get buy-in across the company for what we had to get done. We spent a lot of time communicating across the company.

First, to communicate how dire the circumstances were. This wasn't just going to be the slogan or program of the month. This was something that was going to take us a number of years to fix and we needed to get everybody on board.

We had to look at our cost structure too, because getting these rate increases, for any utility, even one in a high growth environment, it's never easy. Even in our growth environment, we had to streamline processes and reduce costs.

It's one thing to talk about the regulatory process, but it's another to get buy-in across the company for what we had to get done.

I tasked our chief operating officer and our chief financial officer to co-head a team that would look at process improvement. I could sit here and do a line item veto on the budget, but we needed to analyze all our processes and benchmark every process against our peers. It was somewhat like how we looked at the regulatory process earlier. It took about three or four years in total.

LL: If there was a silver lining to the shock to the company employees, it must be the innovations that were developed at that time. I think you were on the leading edge with automated meter reading?

Don Brandt: We probably started it around '04, '05. We were one of the first utilities to deploy an automated meter reading system. For a percentage of customers, we're at ninety-eight percent, other than the most remote customer.

We deployed this system over a number of years. We had about a hundred and thirty meter readers, and told them we would train them for other jobs and provide preferential treatment if they could qualify for these jobs. This provided them time to build up the skillset to ramp into another long-term job.

Yes, we were one of the first. I think we still probably are from a penetration standpoint. But AMR also afforded us the opportunity to implement a variety of customer rate options,

Members of the APS VETRN employee networking group pose with Don Brandt and the Freedom Award. VETRN is an important resource for veteran employees, especially those transitioning from military service to a civilian career.

including residential demand rates. And we have about twenty percent of our residential customers that are on these demand rates.

LL: I know that you are very passionate about the skills and capabilities of our military veterans. Please discuss APS and veterans.

Don Brandt: Yes, more than twenty percent of our employees are vets. We find their mission-driven work ethic provides for excellent, outstanding employees, almost without exception. And we make a very concerted effort to hire vets for that very reason.

The so-called grunt of World War II or even Vietnam doesn't exist anymore. These women and men are very adept at computers and other advanced forms of technology. When they get involved with our technology, it's second nature for them.

They embrace it, and with our training, they're up to speed quickly. They tend to be long-tenured employees. They do exceptionally well and they stay with us.

LL: To recruit and train vets at this scale, at twenty percent of your employee base, do you have a well-developed program in place?

Don Brandt: Yes. We hold a lot of vet hiring events and we sponsor events throughout the state and utilize our employees' own network. About a year ago we put together a program with Senator John McCain where we go out with some of the other larger employers, like Freeport-McMoRan, to basically explain to smaller employers the benefits of hiring vets. Because quite frankly, a lot of smaller employers, who have a lot of the available jobs, aren't aware of or have misconceptions about vets.

LL: What are some of the misconceptions?

Don Brandt: The psychological impact of however many deployments in Iraq, Afghanistan. And yes, it's there. But ninety-five percent of these men and women, with a little bit of training and a little bit of compassion, get over their issues. Nobody comes back, you just can't come back from an environment like that at a hundred percent.

We have an affinity group we call VETRN. It's a group of both vets and non-vets. Their job is to meet with these folks, kind of be their mentors, sounding boards, so they are not walking into an environment of strangers. They have a group to help assimilate into our company. We would not have the success and strong retention of these employees without that group.

At an industry level, we have a Troops to Energy program. We were one of four utilities that EEI helped put together to start that program. It's a lot more than four now, and we have improved it every year since it was initiated, about five years ago.

LL: With this these types of programs in place, I imagine that there is a group of high-potential veterans to consider.

Don Brandt: Yes, we do a number of job fairs and advertise to attract the best of the best. It's really worked out well. And it's something I'm pretty darn proud of.

LL: APS was recognized for its employment practices and treatment of vets and reservists by the Department of Defense in 2014. APS was the recipient of the 2014 Freedom Award. What an honor it must be, Don.

Don Brandt: I got a call from the Pentagon one day. I had never heard of the award before. And one of our vets, an army sergeant, had nominated us. We didn't even know we'd been nominated, and they were calling to tell me we won and were inviting us to the Pentagon to accept it. It was a great honor. PUF

Listen for more with Don Brandt on the 2014 Freedom Award ceremony in our podcast coverage of this interview. To hear the full interview, please link to the podcast at Leadership Lyceum: A CEO's Virtual Mentor, available at Apple iTunes. Search iTunes Podcasts, with the keyword Leadership Lyceum.