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# BEFORE THE IDAHO PUBLIC UTILITIES COMMISSION

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| **IN THE MATTER OF IDAHO POWER COMPANY'S APPLICATION FOR AN ACCOUNTING ORDER FOR COSTS ASSOCIATED WITH CLOUD COMPUTING ARRANGEMENTS** | ) | **CASE NO. IPC-E-20-11**<br><br>**COMMENTS OF THE COMMISSION STAFF** |

**STAFF OF** the Idaho Public Utilities Commission, by and through its Attorney of record, Dayn Hardie, Deputy Attorney General, submits the following comments.

## BACKGROUND

On March 9, 2020, Idaho Power Company ("Company") applied to the Commission seeking an order (1) approving the deferral of costs associated with future cloud computing arrangements to a regulatory asset, and (2) acknowledging that the unamortized regulatory asset amounts are eligible for rate base treatment and the associated annual amortization expense is eligible for potential recovery in a future rate proceeding.

The Company's information technology ("IT") system includes both on-premise solutions and cloud computing. The Company proposes to capitalize all costs associated with cost-effective cloud computing because the cloud computing investments are "equivalent to that of a traditional on-premise [IT] solution."

## STAFF ANALYSIS

Commission Staff has reviewed Company's Application and accompanying testimony of Matt Larkin, along with the resolution adopted by the National Association of Regulatory Commissioners ("NARUC") encouraging State utility commissions to consider improving the regulatory treatment of cloud computing arrangements. Based on its review, Staff recommends that the Commission issue an order authorizing the deferral of reasonable and prudent costs associated with future cloud computing arrangements to a regulatory asset to be eligible for rate base treatment. Additionally, Staff recommends that the Commission also authorize the associated annual amortization expense be eligible for potential recovery in a future rate proceeding. However, to be consistent with the accounting treatment for capital expenditures included in Plant-in-Service, Staff recommends the Company begin amortizing the cloud computing arrangements when placed in service and it becomes used and useful. Staff discusses its recommendation in greater detail below.

### Cloud Computing

Cloud computing is the delivery of computing services that include software, servers, storage, databases, networking, and other forms of IT over the internet, or "cloud". Cloud computing arrangements differ from traditional, on-premise IT solutions.[1] The basic notion behind cloud computing is that the location of the hardware or operating system on which a product is running is irrelevant to a user, allowing products to be updated easily and often with minimal business disruptions. Due to changes in technology over the last several decades, cloud computing solutions have evolved leading to the current environment that sometimes favors cloud-based solutions over on-premise solutions. The most common cloud computing services include storage, networking, processing power, and standard office software applications.

Cloud computing services can provide a utility with access to vendors who operate specialized technology, while providing a way to address technological obsolescence as the contracts with these companies allow for renewals that use the latest technologies. These cloud computing services have increased the functionality of IT, offering faster and more flexible resources in a secure manner. The Company has entered into several arrangements for cloud

[1] On-premise IT solutions are onsite products or applications for which the Company must buy a license or copy of the software and are stored or maintained on-site.

computing services covering a broad array of applications necessary to provide essential services to customers because on-premise solutions had either become obsolete or were cost prohibitive.

An advantage of cloud computing is the ability to allow current IT staff to focus on other issues within the Company. The Company could potentially save additional resources, including: time, hiring new Staff, and replacement of outdated IT infrastructure. The Company did not provide the potential cost savings it expects from using cloud computing. Staff expects the Company to provide the benefits and cost savings in a future rate case proceeding.

**Accounting Treatment**

Current Accounting Treatment

Fee structures for cloud computing arrangements can vary but generally reflect a monthly, quarterly, or annual payment schedule. For a traditional on-premise IT solution, an upfront payment can be made in return for a reduced monthly fee—or no ongoing fee at all—over the course of the contract period. The costs of cloud computing arrangements however are not accounted for the same way as costs associated with the purchase of traditional on-premise IT solutions. Based on current accounting guidelines, the Company currently classifies investments in traditional on-premise IT solutions, including the integration costs, as a capital expenditure. Cloud-based products and services are generally accounted for as operating expenditures, except for the implementation and integration costs—which can be capitalized.

Traditional on-premise IT solutions are capitalized with the book value, net of accumulated depreciated, included in rate base. The Company begins depreciating the on-premise IT assets when it is placed in service and becomes used and useful. In a rate proceeding, the Company can recover the annual depreciation expense and earn a return on the undepreciated book value remaining.

In April 2015, Financial Accounting Standards Board ("FASB"), issued Accounting Standards Update No. 2015-05 to Accounting Standards Codification ("ASC") 350-40: Accounting for the Costs of Computer Software Developed or Obtained for Internal Use, which provides further direction and treatment for cloud computing. The update provided additional guidance of how to treat software license fees, and under certain conditions in which fees can be considered intangible assets and therefore be capitalized. The Company states that no cloud computing arrangements to date have been capitalized. In Accounting Standards Update

("ASU") No. 2018-15, FASB again provided additional clarification and provided users an opportunity to capitalize and amortize the costs over the term of the cloud computing arrangement.

On December 20, 2019, the Federal Energy Regulatory Commission ("FERC") issued Docket No. AI20-1-000, that provided additional guidance to utilities regarding cloud computing arrangements involving a service contract. "ASU No. 2018-15 clarifies that an entity obtaining a service contract in a cloud computing arrangement should follow the existing guidance [ASC] 350-40 to determine which implementation costs can be capitalized…shall be amortized over the term of the associated arrangement." ASC 350-40-35-13 states, "a Service Contract … shall be amortized over the term of the associated hosting arrangement, on a straight-line basis." ASC 350-40-35-17 provides additional guidance which states, "each module or component of a hosting arrangement, an entity shall begin amortizing the capitalized implementations costs related to the hosting arrangement that is a service contract when the module or component … is ready for its intended use." Staff has reviewed the different orders and guidance cited by the Company and believes that if all costs associated with a cloud computing arrangements are deferred, then the Company should begin to amortize said costs when its placed into service and ready for its intended use.

Proposed Accounting Treatment

The Company proposes to capitalize all costs associated with cost-effective cloud computing arrangements because the services provide the Company with an investment equivalent to that of a traditional on-premise IT solution. A deferral mechanism would remove a financial disincentive for the Company to pursue cost effective, cloud-based IT solutions that exist today.

The Company's proposed accounting treatment would book all cloud computing transactions, including implementation costs, integration costs, and licensing fees to a regulatory asset. The Company proposes that the regulatory asset would be eligible for rate base treatment, and the associated amortization expense be eligible for recovery in the Company's next general rate case. Matt Larkin states the Company prefers similar treatment to traditional on-premise IT solution, which, if applied, would provide the Company the most value without forcing the Company to base its IT decisions on regulatory accounting incentives. Larkin, DI page 15-16.

Staff does not disagree with this statement but is concerned that the Company is only making economic cloud computing arrangements if there are incentives to the Company.

To be consistent with the recovery of on-premise IT solutions, Staff recommends that the Company begin amortizing deferred costs of the cloud computing arrangement when it is ready for its intended use. The amortization period for each arrangement should be the length of the specific contract for that arrangement. If no contract period exists, Staff recommends an amortization period of 5-years, which is consistent with the depreciation life of FERC Account 303, Miscellaneous Intangible Plant. This recommendation removes the disincentive for the Company to invest in cloud-based IT solutions. Staff recommends using the FERC accounts proposed in the Company's Application, as they would be used for on-premise IT investments.

**STAFF RECOMMENDATION**

Staff recommends the Commission approve the deferral of costs associated with future cloud computing arrangements to a regulatory asset account, with amortization of the arrangements to begin when they are placed in service and become used and useful. Staff further recommends that the Commission establish the amortization period of the cloud computing arrangement to match the length of the service contract, or if the contract length is indeterminant, the amortization period should default to 5 years. The book value of any prudent cloud computing arrangements, net of accumulated amortization, will be eligible for rate base treatment in the Company's next general rate case, and any remaining amortization expense for prudently incurred cloud computing expenditures will be eligible for recovery.

Respectfully submitted this 21st day of May 2020.

Dayn Hardie
Deputy Attorney General

Technical Staff: Travis Culbertson
Rachelle Farnsworth

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## CERTIFICATE OF SERVICE

I HEREBY CERTIFY THAT I HAVE THIS 21st DAY OF MAY 2020, SERVED THE FOREGOING **COMMENTS OF THE COMMISSION STAFF,** IN CASE NO. IPC-E-20-11, BY E-MAILING A COPY THEREOF, TO THE FOLLOWING:

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