

# PUBLIC UTILITIES

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## THE SERVICE CHARGE AND ITS DEVELOPMENTS IN NEW YORK

The service charge doctrine has been actively sponsored by the national utility associations, and has obtained the support of most of the engineers who have had to do with rates, particularly those employed by the companies. It has also been avowed by a considerable number of commissioners, who have been almost incessantly bombarded with "scientific" literature and discussion by representatives of the utility organizations. But, in reality, there has been little of real scientific research, little impartial analysis; and the broad public side has received scant consideration.

### THE NATURE OF THE SERVICE CHARGE

The service charge consists of a separate charge made for the rendering of service, as distinguished from the delivery of gas or electricity itself. In its direct form, it appears as a fixed sum per month per customer (commonly \$1.00) to cover all the costs which are held to be customer costs, such as meter reading, billing, collecting, and similar items which can be more or less directly identified as due to the number of customers and not to gas or electricity delivered.

The service charge idea has been incorporated in the rate structures in so many different forms, that we shall not endeavor to present a detailed description. In its direct form it has met almost general resistance on the part of ordinary domestic consumers; hence, it has been extensively modified, so as to include a small quantity of gas or electricity with the fixed monthly charge. But this modification has been recognized as an evasion, and has met almost as much resistance as the direct service charge.

### DISTINGUISHED FROM MINIMUM BILL

The service charge form of rate is generally distinguished from the minimum bill, which has been rather widely recognized as a reasonable provision. The minimum bill, also, fixes a definite monthly sum to be paid by the consumer;

but the amount may be applied to a substantial quantity of gas or electricity. Thus; for a fixed minimum bill of \$1 per month, the customer would be entitled to receive 800 cubic feet, or some other substantial amount of gas, or 10 kilowatt hours of electricity.

The object of the minimum bill is fundamentally the same as that of the service charge—to protect the company against losses on the part of very small customers who require as much attention, and to a certain extent involve as much cost, as do the larger customers. The difference between the two types is that the one provides a distinct charge without any gas or electricity, while the other permits the consumer to use a substantial amount of gas or electricity for the amount paid. The service charge, therefore, makes the ordinary or small users pay a higher average rate than the large consumers; and, whenever it is first introduced, results in raising the bills of about two-thirds of the customers, and in reducing the bills of the much smaller group of larger customers.

### THE SPREAD OF THE SERVICE CHARGE

The drive on the part of the companies has been for the service charge, or its equivalent, with a very small quantity of gas or electricity included with the initial charge. This form of rate has been rapidly extended throughout the country. For the most part, it has been introduced by the companies with the more or less tacit approval of the commissions. The opposition has consisted almost altogether of declaration and rhetoric, rather than cost analysis with relation to a reasonable schedule of rates.

Where any substantial effort was made to support the service charge with proof, the companies have generally presented cost allocations patterned after the analysis sponsored by the national associations. In these calculations, all costs were divided into two groups: (1) Those supposedly dependent upon the number of cus-

tomers, and (2) those dependent upon the quantity of gas or electricity used. If the underlying assumptions as to the *cause* of the costs were to be accepted, and if the allocations were properly made, then unquestionably the first group would be properly divided equally between the number of customers, and the second equally by the quantity of gas sold. The result would be an equitable rate for all consumers.

But, the difficulty has been with the basic assumptions and with the practical subdivisions into the assumedly fundamental group, and, in part, with the disregard of other considerations that enter into a reasonable rate schedule. There are, of course, distinct customer costs, and definite commodity costs; but most of the costs incurred by a company do not fall into this simple grouping, but have mostly been arbitrarily classified as customer costs. This applies to all the general and miscellaneous expenses, to most of the supervisory costs, and to the bulk of the taxes and return on property used in the public service. These are all more or less fixed costs or overheads, and do not depend directly on either the number of customers or quantity of gas or electricity sold. Their inclusion among customer costs is wholly arbitrary, and produces a service charge which is excessive and discriminatory against the smaller users.

The character of these relatively-fixed and non-variable costs, and their relation to a reasonable schedule of rates have been ignored in practically all of the service charge cases. These costs not only do not depend upon the number of customers, but mostly they vary enormously with conditions under which customers are served. Take, for example, the costs relating to distribution mains (or lines) and services. In territories of elaborate single-family houses, the cost per customer is large; while in sections of large apartment houses, the cost per customer is low; but, at the same time, the larger users live mostly in single family houses, and the smaller users in apartments. If, under these circumstances, all such costs are divided equally per customer, and are thus included in a service charge, the smaller customers obviously are compelled to pay costs which are due largely to conditions under which the larger customers are served.

This cost relationship between size of customers and conditions under which the service is furnished, has practically been ignored by the commissions—because it has not been adequately brought out by the opponents of the service

charge. Up to the time the New York cases were first heard in 1928, these variations in relative costs with different conditions of service, were never presented to the commissions, and the service charge had become widely accepted, on the erroneous assumption that the costs were due to customers and were the same per customer under all conditions of service.

#### THE SERVICE CHARGE IN NEW YORK

The service charge movement struck its first intensive resistance in the state of New York. In 1923, after the gas companies (which, much more than the electric companies, have forced the service charge type of rate), had attempted to introduce the service charge extensively throughout the state of New York, the legislature blocked the effort by amending the Public Service Commissions Law so as to make the service charge illegal for gas companies.

Immediately after the enactment of the bill prohibiting the service charge, a considerable number of companies merely changed the rate, from a direct service charge, to the so-called "initial charge," by allowing the consumer, for such a charge, 100 or 200 cubic feet of gas. This modification was, manifestly, a thinly-disguised service charge; but it was permitted to go into effect by a commission which as then constituted was none too critical of the proposals of the companies.

This was the situation in the summer of 1927, when the Brooklyn Borough Gas Company filed a new schedule of rates which, for domestic consumers, replaced the flat rate of \$1.30 per M cubic feet of gas, with \$1 a month per customer for the first 200 cubic feet of gas or less, and 11 cents per hundred cubic feet for additional gas consumed per month. This rate became legally effective before the consumers were aware of the change. But with the receipt of the first bills under the new schedule, active opposition started, and the commission was petitioned to investigate the legality and the reasonableness of the initial charge. Before the inquiry got far under way, the Brooklyn Union Gas Company filed a similar schedule of rates, which was immediately suspended by the commission, pending investigation of its reasonableness. The two sets of hearings were then continued simultaneously; but in the Brooklyn Borough case the new form of rates was in effect, while in the Brooklyn Union case it was suspended, and the old flat rate of \$1.15 per M cubic feet remained.

Just as the procedures in the two cases were different, so the decisions were out of harmony. Although the same issues and the same kinds of facts were presented in the two instances, in the Brooklyn Union case the proposed schedule was rejected, while in the Brooklyn Borough case it was approved. In both cases, however, petitions were filed promptly for re-hearing.

#### EXTENSION TO ELECTRICITY

Before the re-hearings in these gas cases were completed, the same issue was raised as to electric rates. The four electric companies in the Consolidated Gas system, which supply the bulk of electricity in different sections of New York City, filed a new schedule of rates in the summer of 1930. Their rate schedule had differed widely, both as to form and as to level of charges for similar kinds and quantities of service, and the new schedules proposed uniform rates throughout. They provided a direct 60 cents service charge per month, and a 5 cent rate for practically all electricity used for residential purposes.

This proposal met with opposition, because the 60 cents service charge would result in increasing the rates to the ordinary and small users, against a decrease for large users. In Manhattan especially, there had been the single flat rate of 7 cents per kilowatt hour up to 1000 kilowatt hours a month. The new schedule would result in an increase for all customers up to 30 kilowatt hours per month, and a reduction for those above that quantity. Since the small users are mostly apartment house dwellers, and since Manhattan is mainly an apartment house territory, the increases would apply heavily to Manhattan consumers.

In the case of electricity, the only question raised was the reasonableness of the service charge, and not its legality, because the legislative prohibition did not extend to electric rates. The commission announced, however, early in the electric hearings (also about the same time in the gas hearings), that it would consider all three cases on the same basis, notwithstanding the difference in legal status.

#### THE RECENT DECISIONS

Early in the summer of 1931, the commission decided, first, the electric case, and then the gas cases. Its interest was centered especially upon the desirability of uniformity and the establishment of proper type of rates not only in New York but throughout the state. The actual

decisions carry the sign of compromise, so far as specific provisions within the general form of rate adopted are concerned.

In general, the service charge was rejected as a desirable part of a schedule of gas or electric rates. The rejection was based partly upon the difficulty or impossibility of determining a reasonable service charge which would operate equitably throughout among all classes of consumers; and partly upon the fact that there is the psychology of resistance against the service charge.

The commission, however, recognized the fact that there are certain inescapable costs incurred by the companies as long as customers are attached, even though they use no gas or electricity. To meet this condition, and to prevent such outright costs to be paid by other customers, the commission adopted a minimum bill, under which the customers are allowed a substantial quantity of gas or electricity with the fixed monthly amount paid.

The minimum bill, both for gas and electric companies, was put at \$1 a month per customer. For gas, there was included in the minimum bill 600 cubic feet per month per customer for the Brooklyn Union Gas Company, and 500 cubic feet for the Brooklyn Borough Gas Company.

For electric residential customers, the minimum bill of \$1 allows 10 kilowatt hours; the next 5 kilowatt hours are furnished at 6 cents, and all over 15 kilowatt hours, 5 cents per kilowatt hour.

#### AN INDIRECT SERVICE CHARGE

Analysis of these rates shows that the commission does provide for an indirect service charge, as embodied in the minimum bill and, in the case of electricity, in the somewhat higher intermediary charge between 10 and 15 kilowatt hours per month. In the case of gas, the follow-up commodity rates were not definitely fixed. It is assumed, however, that for the Brooklyn Union Company the follow-up rate will be 9 cents per 100 cubic feet, and for the Brooklyn Borough 10 cents. On this basis, all consumers who use at least the amount of gas provided for in the minimum bill, will pay a service charge of 46 cents to the Brooklyn Union, and 50 cents to the Brooklyn Borough.

Similarly for the electric companies, the ordinary consumers who use at least 15 kilowatt hours a month, the indirect service charge comes to 55 cents a month. Those who use less than the amount of gas or electricity allowed in the mini-

imum bill, will pay more than the standard indirect service charge, and the maximum comes to \$1 per month per customer.

Thus considered, the standard service charge ranges from 46 cents a month for the Brooklyn Union, to 55 cents a month for the electric companies. In each case, however, the customer is entitled to a substantial quantity of gas or electricity with the fixed one dollar per month. The schedules tend to meet the requirement of reasonable rates, as well as the legal prohibition of the service charge for gas.

The one dollar per month as thus fixed cannot be designated directly as a service charge in form. It is of the minimum-bill type, which was not prohibited by the New York statute, and which is generally distinguished from the service charge form.

Considered merely as to the amount of the indirect provisions to meet the cost of service, as distinguished from charges for gas or electricity, a charge of 46 cents to 55 cents cannot be regarded as unreasonable. If distinct provisions are to be made, directly or indirectly, in a rate schedule for the rendering of service, then the amount could not be much less than established indirectly through the type of minimum bill as fixed by the commission.

#### DOUBT AS TO REASONABLENESS

Under New York City conditions, and generally under conditions prevailing in cities throughout the country, there is doubt whether even such a moderate, indirect service charge should be imbedded in the schedule of rates for domestic users. While, of course, there are distinct service costs which, *considered by themselves*, would under most city conditions come close to 50 cents a month per customer, this is not all there is to an appropriate cost analysis. There is, first, the question whether all properly determined customer costs are really equal, per customer, for all customers. And there is the second question, as already indicated, whether the relatively fixed costs do not vary greatly with service conditions, and whether in reality they should not properly be allocated much more per customer to the larger users.

In New York, and in most cities, there is a wide difference in service costs between different customers. There is a still greater difference in the fixed costs imposed upon the company by the relative conditions under which different classes of customers are served. If these dif-

ferences are properly considered and balanced against the service costs, in our judgment the validity of a standard service charge disappears, and a flat rate with a minimum bill seems the most reasonable all-around rate for domestic schedules.

As applied to the New York rates, there is grave doubt whether there is justification for a higher commodity rate applied to the gas included in the fixed monthly charge than for consumption beyond the initial quantity.

#### APARTMENT HOUSE CUSTOMERS

While there are all kinds of variations in conditions under which different classes of customers are served, the most significant distinction in New York, and in most cities, appears between the mass of apartment house users and consumers in single family houses. The small users, as a class, dwell mostly in apartment houses, while the larger users, as a class, dwell in single family houses. If all the costs relating to these classes are carefully analyzed, it will appear that the cost per customer is much less for the apartment house consumers than for the single family house consumers. This applies not only to ordinary service costs but particularly to fixed costs; less, generally, per customer for the small users, and more for the large consumers.

If, therefore, a separate service charge is to be established in the rate structure, there should equitably be a distinct difference in the amount for the two classes of conditions, and there should also be variations for intermediary circumstances. But the fixing of different service charges for different conditions leads to complication of rate structure and would probably not be practicable. Hence, to offset the conditions of lower customer costs and fixed costs for customer for the small users in apartments, as against the higher per capita costs for the larger users in the single family houses, the flat rate automatically provides a balancing of the obverse cost factors. While it would overburden the small apartment house customers with some costs, it would undercharge them as to others; and it would affect obversely the large single family house users. There is, in our judgment, no single and simple form of rate which, in a large territory, meets all-around more equitably the wide variations in service conditions. There is, however, justification in coupling the flat rate with a moderate minimum bill, to protect the company against losses from very small users.