Fact Sheet
Local Government

# Estimating future rate pegs

16 April 2024

## 1 We changed our rate peg methodology in 2023

As part of our 2023 Review of the rate peg methodology, we made major changes to the rate peg methodology which we implemented for the rate peg for the 2024-25 financial year.

The new method for setting the rate peg is simpler than the old method and will result in rate pegs that more accurately reflect changes in the costs NSW councils incur in providing their current services. For more information see our Final Report.

Our new rate peg methodology is described by the following formula:

$$Rate\ peg = Base\ Cost\ Change\ (BCC)\ model - productivity\ factor + population\ factor \\ + Emergency\ Services\ Levy\ (ESL)\ factor + other\ adjustments$$

Our new rate peg methodology:

- Measures the annual change in NSW councils' base costs for 3 groups of councils (metropolitan, regional, and rural councils).
- Uses a new, simpler model with forward-looking indicators to measure this change, known as the Base Cost Change (BCC) model. It comprises 3 components:
  - Employee costs (primarily wages, including superannuation guarantee) measured by the Local Government (State) Award (Award). However, if the Award increase is not known at the time we set the rate peg (around September), we will use the Reserve Bank of Australia's (RBA's) WPI forecast.
  - Asset costs measured by the RBA's forecast change in the Consumer Price Index (CPI), adjusted to reflect the average 5-year historical difference between changes in the Producer Price Index (PPI) (Road and bridge construction, NSW) and changes in the CPI.
  - All other operating costs (including administration, utility costs, insurance but excluding the Emergency Services Levy (ESL)) measured by the RBA's forecast change in the CPI.
- Includes a separate council-specific ESL factor, lagged by one year,[a] that reflects the annual change in each council's ESL contribution.
- Maintains our existing approach of making additional adjustments for costs driven by external factors outside councils' control as needed, if ratepayers will benefit from these costs and we have the information we need to calculate the necessary adjustment.
- Continues to add a population factor but uses a refined approach to more accurately measure the change in councils' residential populations by excluding prison populations.
- Retains the productivity factor at a default value of zero.

[a] For example, the ESL factor in the rate peg for the 2024-25 financial year will capture the change in invoiced ESL contributions amounts between the 2022-23 and 2023-24 financial years (adjusted for cost sharing arrangements for specific councils).

# 2 Estimating future rate pegs

This Fact Sheet provides advice on estimating the rate peg under the new methodology, which uses forecasts, to assist councils in long term financial planning. Councils may also use different forecasts. We note that the 'other adjustments' to the rate peg are at the discretion of the Tribunal.

## Table 2.1 Estimating future rate pegs by rate peg component

| Rate peg component | How is it measured? | Estimating the rate peg one year in advance (e.g. for 1 July 2025) | Estimating the rate peg beyond one year in advance (e.g. from 1 July 2026) |
|---|---|---|---|
| Base cost change (BCC) model | The BCC is a weighted average of forecast inflation (CPI and PPI)[a] and the expected increase in employee costs.<br>In the rate peg, employee costs make up around 40% of total costs.<br>Our estimate of PPI is based on CPI forecasts because PPI forecasts are not available. | RBA's latest available CPI forecast x 60% + Award increase[b] x 40%.<br><br>E.g. For 2025-26:<br>2.6% x 60%+ 3.5% x 40% = 3.0%.<br><br>The RBA's forecasts are available in the Statement on Monetary Policy. | Use the midpoint of RBA's target range for inflation (2.5%) x 60% + your estimate of the increase in Award wages x 40%.<br><br>E.g. From 2026-27: 2.5% x 60% + 3.0% x 40% = 2.7%. |
| Productivity factor | Default value of 0%. | Default value of 0%. | Default value of 0%. |
| Population factor | The population factor measures the annual change in residential population less supplementary valuations. Please refer to our Information Paper, *Rate peg for NSW councils for 2024-25* (pp 7-9). | Councils can estimate their population factors using information they have on population growth such as historical trends. Councils can refer to the rate peg formula in our Final Report, *Review of the rate peg methodology*, and use our rate peg model for the 2024-25 financial year. | Councils can estimate their population factors using information they have on population growth such as historical trends. Councils can refer to the rate peg formula in our Final Report, *Review of the rate peg methodology*, and use our rate peg model for the 2024-25 financial year. |
| ESL factor | The ESL factor is based on the year-on-year change in a council's ESL contributions with a 1-year lag. | Councils can estimate the ESL factor 1 year in advance once ESL contribution information is known in April, using the ESL calculator. | When the ESL contribution is not known yet a factor may be based on a reasonable estimate based on historical year-on-year changes in contributions or any known step changes. |
| Other adjustments | The rate peg for the 2024-25 financial year included an adjustment for some councils to account for ESL contribution increases that were not captured in the rate peg due to the NSW Government subsidy. | IPART will decide on other adjustments in consultation with the council implementation reference group and ratepayer workshops. | IPART will decide on other adjustments in consultation with the council implementation reference group and ratepayer workshops. |

a. CPI: Consumer Price Index and PPI: Producer Price Index.

b. In broad terms, the increase in employee costs is the permanent increase in Award wages plus the increase in the superannuation guarantee. The superannuation guarantee is expected to increase from 11.5% in 2024-25 to 12% in 2025-26. If the Award increase is not known at the time we set the rate peg (around September), we will use the RBA's WPI forecast plus the increase in the superannuation guarantee.

See our **website** for our:

**Rate peg model for the 2024-25 financial year** and **ESL factor and ESL adjustment factor calculator**

# 3 Estimating future rate pegs for SV applications

Councils applying for a special variation (SV) can use this guidance to estimate future rate pegs for financial years after the year where the rate peg is already set. For example, councils applying for an SV for the 2025-26 financial year would be able to use the rate peg set by IPART (around September 2024) in their applications.

For future years, the Office of Local Government (OLG) Guidelines refers to an assumed rate peg of 2.5%. If a council decides to follow the guidance in this Fact Sheet to estimate a rate peg that may be different to the assumed rate peg of 2.5%, the council would need to explain this and how it did so in the SV Part B application form. The requirement for a council to explain its estimated rate peg if it chooses not to use the assumed rate peg percentage still applies.

## 3.1 Councils should apply for the total percentage increase required

As set out in the OLG Guidelines, when a council applies for an SV, a council should identify the additional revenue required over the period and then apply for the annual percentage required to produce this amount.

The annual percentage variation in any SV instrument replaces the rate peg. It is not an incremental increase above the rate peg. There is no automatic adjustment where the actual rate peg in a year covered by an SV differs from the rate peg assumed at the time of the SV application.

However, where the rate peg for a particular year exceeds the annual percentage increase specified for that year in a section 508A multi-year special variation, then the council is entitled to increase its general income by the rate peg in that year.