

11 September 2018

WHAT

IPART has set the 2019-20 rate peg for NSW councils at **2.7%**.

The rate peg sets the maximum increase in each council's general income for the 2019-20 financial year. For most councils, general income consists entirely of rates revenue.

The rate peg is based on the change in the Local Government Cost Index (LGCI) and consideration of a productivity factor.

HOW

We calculated the rate peg for 2019-20 by:

- ▼ taking the increase in the LGCI to June 2018 of 2.7%, and
- ▼ setting the productivity factor to 0.0%.

WHO

Councils have discretion whether to increase rates up to the maximum, and how to allocate any increase between different ratepayer categories. Individual rates are also affected by other factors, such as land valuations.

Councils may apply to IPART for a special variation to increase general income above the rate peg.

WHAT'S NEW

We have changed when we release the rate peg, following consultation with stakeholders.

We are now releasing the rate peg in September. Councils agreed that this would give them more time to prepare annual budgets, and better engage with their communities on special variation applications.

To facilitate the earlier release of the rate peg, we have considered changes in costs measured by the LGCI up until the June quarter 2018.

WHAT NEXT

Councils have discretion to increase general income up to the rate peg, by less than the rate peg or not at all. However, councils must not increase general income by more than the rate peg, unless IPART grants approval for a special variation.

Councils applying for a special variation must satisfy the criteria listed in the Office of Local Government's Guidelines. The Guidelines will be available on IPART's website when published.

Councils applying for a special variation for 2019-20 must notify IPART by 30 November 2018.

IPART's website also includes general [information on the special variation requirements](#) and recent applications from councils.

1 What is the rate peg?

The rate peg is the maximum percentage amount by which a council may increase its general income for the year. For most councils, general income consists entirely of rates income. For a small number of councils, it also includes some annual charges such as drainage levies. The rate peg does not apply to stormwater, waste collection, water and sewerage charges. The rate peg applies to general income in total, and not to individual ratepayers' rates.

2 What is the Local Government Cost Index (LGCI)?

The LGCI is a price index for councils in NSW. It measures price changes over the past year for goods, materials and labour used by an average council. It is similar in principle to the Consumer Price Index (CPI) which is used to measure changes in prices for a typical household.

The LGCI is designed to measure the average change in prices of a fixed 'basket' of goods and services that are purchased by councils, relative to the prices of the same basket in a base period.

- ▼ The index has 26 cost components, such as employee benefits and on-costs, and building materials for roads, bridges and footpaths. The cost components represent the purchases made by an average council to undertake its typical activities.
- ▼ Each year, the ABS adjusts the change in the price of each cost component for improvements in both labour and capital productivity, by adjusting the price downwards for any improvement in the quality of that component.

To calculate the LGCI in 2019-20, we combined the 26 cost components using expenditure weightings in a 2015 cost survey (based on NSW councils' expenditure in 2013-14 and 2014 - 15). We aim to update the expenditure weightings every four years to ensure the impact of each cost item on the LGCI remains accurate.

For more detail on the Local Government Cost Index see our Fact Sheet, *Local Government Cost Index Survey 2015* published in October 2015. This is available on our [website](#).

What price changes influenced the LGCI?

We used the change in the LGCI to June 2018 when setting the rate peg for 2019-20. This change in the LGCI was 2.7%. The main contributors to the change in the LGCI for the period ending June 2018 were an:

- ▼ increase of 2.4% in employee benefits and on-costs, measured by the ABS wage price index for the NSW public sector
- ▼ increase of 14.4% in electricity and street lighting charges, measured by the ABS consumer price index for electricity costs – Sydney, and
- ▼ increase of 2.4% in construction works – roads, drains, footpaths, kerbing, bridges costs, measured by the ABS producer price index for roads and bridge construction – NSW.

Most components of the LGCI experienced moderate price inflation over the period to June 2018 (see Section 4 below for a table showing the price changes in cost items for all components of the LGCI).

3 Setting the rate peg in September

In consultation, and in previous submissions, councils have indicated to IPART they would prefer the rate peg to be released earlier than in previous years, to allow more time to prepare annual budgets, even if they do not apply for a special variation.

We have changed the timing of the release of the rate peg and will now set the rate peg in early September each year, rather than around the beginning of December as in previous years. This change applies for the 2019-20 rate peg and thereafter.

This change will improve the community consultation component of the special variation process for councils and enable ratepayers to have a clearer understanding of what is proposed. Councils will also have more time to prepare an application for a special variation knowing the rate peg for the following year and more time to prepare annual budgets even if they do not apply for a special variation.

This earlier notification should help councils that apply for a special variation to improve consultation with their communities. In practice, most councils that apply for a special variation begin their community consultation and Integrated Planning and Reporting documentation before December. Previously, these councils may have needed to amend their documentation and consult further after the rate peg announcement.

Releasing the rate peg earlier reduces this problem by allowing councils to include the actual rate peg in their consultation before December.

How are we transitioning to a September release?

In previous years, we calculated the rate peg based on annual data up to and including September. This gave us four quarters of annual data on which to make our calculations.

As we have brought forward when we set the 2019-20 rate peg by three months, the approach for the 2019 - 20 rate peg uses three quarters of annual price changes up to June 2018 (December 2016 to December 2017, March 2017 to March 2018 and June 2017 to June 2018). The method is:

$$\frac{LGCI (Dec 2017) + LGCI (Mar 2018) + LGCI (Jun 2018)}{LGCI (Dec 2016) + LGCI (Mar 2017) + LGCI (Jun 2017)} - 1$$

Given the change in our method this year, we cross-checked this method by using two alternative approaches. Both these approaches incorporated four quarters of annual data by using a proxy for the September quarter. Both produced comparable increases in the LGCI.

In future years, the LGCI will be based on four quarters of annual price changes up to June. That is, for the 2020-21 rate peg we will use:

$$\frac{LGCI (Sep 2018) + LGCI (Dec 2018) + LGCI (Mar 2019) + LGCI (Jun 2019)}{LGCI (Sep 2017) + LGCI (Dec 2017) + LGCI (Mar 2018) + LGCI (Jun 2018)} - 1$$

The underlying data series used to calculate the LGCI are available quarterly, and we do not propose to change the underlying methodology.

4 Change in the LGCI for the year ended June 2018

Cost items	Effective weight as at end-Jun 2017 (%)	Price change to end-Jun 2018 (% annual average)	Contribution to index change (percentage points)
Operating cost items			
Employee benefits and on-costs	41.7	2.4	0.98
Plant & equipment leasing	0.3	1.0	0.00
Operating contracts	1.0	3.1	0.03
Legal & accounting services	0.8	2.6	0.02
Office & building cleaning services	0.3	4.5	0.01
Other business services	6.0	2.5	0.15
Insurance	1.7	3.3	0.06
Telecommunications, telephone & internet services	0.5	-4.1	-0.02
Printing publishing & advertising	0.5	0.9	0.00
Motor vehicle parts	0.3	2.4	0.01
Motor vehicle repairs & servicing	0.6	1.1	0.01
Automotive fuel	0.7	12.1	0.09
Electricity	2.7	14.4	0.40
Gas	0.1	8.0	0.00
Water & Sewerage	0.3	2.0	0.01
Road, footpath, kerbing, bridge & drain building materials	2.4	2.4	0.06
Other building & construction materials	0.5	3.4	0.02
Office supplies	0.2	2.5	0.01
Emergency services levies	1.4	2.0	0.03
Other expenses ^a	8.9	2.1	0.19
Capital cost items			
Buildings – non-dwelling	4.1	3.4	0.14
Construction works – roads, drains, footpaths, kerbing, bridges	19.2	2.4	0.46
Construction works – other	1.9	2.4	0.05
Plant & equipment – machinery, etc	3.4	0.4	0.01
Plant & equipment – furniture, etc	0.1	0.9	0.00
Information technology & software	0.4	-2.8	-0.01
Total	100.0		2.7

^a Includes miscellaneous expenses with low weights in the Index, eg, councillor and mayoral fees.

Note: Figures may not add due to rounding. Percentage changes are calculated from unrounded numbers.