

FACT SHEET

Carbon price advance to the 2012/13 rate peg

6 December 2011

IPART has included a carbon price advance of 0.4% in the rate peg for 2012/13. This fact sheet includes a short explanation of how we have set the carbon price advance in the rate peg.

What is the rate peg?

The rate peg determines the allowable increase in local councils' general income. General income mainly includes income from council rates, but also includes certain other types of council income.

IPART has set the rate peg percentage for 2012/13 at 3.6%. We set the rate peg using the following approach:

- ▼ we took the increase of 3.4% in the Local Government Cost Index (LGCI) for the year to September 2011
- ▼ we deducted a productivity factor of 0.2%
- ▼ for this year only, we have added a carbon price advance of 0.4%.

We have included the carbon price advance because the LGCI we used to set the rate peg for 2012/13 includes price data up to September 2011, so it does not include the impact on prices of the introduction of the carbon price.

How will the carbon price impact local councils?

The carbon price will impact councils as producers of emissions and as consumers of goods and services:

- ▼ As producers of emissions exceeding 25,000 tonnes of CO₂-e per annum through the operation of waste landfill facilities.
- ▼ As consumers of inputs, for example, as purchasers of electricity for a range of purposes, including street lighting, council buildings, water and sewerage operations and swimming pools. There will also be a reduction in fuel tax credits for some fuel uses eg, off-road vehicle use.

This fact sheet principally concerns the impact on councils as consumers of inputs, since this is relevant for the rate peg.

We estimate that the rise in electricity prices will account for around half the impact of the carbon price on council costs as consumers of inputs ie, excluding waste management costs. The other council costs most affected are likely to be those related to construction (steel, bitumen, concrete and timber).

Councils set their waste management charges based on the reasonable costs of providing their waste management services. These costs are audited. This will continue to be the case.

What is the carbon price advance and why is this necessary?

The carbon price advance increases the 2012/13 rate peg by 0.4%. The advance will increase councils' general income and assist them in meeting higher prices resulting from the introduction of the carbon price.

The advance is necessary because the rate peg for 2012/13 is set using past prices. The LGCI includes price data for the year to September 2011 as this is the latest data available at the time we determine the rate peg. The LGCI does not yet include the impact of the carbon price to come into effect from 1 July 2012.

The effects of the carbon price will gradually flow through to electricity and other prices used in the LGCI in 2013/14 and 2014/15. The advance will assist councils with their cash flow until this occurs.

How have we calculated the carbon price advance?

Estimates of the effect of the carbon price on a range of consumer prices have been made by the Commonwealth Treasury.

We have used Commonwealth Treasury estimates of the impact of the carbon price on the Consumer Price Index and some of our own.

We have applied relevant estimates to the cost indices in our LGCI.

On this basis, we estimate that when the carbon price flows through the economy into prices, the impact on the LGCI will be an increase of 0.6%.

Why have we set the carbon price advance at 0.4%?

We have used Commonwealth Treasury estimates of the impact of the carbon price on the Consumer Price Index and applied relevant estimates to our LGCI. This calculation implies that the LGCI will increase by 0.6% in a full year.

We consider that this estimate could overstate the impact of the carbon price on the index because there are a number of factors that are not reflected in the calculation. For example:

- ▼ We assume that there is immediate and full pass-through of the carbon price, and buyers continue to purchase the same goods and services, despite changes in relative prices. In all likelihood, there may be either a delay in passing on the effects of the carbon price or the pass-through may only be partial as some businesses absorb some of the impact.
- ▼ Several Commonwealth Government schemes are available to councils to fund various energy efficiency and other schemes. This should help to offset the impact of the carbon price on councils' total costs, even if they cannot avoid the impact on the unit costs they face.

We cannot be certain of the speed or size of the pass-through of increased prices to councils, nor the value of the offsets that councils as a whole may gain. Therefore, as a matter of judgment, we decided to set the carbon price advance in the rate peg for 2012/13 at 0.4%.

The actual impact of the carbon price will eventually be reflected in the price indices we use in the LGCI.

Why is IPART reversing the carbon price advance over 2 years?

If we did not reverse the carbon price advance, we would be double-counting the effect of the carbon price in the rate peg.

The effects of the carbon price will flow through to electricity, building costs and other prices used in the LGCI in 2013/14 and 2014/15. We will make a downward adjustment to the rate pegs in these years to reverse the carbon price advance made in 2012/13. We will remove 0.1% of the advance in the 2013/14 rate peg and 0.3% of the advance in the 2014/15 rate peg.

What is the impact on councils' waste charges?

IPART has not estimated the impact of the carbon price on council waste services, since waste services are excluded from the rate peg.

NSW councils recover their waste management costs by levying charges based on recovering the reasonable costs of providing the service. Councils levy annual domestic waste management charges for domestic waste management services made available to households. Councils are required to maintain separate accounts on their waste management services and their accounts are audited. This arrangement will remain in place.

Want more information?

See the IPART website for related information papers:

- ▼ 2012/13 rate peg
- ▼ Effects of the carbon price on local councils.

Go to the IPART website:

<http://www.ipart.nsw.gov.au/local-government/local-government.asp>