

TO:	CHAIR AND MEMBERS FINANCE AND ADMINISTRATIVE SERVICES COMMITTEE MEETING ON MARCH 26, 2012
FROM:	MARTIN HAYWARD CITY TREASURER, CHIEF FINANCIAL OFFICER
SUBJECT:	YEAR 2012 TAX POLICY

RECOMMENDATION

That, on the recommendation of the City Treasurer, the following actions be taken with respect to property taxation for 2012:

1. A by-law be enacted in accordance with Sub-sections 308(4) and 308.1(4) of the Municipal Act, 2001 to set tax ratios in the multi-residential, pipeline and farm property classes as indicated on Schedule G and such proposed by-law (Appendix A) **BE INTRODUCED** at the Council meeting of April 10, 2012;
2. A by-law be enacted in accordance with Sub-section 308(4) of the Municipal Act, 2001 to set tax ratios in the commercial and industrial property class as indicated in Schedule G of this report; so that tax ratios for these classes are maintained at Provincial thresholds/averages and such proposed by-law (Appendix A) **BE INTRODUCED** at the Council meeting of April 10, 2012;
3. A by-law be enacted to fully utilize options available in 2012 to exclude properties in capped property classes which have reached current value assessment tax levels or higher in 2011 from being capped again in 2012 and future years and such proposed by-law (Appendix B) **BE INTRODUCED** at the Council meeting of April 10, 2012;
4. A by-law be enacted in accordance with Section 330 of the Municipal Act, 2001 to claw back a portion of tax decreases in each of the commercial, industrial, and multi-residential classes sufficient to fully finance the capping of increases as required under Section 329 of the Municipal Act, 2001 and such proposed by-law (Appendix C) **BE INTRODUCED** at the Council meeting on April 10, 2012;
5. A by-law be enacted in accordance with Section 329.1 of the Municipal Act, 2001 for 2012 to adopt the same capping formulae for the commercial, industrial and multi-residential property classes as was applicable in 2011 and such proposed by-law (Appendix D) **BE INTRODUCED** at the Council meeting on April 10, 2012;
6. A phase-in program for tax changes resulting from the reassessment of properties in the residential, farmland, and managed forests property classes in accordance with Section 318 of the Municipal Act, 2001 not be adopted.

PREVIOUS REPORTS PERTINENT TO THIS MATTER
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Finance and Administrative Services Committee Report - January 16, 2012 – Assessment Growth for 2012, Changes in Taxable Phase-in Values, and Shifts in Taxation as a Result of the 2012 Changes in Taxable Phase-in Values
 Finance and Administration Committee Report - November 2, 2011 - Future Tax Policy

BACKGROUND

Recommendations 1 and 2 – Tax Ratios for 2012 Taxation

Definition of the Term “Tax Ratio”

Tax ratios compare the tax rate for municipal purposes in a particular property class to the residential class. The ratio for the residential class is deemed to be 1.00. A tax ratio of 2.00 would therefore indicate a municipal tax rate twice the residential municipal tax rate. Education tax rates are set by the Province and are not dependent on tax ratios approved by municipal Councils.

History of Tax Ratio Setting Restrictions

Beginning in the year 2001, the Province established threshold tax ratios for three property classes - commercial, industrial, and multi-residential. At the time, the Province indicated that these threshold ratios represented the Provincial average in each class. Under provisions of the Municipal Act and related regulations, municipalities were not permitted for the year 2001 or subsequent years to impose a general municipal levy increase on a property class which had a ratio exceeding the Provincial threshold or average. Beginning in 2004, this restriction was modified somewhat to permit levy increases at half the residential rate in property classes with tax ratios above Provincial thresholds. The Province has advised that this flexibility will be provided to municipalities again for 2012 taxation.

London’s Tax Ratios, Provincial Thresholds, and Municipal Comparisons

In reviewing tax policy for 2012, it should be noted that none of the property classes in the City of London are above the Provincial thresholds. The only property class in London that was ever above the Provincial threshold was the industrial class. Council moved the industrial ratio down to the threshold for 2001 taxation. At the time of the last reassessments in 2006 and 2009, Council maintained the policy of not permitting tax ratios in any property class to exceed Provincial thresholds.

Schedule A attached, summarizes the tax ratios for all municipalities with populations greater than 100,000 included in the 2011 Municipal Study prepared by BMA Management Consulting Inc. When residual and large industrial optional classes are combined, London is within about 8% of the median tax ratio value for all property classes on Schedule A, even without any weighting of the City of Toronto to reflect its size in the group. This would suggest that the relative treatment of property classes in London for the purposes of municipal taxation is reasonably close to the average range when considered in the context of the entire Province.

The tax ratios in effect for the year 2011 and their proximity to the Provincial thresholds or averages established in 2001, as well as the Provincial targets or allowable ranges can be summarized as follows:

	City of London 2011 Tax Ratio	Provincial Threshold/Average (O.Reg. 73/03)	Provincial Targets/Allowable Ranges (O.Reg. 386/98)
Commercial	1.980000	1.98	0.6 to 1.1
Industrial	2.630000	2.63	0.6 to 1.1
Multi-Residential	2.087700	2.74	1.0 to 1.1
Pipeline	1.713000	N/A	0.6 to 0.7
Farm	0.250000	N/A	N/A
Residential	1.000000	N/A	N/A

Schedule B attached, provides comparative information on how different municipalities tax the various different major property classes. The information from Schedule B comes from the 2011 BMA Municipal Study and includes all municipalities with populations greater than 100,000. The last column of Schedule B is a theoretical calculation that shows the tax increase that would be required in the residential property class in each municipality if all property classes had a tax ratio of 1. The Schedule indicates that the theoretical adjustment for the City of London would be close to the middle of the group without giving special weighting to Toronto to reflect its much larger size. Schedule B again suggests that the City of London's tax ratios are reasonably close to the average range and not unusual when compared to other major centres in the Province.

Tax Ratios, Economic Development, and Assessment Growth (Future Tax Policy)

While Schedules A and B indicate that the City of London's tax ratios are reasonably close to the average range and not unusual when compared to other major centres in the Province, it can be seen on Schedule A that the ratio for the industrial class in London is above both the median and the average. The industrial ratio is 7.1% higher than the group median and 9.7% higher than the group average. The industrial tax ratio is by far the highest tax ratio in the City being much higher than commercial. In recent years the Region of Waterloo has reduced tax ratios in the industrial class to the commercial level. As was discussed in the Future Tax Policy report delivered to Council in November 2011, there appears to be no logical basis for higher tax rates on industrial properties compared to commercial properties in Ontario. It seems to be the result of nothing more than historical tradition.

The issue of tax ratios and the possibility of reducing tax ratios in the industrial and multi-residential class was the subject of Future Tax Policy report presented to Council in November 2011. At that time concerns were expressed about the impact on the residential class of making any tax ratio changes for 2012, and the report was received for information. Comments were made during Council's deliberations to the effect that it would be advisable to look at the issue again in the future in conjunction with the new Province wide assessment coming in 2013. The Finance Department intends to follow that suggestion and to proceed with an in-depth review of the implications of the suggested ratio changes in 2013.

The key problem with the issue of changing tax ratios is that there will be both short-term and long-term consequences and the consequences will be very different based on the time frame you are considering. In the very short-term (i.e. the current year) the effect is very simple to calculate and results in taxes shifting away from the property class where a tax ratio is lowered and towards the other classes. In the longer term however, the design of tax ratios will have implications for the economic development opportunities that a municipality will attract, the number and type of jobs available in the community and the level of assessment growth in the municipality. These potential benefits will all come in the years that follow the year of the tax ratio change and will be dependent on how significant the tax ratio change is to the various property classes involved. The pattern of assessment growth in the City of London since year 2000 is presented in bar graph form as Schedule J attached to this report.

As was explained in the Future Tax Policy report presented to Council in November 2011, making the recommended changes to the industrial and multi-residential property in London in 2012 would not have had a huge impact on other classes in the short-term. It was calculated the impact would have been about 1.3% of the previous year's taxes for other property classes including residential and commercial. For a typical residential property this would have amounted to about \$31. On the other hand, the tax impact for industrial properties would have been significant. Industrial properties would have experienced a municipal tax decrease in the 23% range.

In the past the industrial sector has been an extremely important source of high quality jobs in Ontario and North America. As everyone is aware, the recent economic downturn which began in 2008 has had significant negative consequences for this sector. The first signs of improvement however, are more and more starting to emerge in some parts of North America. The Boston Consulting Group released a study in August 2011 related to the potential for growth in the manufacturing sector on the North American Continent in coming years. The report draws the conclusion that manufacturing will be staging a major return to North America within a couple of years. An excerpt from the report is reproduced below:

“..... a combination of economic forces is fast eroding China’s cost advantage as an export platform for the North American market. Meanwhile, the U.S. with an increasingly flexible workforce and a resilient corporate sector is becoming more attractive as a place to manufacture many goods consumed on this continent. An analysis by The Boston Consulting Group concludes that, by sometime around 2015- for many goods destined for North American consumers – manufacturing in some parts of the U.S. will be just as economical as manufacturing in China.”

Whenever a company makes a decision about locating a plant, net long-term cash flow from the location will be the key consideration. The level of municipal property taxation will always be a significant element in the analysis of the long-term cash flow for all the sites under consideration. It is in the City’s interest to ensure that its industrial tax rates are competitive.

The following comments appeared in the Financial Post in February 2012 article by Jack Mintz of the University of Calgary:

“The story of the past decade is that corporate investment in machinery and structures have risen significantly with tax reforms and many businesses today are starting to ramp up capital spending in anticipation of a better global economy.

Most credible economic studies have shown that corporate tax reductions increase investment through a lower cost of capital. Yes many factors influence corporate investment, such as the state of the economy, but proper statistical testing separates the various confounding factors that influence investment. A 10% increase in the gross-of-tax cost of capital causes investment to decline by 7%.”

As was indicated in the Future Tax Policy report, changing tax ratios is not considered a tax levy increase under Provincial law and would not have to be identified and described as such on any tax bill.

2009 Reassessment, 2012 Phase-In and Tax Ratios

All properties in Ontario were reassessed for 2009 taxation based on market values determined as of January 1, 2008. The last Province wide reassessment was for the 2006 taxation year. That last reassessment was based on market values as of January 1, 2005. The assessed values for 2009 taxation therefore started to reflect the change in market values that had occurred between January 1, 2005 and January 1, 2008.

Reassessments have no effect on the amount of the City’s tax levy or the level of taxation. They do however affect the way the tax levy is allocated between property classes and between individual properties within the various property classes. Schedule E attached shows the effect of the phase-in of the 2009 reassessment in 2012 on the various major classes assuming no change is made in the tax ratios used in 2011 and no tax levy increase in 2012.

The reassessment for 2009 was the first reassessment where the Province mandated that all property value increases on the assessment roll must be phased-in over four years. The result of the phase-in is that the tax change impact that would have otherwise occurred as a result of the 2009 reassessment has been slowed down and been spread out over the four years from 2009 to 2012.

Schedule E indicates that the impact of the reassessment in 2012 without any tax ratio changes from 2011 is to decrease taxes in the residential class by approximately 1/10th of 1% in 2012.

The new four year phase-in of value increases on the assessment roll has significance for the setting of tax ratios. It appears that there is no longer any need to consider using ratio setting as a tax mitigation tool at the time of a reassessment. The mitigation provided by the four year value phase-in provided on the roll is substantial.

Commercial and Industrial Tax Ratios

In theory, the City has some flexibility to increase tax ratios in the commercial and industrial classes to adjust for tax shifts away from those classes at the time of a reassessment. This theoretical flexibility however has no practical application for the City of London in 2012. The reason for this is that tax ratios for the commercial and industrial classes in London are currently at the Provincial thresholds/averages. If the City attempted to raise the tax ratios for those classes, the City would be

subject to a levy restriction which would significantly restrict the City's ability to impose tax increases in the commercial and industrial classes. The net effect of the levy restriction would actually be to shift taxes towards the residential class rather than away.

In addition to the levy restriction problem with respect to increasing tax ratios in the commercial and industrial classes, we also strongly recommend against increasing tax ratios in the commercial and industrial classes for reasons of economic competitiveness. As mentioned above, Schedule A provides comparative data for tax ratios included in the BMA Municipal Study. As noted, London is in the middle range and it is in the City's best interest not to move into the higher ranges. Over time the general trend of municipalities in Ontario has been to try to lower commercial and industrial tax ratios particularly where they exceed the established Provincial thresholds. As mentioned above, historically the City has adopted and maintained the policy that it would not move any tax ratio above the established Provincial thresholds/averages at the time of a reassessment.

The overall effect of the 2009 reassessment on the commercial property class over the four year phase-in period 2009 to 2012 is negligible. Over the four years, the total reassessment related tax change for the class as a whole will amount to less than 1/10 of 1%. Total taxes in the industrial class as a whole will decline by about 4.6% from what they otherwise would be as a result of the phase-in of the 2009 reassessment over the four years 2009 to 2012.

We are not recommending any change in the commercial or industrial tax ratios in 2012. Administration will closely monitor tax ratios in the commercial and industrial classes in Ontario to ensure that London's tax ratios in these classes are competitive with other major centres in Ontario. As explained in the next section, commercial and industrial property owners in London should be experiencing decreases in the education property taxes through to the year 2014. In 2011 education taxes comprised 41.9% of the typical commercial property tax bill and 37.7% of the typical industrial property tax bill.

Ongoing Reductions in Business Education Taxes Until 2014

In April 2005, London City Council passed a resolution requesting that the Minister of Finance for the Province of Ontario "review the entire process for setting education property tax rates for business properties and that education tax rates for properties in the City of London be lowered to a level consistent with other municipalities in the Province". The resolution, along with a letter from the Mayor went to the then Minister of Finance, Greg Sorbara in April 2005. After a letter from the Minister in June 2005, the Mayor followed up with a second letter in February 2006 to a new Minister of Finance – Dwight Duncan. In 2007, Dwight Duncan announced that major tax reform would occur in the area of education property taxes along the lines requested by the City beginning in 2008 and would be phased-in over the seven year period ending in 2014. As a result of this major reform, the Province has indicated that by the year 2014 when the phase-in is complete, education property taxes in the City of London will be reduced by \$33.6 million each and every year into the future from what they otherwise would have been.

Multi-Residential Tax Ratio

As can be seen from Schedule E, the phase-in of the 2009 reassessment in 2012 is causing some shift in taxation towards the multi-residential class. The past policy of the City since major tax reform occurred in 1998, has been to set the tax ratio for the multi-residential property class so that the tax levy increase for the residential and multi-residential classes are approximately equalized. We recommend the continuation of this policy in 2012. The effect of the continuation of this policy is to adjust taxation in the residential class by about 1/10th of 1% and to decrease taxation in the multi-residential class by about 1% from what it would be without any tax ratio change.

It should be noted that Schedule A indicates that the tax ratio for the multi-residential class in London is below the average and the median for the group included in the BMA Study and well below the established Provincial threshold/average for the multi-residential class.

Farm Property Class Tax Ratio

The tax ratio for the farm property is set in accordance with Section 308.1 of the Municipal Act, 2001. Under the provisions of that Section, the ratio is automatically reset to .25 every year unless the Municipality sets it at a lower level by by-law each year. The farm property class is a very small class in the City of London, and changes in the tax ratio for the farm class have no significant impact on any other property classes. In the past the City has always followed a policy of setting the farm

property class tax ratio at a level that would result in the farm class receiving the average tax increase for the City subject to the .25 maximum in the legislation. We recommend continuation of this policy for 2012. This policy will result in a .25 tax ratio in the farm class in 2012.

Pipeline Tax Ratio

Unlike the commercial, industrial, and multi-residential classes, the Province has not set any threshold tax ratio level or levy restriction with respect to the pipeline class. In accordance with Section 9(3) of Ontario Regulation 385/98, however, it is not possible for the City to increase the tax ratio for the Pipeline Class without simultaneously changing the tax ratio in the commercial class and increasing taxes in the residential property class by an amount that would be greater than any increase in the pipeline property class. It is therefore recommended that the tax ratio for the pipeline class not be changed for the year 2012.

Summary of Tax Ratio Recommendations

In summary, for 2012 we are recommending decreasing the tax ratio in the multi-residential class so as to equalize the tax levy increase with that of the residential class in accordance with past tax policy recommendations. This will not have a significant impact on the residential property class because of the relative sizes of the two property classes. All other tax ratios for the various property classes are recommended to be the same in 2012 as they were in 2011. The recommended tax ratios for 2012 and the tax levy approved by Council for 2012 are reflected on Schedule G attached to this report.

Recommendation 3 – Utilizing Options Available to Bring an End to Capping Tax Increases and Clawing Back Tax Decreases in the Commercial, Industrial, and Multi-Residential Property Classes

Since major Province wide tax reform began in 1998, the Province has mandated a complex system of capping tax increases and clawing back tax decreases in the commercial, industrial, and multi-residential property classes. We have long believed the entire system was unfair to taxpayers, damaging to economic development, and administratively onerous. Based on consultation with municipal representatives including the City of London during 2008, the Province provided increased flexibility under the business tax capping program for 2009 and future years. It appears the Province has decided to provide this very significant increase in flexibility to municipalities because of the new tax mitigation provided by the four year phase-in of assessment values beginning with the reassessment for 2009 taxation.

For the first time in 2009, municipalities had options to permanently remove properties from the capping and claw-back system once they have reached their CVA level taxes. Municipalities can have these options apply to all capped property classes or limit the options to individual capped classes. For 2012 this means that any property which had paid CVA taxes or higher (i.e. clawed back) in 2011 can be excluded from having a tax increase capped in 2012. At the same time, a property that had a tax increase capped in 2011 can not have a tax decrease clawed back in 2012 if the options are chosen. Preliminary calculations indicate continuing to fully utilize the options available will significantly reduce the capping of tax increases and clawing back of tax decreases.

We strongly recommend that Council take advantage of this opportunity to substantially bring the capping of tax increases and the clawing back of tax decreases to an end as soon as possible. In 2011 the City utilized all options available to exclude properties from future capping and no problems were encountered. The continued implementation of the new system in 2012 will require Council to pass a by-law in accordance with the Municipal Act, 2001.

Recommendation 4 - By-law to Clawback a Portion of Tax Decreases in Capped Property Classes

Under Section 329 of the Municipal Act, Council is required to cap all year-over-year tax increases after 2001 in certain property classes (i.e. commercial, industrial, and multi-residential). In the year 2008 many properties still had tax increases resulting from the reassessment for 1998 taxation which had not been completely phased-in. In many cases, the reassessments for 2001, 2003, 2004 and 2006 created additional tax increases and decreases subject to new capping and clawing back rules as set out in the Municipal Act.

Council does theoretically have the option of financing the capping of tax increases on the capped property classes by increasing the general tax levy. We do not recommend this course of action however because of the significant impact on the general tax rate. In 2011, approximately \$.7 million of reassessment related tax increases were capped and \$.7 million of reassessment related tax decreases were clawed back. To finance the capping of tax increases entirely from the general tax levy would have required an additional .15% increase in general tax rates for 2011 in the City.

Since 1998, tax decreases that otherwise would have been implemented have been clawed back at the rates indicated on Schedule C to finance the capping of properties with tax increases within each capped property class.

Final claw back percentages that will be applicable for year 2012 are not yet available. As has been the practice in the past, City staff will work closely with the Province to calculate caps and claw backs applicable for 2012 prior to the issuance of final bills for the capped classes. The dollar amounts of cap adjustments by year from 1998 to 2011 are attached as Schedule D.

It is recommended that Council pass the necessary by-law to authorize the clawing back of tax decreases in the capped property classes sufficient to finance the capping of tax increases (i.e. the maximum claw back rate permitted by Section 330 of the Municipal Act).

Recommendation 5 - By-law to Set a Formula for Calculating Caps in the Commercial, Industrial and Multi-Residential Property Classes

For 2008, 2009, 2010 and 2011, Council adopted several options permitted by Section 329.1 to reduce the amount of capping of tax increases and clawing back of decreases in the commercial, industrial and multi-residential property classes. The selected options were as follows:

- capping at 10% of previous years taxes instead of the 5% minimum;
- utilizing the option of 5% of previous years CVA taxes where applicable;
- reducing cap adjustments equal to or less than \$250 to nil;
- new construction was taxed without any cap adjustment.

The use of all these options significantly reduced the amount of clawing back of decreases as can be seen on Schedules C and D of this report. No significant problems or issues were encountered by the City Tax Office in the 2008, 2009, 2010 or 2011 billings as a result of utilizing the above options. The by-law to use the options only referred to the particular tax year. The use of these options as recommended will expedite the eventual end of the capping and clawing back system as more and more properties reach their CVA level taxes.

It is therefore recommended that a by-law be enacted under Section 329.1 of the Municipal Act, 2001 for 2012 and subsequent years where applicable, to adopt the same capping formula as was applicable to the 2011 taxation.

Recommendation 6 - Phase-In Program for Residential Property Class

All residential properties in the City of London were reassessed for 2009 taxation based on January 1, 2008 market values. The January 1, 2008 market values are being phased-in over a 4 year period from 2009 to 2012 as required by Provincial legislation. For 2006, 2007 and 2008 taxation properties were valued based on January 1, 2005 market values. Assessment related tax changes for 2011 occurring in the residential class have been analyzed and compared to the 2009, 2006, 2004, 2003, 2001 and 1998 reassessments. The results of this analysis are shown on Schedule I attached.

Assessment related tax changes exclude tax increases that result from levy increases. The levy increase is imposed in addition to assessment related tax changes (increases and decreases).

As can be seen from Schedule I, the assessment related decreases and increases for 2012, 2011, 2010 and 2009 are significantly less than the increases and decreases which have occurred in the last five reassessments in the City prior to 2009. The reason for this is that for the first time in 2009, the Province included a phase-in of all reassessment changes on the 2009 assessment roll. This phase-in has continued over the period 2011 to 2012. For 2012, residential properties are being valued on the roll at their January 1, 2008 value.

For 1998 and subsequent reassessments up to and including 2006, Council decided that a phase-in of assessment related tax changes was not necessary. Based on the above data and the fact that the Province has already instituted a four year phase-in of assessment values on the roll, it appears clear that no further tax mitigation in the residential class is necessary.

In summary, based on our analysis of the reassessment data and the existence of a four year phase-in of values on the assessment roll, we believe any additional phase-in of the residential class under Section 318 of the Municipal Act, 2001 is not warranted.

Comments on Unusual Tax Increases after a Reassessment

Whenever a general reassessment occurs as was the case in 2009, there will always be a small number of large tax increases. Inevitably, when over 100,000 properties are valued, some errors and inaccuracies will occur. If a property is overvalued when a reassessment occurs, the remedy is to contact the Municipal Property Assessment Corporation and have the valuation corrected or appeal the assessment in accordance with the provisions of the Assessment Act.

When a property is undervalued or incorrectly classified to the taxpayers benefit, the taxpayer has no financial incentive to have the error or inaccuracy corrected. The error or inaccuracy will typically be corrected at the next reassessment and surface as an unusually large increase. Focusing on the amount or percentage of the increase obscures the real cause of the tax change (i.e. an inaccuracy in the valuation or classification of the property in the past). Phasing-in or capping taxes in these situations only perpetuates errors and inaccuracies in the assessment system and represents a major departure from the fundamental principle of fairness (i.e. that every property owner within a class pays the same tax rate on the market value of his or her property).

SUMMARY

If all of the recommendations in this report are approved by Council, the increase or (decrease) in municipal taxes levied for 2012 including transit area rates in the various property classes would be as follows:

Property Class	2012 Municipal Tax Increase (Decrease) Including Transit
Commercial	0.2%
Industrial	-1.0%
Multi-Residential	0.0%
Residential	0.0%
Farmland	-1.9%
Pipe Lines	-1.3%

The above numbers do not include the effect of education taxes.

Based on education tax rates which have been estimated by the Province, general municipal, transit, and education taxes in both 2011 and 2012 would have average total tax changes as follows:

Property Class	2012 Average Total Tax Increase (Decrease) Including Transit and Education
Commercial	-4.2%
Industrial	-6.6%
Multi-Residential	0.0%
Residential	-0.2%
Farmland	-3.2%
Pipe Lines	-5.0%

The above percentages represent **average** tax changes only. Individual taxpayers would also be affected by the phase-in of the general reassessment and changes to transit taxation as approved by Council in 2009. Tax changes relating to municipal levy increase, reassessment, and education rates are separately identified on the final tax bill in accordance with Provincial regulation.

Properties in the capped property classes would also still be subject to limitations on year-over-year tax increases and decreases in accordance with Provincial legislation. These limitations, however, would also be subject to options adopted to prevent properties from re-entering the Province's capping and clawing back system in the future as recommended in this report.

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