

INTRODUCTION

- [1] On September 28, 2023 the Landlord mailed the Tenants 19 *Notices of Annual Allowable Rent Increases* (the “Form 8 Notices”) which stated that the undiscounted rents for the Units were increased by the annual guideline 3.0% effective January 1, 2024.
- [2] On April 18, 2024, the Landlord filed 19 *Landlord Applications to Request Additional Rent Increases* (the “Applications”) with the Residential Tenancy Office (the “Rental Office”) to request additional rent increases above the annual allowable guideline established by the Director of Residential Tenancy. The Applications seek total rent increases of 6.0%. The Applications contain the current undiscounted rents, the proposed undiscounted rents and a rent increase effective date of May 1, 2024.
- [3] On May 17, 2024 the Rental Office mailed and emailed the parties notice of a teleconference hearing scheduled for 1:00 p.m. on June 18, 2024.
- [4] On June 14, 2024 the Rental Office provided the parties with a 73-page evidence package (“EP”), which included a *Landlord Statement of Income and Expenses* dated June 6, 2024 (the “Statement”).
- [5] On June 18, 2024 at 1:00 p.m. a teleconference hearing was held before the Residential Tenancy Officer (the “Officer”). Three representatives of the Landlord and seven of the Tenants participated in the hearing. After the hearing the Landlord was permitted to submit additional documents, including evidence regarding the Landlord’s expectation to have a reasonable return on its capital investment.

ISSUES

- 1. Does the *Rental of Residential Property Act* or the *Residential Tenancy Act* authorize rent discounts pursuant to written agreements?
- 2. Does the evidence presented support 6.0% rent increases for the Units?

SUMMARY OF EVIDENCE**Landlord’s Evidence and Submissions**

- [6] The Landlord’s evidence is summarized as follows.
- [7] The 19 Units are located in three one-unit buildings, four two-unit buildings and two four-unit buildings. The construction of the Units started in the Spring of 2021 and finished in the Spring of 2022.
- [8] The Landlord submitted into evidence documents supporting the proposed rent increases, including letters to the Tenants (the “Letters”) that accompanied the Applications.
- [9] The Landlord provided the following explanation for the rent discounts identified in the Letters. When construction is completed there is a high volume of rental units that enter the market at the same time. In order to keep in good financial standing, it is in the Landlord’s best interest to have tenancy agreements in place as quickly as possible following completion because it helps getting final mortgage draws and financing in place. The Landlord is trying to manage risk and a variety of pressures. The Landlord submits that if it waited longer, then it would be able to rent the Units for higher amounts. The Landlord does not take away the discount while the same tenant occupies the unit.

- [10] The Landlord's rental income ledger (EP10) also included the following comment regarding rent discounts:

"During the original rent up of the new construction, there is a large volume of units available. Rents are often discounted to minimize vacancy during initial rent up. These discounts are communicated to tenants in their leases, and the discounts are honored for the duration of the tenant occupancy. We are requesting approval for the rent increase on base rent before the discount. We will apply the IRAC increase amount to the current rent the tenant is paying and keep their discount in place during their tenancy."

- [11] The Letters provide details regarding increasing costs, stating in part as follows:

"Between 2022 and 2024 examples of property related cost increases include: property taxes (27%), repair and maintenance costs (30%), insurance premiums (50%) etc.

CPI in PEI over this period has been: 2022 at 9% and 2023 at 3.6% for a total of 12.6% or an average of: 6.3% per year.

During this same period allowable annual rent increases from Government were: 1% in 2022 and 0% in 2023 for a total of 1% or an average of 0.5%. This has done little to make up for increases in costs.

If the 6% increase is granted, the average increase over the 3 years of 2022-2024 will be 2.3% and far below the increases in costs that have taken place."

- [12] The Statement provides details of the changes in the expenses for the Units.
- [13] The Landlord submits that the rent increase caps in the new legislation create challenges when there are significant and immediate cost increases, such as increases in mortgage interest rates.
- [14] The maturity dates of the current mortgage renewal terms for the Units occur in 2027 for seven of the buildings and 2032 for two of the buildings.
- [15] The Landlord's capital investment amount in the Statement is the purchase price plus capital expenditures. With regard to a mortgage deduction for calculating capital investment, the Landlord questioned why a different formula is being considered when the Statement contains a calculation with no mortgage deduction. The Landlord submits that a mortgage deduction would not align with the guidance given when preparing materials and it is not logical or fair.
- [16] The Landlord submits that deducting the mortgage from the purchase price plus capital expenditures would be a significant deterrent for property owners taking on the high risks of purchasing and owning rental properties.
- [17] The Landlord submits that the formula for calculating return on investment seems to be a moving target. The Landlord would be very grateful if there was one clear formula put forward for the Landlord to plan around.
- [18] The Landlord provided return on investment calculations based on different mortgage scenarios.
- [19] The Landlord submits that the minimal attendance for the hearing relative to the number of Units indicates that many of the Tenants understand that the rent increases are fair. The Landlord submits that IRAC's 2023 rent increase was supposed to be 5.8% until it was reduced to 0.0% by Government. The Landlord provided evidence regarding increases in CPP and OAS.

- [20] The Landlord submits that there needs to be a logical approach to rent increases. The Landlord submits that otherwise the net result will be rental units moving to condos as is happening in the market today. The Landlord submits that this is not what the Landlord wants and is not a threat to any of the Tenants. The Landlord submits that there needs to be understanding by IRAC and Government of making these projects function long term with some level of clarity.

Tenants' Evidence and Submissions

- [21] The Tenants' evidence is summarized as follows.
- [22] At the hearing some of the Tenants provided evidence regarding maintenance and service matters. Some of the Tenants stated that they were happy with the quality of the Units. Some of the Tenants face financial challenges because of their fixed incomes.
- [23] Part of the documentary evidence submitted by some of the Tenants opposes above guideline rent increases.

ANALYSIS

ISSUE 1 – Does the *Rental of Residential Property Act* (the “RRPA”) or the *Residential Tenancy Act* (the “Act”) authorize rent discounts pursuant to written agreements?

- [24] For the reasons below, the Officer finds that the *RRPA* and the *Act* do not authorize rent discounts by written agreements.
- [25] The *RRPA* governed residential rent increases from January 18, 1989 to April 7, 2023. During the time the *RRPA* was in force, the Island Regulatory and Appeals Commission (the “Commission”) issued decisions regarding rent discounts.
- [26] On October 17, 1995 the Commission issued Order LR95-12¹, which determined an unlawful rent increase matter. In this decision the Commission found that the *RRPA* did not permit rent discounts, stating as follows:

“Even more significant, however, is that rent control legislation does not permit a Lessor to vary the rent depending upon how many people reside in an apartment or what kinds of services are provided. A lessor is also not able to give a discount to one tenant but not to another. Rent is fixed by law. Each rent relates to a specific apartment, not a specific “situation”. Changes in tenants are irrelevant.

This is not to say that the Act is inflexible. Any lessor who has extraordinary expenses may apply to the Director for an increase to cover those expenses (s.23). Any lessor who wishes to discontinue a service previously included within the rent may apply to the Director for permission (s.6).”

[Emphasis added]

- [27] The Commission issued at least two further *RRPA* decisions which imply that rent discounts were not authorized by this earlier rental legislation. In these cases, a landlord had originally charged a higher rent for a unit, later lowered the rent, and then purported to increase the lower rent above the annual allowable percentage without a Rental Office order. The Commission found that, after charging a lower rent, the landlord was required to obtain an order to increase the rent even though historically the landlord had in fact collected a higher rent.

¹ Order LR95-12 is available at: <https://irac.pe.ca/wp-content/uploads/LR95-12.html>

[28] In the first decision, Order LR09-11², the Commission stated in part:

"While the evidence before the Commission is clear that the rent for the premises had been \$980.00 per month in 2006, the Commission finds that [the landlord] made the decision to advertise the premises at the rate of \$780.00 per month in order to attract a new tenant. [The tenant] agreed to rent the premises at that monthly rate. At that point, the established rental rate for the premises was set at \$780.00. For the purposes of the present appeal, the Commission accepts the evidence of [the landlord] that the reduction in rent was necessary because previous tenants left the premises in poor condition..."

While [the tenant] did sign the August 18, 2007 rental agreement, the increase in rent was contrary to the Act as [the landlord] did not follow the required process to seek a rental increase. Accordingly, the Commission agrees with the findings contained in the Director's Order LD09-112 and the appeal is hereby denied."

[29] In the second decision, Order LR22-18³, the Commission stated in part:

"The Commission accepts that the rent for the Premises was initially \$1,400 per month, but that rate was then reduced. While the Appellants may have requested rent higher than \$1,200 per month from the tenants immediately prior to the Respondents, the Appellants deposited the post-dated cheques as they came due and thus are deemed to have accepted rent at \$1,200 per month. Unfortunately for the Appellants, such acceptance established the rent for the Premises at \$1,200 per month and no application was made to the Director to lawfully increase the rent prior to the Respondents leasing the Premises."

[30] These two *RRPA* decisions establish that the authorized rent is based upon the amount actually charged and collected. This is also consistent with the definition of rent in subsection 1(n) of the *RRPA*, which states:

"rent" means the amount of the consideration, whether or not in money, paid, given or agreed to be paid or given by a lessee to a lessor for occupancy of residential premises and for any service, privilege or thing that the lessor may provide for the lessee, whether or not a separate charge is made therefor.

[31] With regard to the Act, which has been in force since April 8, 2023, rent is defined in subsection 1(n) as follows:

(n) "rent" means money paid or agreed to be paid, or value or a right given or agreed to be given, by or on behalf of a tenant to a landlord in return for the right to possess a rental unit, for the use of common areas and for services or facilities, but does not include
(i) a security deposit, or
(ii) a fee prescribed under clause 107(1)(j).

[32] From these definitions, it appears to the Officer that the authorized rent is based upon the amount of rent actually charged and collected.

[33] In this case, most of the Landlord's rent discounts are approximately \$100.00 to \$150.00 in excess of the rents actually charged.

[34] However, the logical extension of rent discounts in written agreements would render meaningless Part IV (sections 20 to 23) of the *RRPA* and Part 3 (sections 47 to 50) of the Act.

² Order LR09-11 is available at: <https://irac.pe.ca/wp-content/uploads/LR09-11.html>

³ Order LR22-18 is available at: <https://irac.pe.ca/wp-content/uploads/Order-LR22-18.pdf>

- [35] For example, a landlord could purport to have an authorized rent in a written agreement of \$2,000.00 with a discount of \$1,000.00, with the rent actually paid being \$1,000.00. At a later date the discount expires and the rent actually paid increases from \$1,000.00 to \$2,000.00, being a 100% rent increase from the rent that was previously paid, well above the 6% maximum.
- [36] The legislated rent increase restrictions are intended to provide a comprehensive framework for increases that cannot be avoided. It appears to the Officer that a purported rent discount in a written agreement cannot validly authorize a later above guideline increase of the rent actually paid.
- [37] With regard to the Units, there does not appear to be previous Rental Office or Commission orders authorizing phased in rents.
- [38] The Officer will determine the Applications based upon the rents actually charged as shown in the rental income ledger provided by the Landlord (EP10 to 13).
- [39] Based upon the evidence presented, it appears that the rent for 3 KSW increased on July 1, 2022 above the annual allowable percentage due to the removal of a rent discount. The Officer notes that this was the only Unit with a Letter to the tenant containing no rent discount. The rent increase occurred after a tenant moved out and a new tenant moved into the Unit. The Officer calculates the increased rent for this Unit based upon the actual monthly rent paid as of June 1, 2022, in the amount of \$1,975.00.

ISSUE 2 – Does the evidence presented support 6.0% rent increases for the Units?

Adjustments to the Statement

- [40] The Officer's adjustments to the Statement are provided below and are reflected in Appendix "A".
- [41] The annual income, arrears, net income and management fees are calculated based upon the actual rents charged, as shown in the Landlord's rental income ledger. The calculation of the annual income is provided in Appendix "B".
- [42] Pursuant to clause 107(1)(d), the Lieutenant Governor in Council may make regulations defining a word or expression that is used but not defined in the *Act*. The following terms regarding rent increases have been defined in the *Residential Tenancy Regulations* (the "*Regulations*"): maintenance, management fee, rental income, capital expenditures and operating costs.
- [43] The term "capital investment" is undefined.
- [44] The Landlord opposes a mortgage deduction for calculating the capital investment value for the Units. However, it appears to the Officer that a mortgage deduction is necessary in order to normalize the treatment of landlords with varying amounts of loaned funds for residential properties.
- [45] For example, consider a landlord that purchases a residential property using partly its own funds and loaned funds. If there is no mortgage deduction when calculating the value of the landlord's capital investment, then the landlord's return on investment could be calculated based upon the entire original purchase price and capital expenditures. This landlord could also include the mortgage interest as a deduction in the landlord's expenses.
- [46] Had the landlord used only its own funds to purchase the property, without any loan, then the landlord would have the same capital investment value, but no mortgage interest deduction.
- [47] Making no mortgage deduction in the calculation of capital investment appears to the Officer to be an incorrect approach.

- [48] When the landlord did not borrow any funds it put more of its own funds at risk. However, it would have less support for an above guideline rent increase compared to if it had borrowed funds. By including the mortgage deduction in the value of the landlord's capital investment, the treatment of landlords with varying amounts of loaned funds is normalized.
- [49] The Officer also notes that in Order LR23-80⁴ the Commission referred to "equity" when calculating return on investment.
- [50] The Officer will calculate the Landlord's capital investment with a mortgage deduction.
- [51] The Landlord's capital investment is \$1,166,110.00 based upon the purchase price plus capital expenditures amount in the Statement minus the outstanding mortgage (\$5,371,110.00 minus \$4,205,000.00).
- [52] The Landlord provided an alternate value of \$6,840,000.00 based upon the current estimated replacement cost of the Units. This appears to the Officer to be similar to using an appraised value and therefore would need to be averaged with the tax assessed value of \$3,356,900.00 (see paragraph [61], below). The averaged value would be \$5,098,450.00. After deducting the mortgage (\$4,205,000.00), the Landlord's capital investment would be \$893,450.00.
- [53] The Landlord's return on investments are shown in Appendix "A" using both calculated values of capital investment.

Factors

- [54] In order to determine the proposed rent increases, the Officer must consider the following factors in subsection 50(3) of the *Act*:
1. The rent history for the affected Units in the three years preceding the date of the Applications.
 2. A change in operating expenses and capital expenditures in the three years preceding the date of the Applications that the Director considers relevant and reasonable.
 3. The expectation of the Landlord to have a reasonable return on the Landlord's capital investment.
 4. The expectation of the Tenants that rent increases will remain within the annual guidelines.
- [55] Subsection 50(4) provides the Officer with discretion to consider any other relevant factor and any factor prescribed in the *Regulations*. The only other factor stated in the *Regulations* is that the purchase of a residential property should not require an increase of rent within the first year in order to achieve a reasonable return on the landlord's capital investment. This factor is not relevant in this case because the Landlord has owned the Units since they were constructed in 2022.

Review and Weighing the Factors

- [56] The Landlord's rental income ledger shows that the rents for the Units have not increased since they were built, except for the purported rent increase of 3 KSW due to the removal of a rent discount. Some of the Landlord's operating costs and capital expenditures have increased since 2022. These factors provide some support for rent increases above the 3.0% guideline.

⁴ See paragraph 43 of Order LR23-80, available at: <https://irac.pe.ca/wp-content/uploads/Order-LR23-80.pdf>

- [57] In this case, there was some tenant participation opposing the rent increases in the documentary evidence. In general, it would be reasonable for a tenant not to expect an above guideline rent increase due to the relatively recent construction of the Units. The Landlord noted that the Commission's 2023 allowable percentage, which was 5.2% for unheated units, was reduced to 0.0% by legislation. Based upon these considerations this factor appears to be neutral regarding the proposed above guideline rent increases.
- [58] It appears to the Officer that the Landlord's return on investment heavily weighs against above guideline rent increases.
- [59] The Landlord's calculated return on capital investment with the current rents would be 10.1% based upon the original purchase price, capital expenditures and mortgage balance. This return would increase to 12.3% with rent increases of 6.0%.
- [60] The Landlord's return on capital investment with the current rents would be 13.1% based upon the current, averaged replacement cost and tax assessed value and mortgage balance. This return would increase to 16.0% with rent increases of 6.0%.
- [61] In a recent decision, Order LR24-27⁵, the Commission stated as follows regarding reasonable return on investment:
- "In previous Orders, the Commission has considered reasonable return on investment rates and has found them to be, in recent years, in the range of 4% to 7%. The Commission has used 7% as an appropriate ROI where the Landlord is relying on a recent actual purchase price or on the tax assessed value. A lower rate of 4% has been used when the Landlord is using a blend of the tax assessed value and an appraisal done for the Landlord's benefit..."*
- [62] The Landlord would currently be making a return on investment 3.1% higher than the typical 7.0% based upon the first calculation using the original purchase price plus capital expenditures.
- [63] The Landlord would be making a return on investment 12.0% higher than the typical 4.0% based upon the second calculation using blended replacement cost and tax assessed values.
- [64] The Officer also notes that the Landlord's operating costs and capital expenditures have been factored into these two return on investment calculations.
- [65] As the Landlord's return on capital investment is significantly higher than the returns typically permitted for above guideline rent increases, the Officer finds that this factor outweighs the other factors. As a result, only 3.0% guideline rent increases are authorized by this decision.

Effective Date

- [66] On September 28, 2023 the Landlord sent the Form 8 Notices to the Tenants for the 3.0% guideline increases effective on January 1, 2024.
- [67] On April 18, 2024 the Applications were filed seeking 6.0% rent increases effective May 1, 2024.
- [68] The Officer notes that it was unnecessary for the Landlord to serve the Form 8 Notices before filing the Applications pursuant to subsection 48(3) of the Act. The Officer also notes that a landlord cannot complete an allowable rent increase and a later, separate above guideline increase within 12-months from the first increase (subsection 48(1)).

⁵ See paragraph 46 of Order LR24-27, available at: <https://irac.pe.ca/wp-content/uploads/Order-LR24-27.pdf>

- [69] It appears to the Officer that the earlier effective date in the Form 8 Notices is not applicable because the Landlord elected to proceed with the Applications seeking the higher 6.0% rent increases.
- [70] The Letters from the Landlord that accompanied the Applications sent to the Tenants state in part:
- “The attached form 9 has an effective date included. Our understanding is there will be no retroactive rent charged and rent will not increase until the date of the IRAC ruling. You will receive further communication before any increase to the monthly rent.”*
- [71] It also appears to the Officer that the rent increase effective date must be a minimum of three clear months from the date the Applications were filed. Otherwise, a landlord could be able to implement an above guideline rent increase faster than a guideline rent increase (which requires three full months’ notice).
- [72] The Officer finds that the appropriate effective date for the rent increases is September 1, 2024.

CONCLUSION

- [73] The Landlord’s Applications for above guideline rent increases are denied. The rents for the Units are increased by the 3.0% guideline as provided below.
- [74] **This decision contains sensitive information and the parties are required to preserve its confidentiality pursuant to subsection 75(3) of the Act.**

IT IS THEREFORE ORDERED THAT

1. Effective September 1, 2024 the maximum allowable rents for the Units are as follows:

<u>Unit</u>	<u>3% Increase</u>
10 BML	\$2,518.00
15 BML	\$2,034.00
17 BML	\$2,034.00
3 KSW	\$2,034.00
5 KSW	\$1,906.00
6 KSW	\$2,261.00
7 KSW	\$1,906.00
9 KSW	\$1,983.00
15 KSW	\$1,983.00
17 KSW	\$1,906.00
19 KSW	\$1,906.00
20 KSW	\$2,086.00
21 KSW	\$1,983.00
22 KSW	\$2,086.00
25 KSW	\$2,086.00
26 KSW	\$2,086.00
27 KSW	\$2,086.00
28 KSW	\$2,086.00
31 KSW	\$2,261.00

DATED at Charlottetown, Prince Edward Island, this 2nd day of August, 2024.

(sgd.) Andrew Cudmore

Andrew Cudmore
Residential Tenancy Officer

APPENDIX "A"**Revised Statement of Income & Expenses (Form 10)**

	Current	3% Increase	6% Increase
Rental Income			
Income (Line 1)	\$457,020.00	\$470,772.00	\$484,524.00
Arrears (Line 2)	(\$4,570.20)	(\$4,707.72)	(\$4,845.24)
Net Income (Line 3)	\$452,449.80	\$466,064.28	\$479,678.76
Expenses			
1st Mortgage (Line 4)	\$129,158.00	\$129,158.00	\$129,158.00
2nd Mortgage (Line 5)	\$0.00	\$0.00	\$0.00
Fuel (Line 6)	\$0.00	\$0.00	\$0.00
Water & Sewer (Line 7)	\$7,730.00	\$7,730.00	\$7,730.00
Electricity (Line 8)	\$12.00	\$12.00	\$12.00
Insurance (Line 9)	\$10,239.00	\$10,239.00	\$10,239.00
Property Tax (Provincial) (Line 10)	\$33,569.00	\$33,569.00	\$33,569.00
Property Tax (Municipal) + IWMC (Line 11)	\$28,888.06	\$28,888.06	\$28,888.06
Management Fee (Line 12)	\$22,622.49	\$23,303.21	\$23,983.94
Maintenance Fee (Line 13)	\$25,106.00	\$25,106.00	\$25,106.00
Capital Expenditures (Line 14)	\$68,646.00	\$68,646.00	\$68,646.00
Other (Line 15)	\$9,015.00	\$9,015.00	\$9,015.00
Total Expenses	<u>\$334,985.55</u>	<u>\$335,666.27</u>	<u>\$336,347.00</u>
Annual Net Profit	\$117,464.25	\$130,398.01	\$143,331.76
Original Purchase Price Plus Capital Expenditure Minus Current Mortgage			
Value of Investment	\$1,166,110.00	\$1,166,110.00	\$1,166,110.00
Net Profit	\$117,464.25	\$130,398.01	\$143,331.76
Return on Capital Investment	10.1%	11.2%	12.3%
Average of Current Replacement Cost and Assessed Value Minus Current Mortgage			
Value of Investment	\$893,450.00	\$893,450.00	\$893,450.00
Net Profit	\$117,464.25	\$130,398.01	\$143,331.76
Return on Capital Investment	13.1%	14.6%	16.0%

APPENDIX “B”

Unit	Rent		
	Current	3% Increase	6% Increase
10 BML	\$2,445.00	\$2,518.00	\$2,592.00
15 BML	\$1,975.00	\$2,034.00	\$2,094.00
17 BML	\$1,975.00	\$2,034.00	\$2,094.00
3 KSW	\$1,975.00	\$2,034.00	\$2,094.00
5 KSW	\$1,850.00	\$1,906.00	\$1,961.00
6 KSW	\$2,195.00	\$2,261.00	\$2,327.00
7 KSW	\$1,850.00	\$1,906.00	\$1,961.00
9 KSW	\$1,925.00	\$1,983.00	\$2,041.00
15 KSW	\$1,925.00	\$1,983.00	\$2,041.00
17 KSW	\$1,850.00	\$1,906.00	\$1,961.00
19 KSW	\$1,850.00	\$1,906.00	\$1,961.00
20 KSW	\$2,025.00	\$2,086.00	\$2,147.00
21 KSW	\$1,925.00	\$1,983.00	\$2,041.00
22 KSW	\$2,025.00	\$2,086.00	\$2,147.00
25 KSW	\$2,025.00	\$2,086.00	\$2,147.00
26 KSW	\$2,025.00	\$2,086.00	\$2,147.00
27 KSW	\$2,025.00	\$2,086.00	\$2,147.00
28 KSW	\$2,025.00	\$2,086.00	\$2,147.00
31 KSW	\$2,195.00	\$2,261.00	\$2,327.00
	\$38,085.00	\$39,231.00	\$40,377.00
Annual Rent	\$457,020.00	\$470,772.00	\$484,524.00

NOTICE**Right to Appeal**

This Order can be appealed to the Island Regulatory and Appeals Commission (the “Commission”) by serving a Notice of Appeal with the Commission and every party to this Order within **20 days of this Order**. If a document is sent electronically after 5:00 p.m., it is considered received the next day that is not a holiday. If a document is sent by mail, it is considered served on the third day after mailing.

Filing with the Court

If no appeal has been made within the noted timelines, this Order can be filed with the Supreme Court of Prince Edward Island and enforced as if it were an order of the Court.