

INTRODUCTION

- [1] On September 28, 2023 the Landlord mailed the Tenants 12 *Notices of Annual Allowable Rent Increases* (the "Form 8 Notices") which stated that the rents for the Units would be increased by the annual guideline 3.0% effective January 1, 2024.
- [2] On April 16, 2024, the Landlord filed 12 *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 rents, the proposed rents and an effective date of May 1, 2024.
- [3] On May 23, 2024 the Rental Office mailed and emailed the parties notice of a teleconference hearing scheduled for 1:00 p.m. on June 27, 2024.
- [4] On June 25, 2024 the Rental Office provided the parties with a 27-page evidence package ("EP"), which included a *Landlord Statement of Income and Expenses* dated June 13, 2024 (the "Statement").
- [5] On June 27, 2024 at 1:00 p.m. a teleconference hearing was held before the Residential Tenancy Officer (the "Officer"). Three representatives of the Landlord and one 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.

ISSUE

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 12 Units are located in three four-unit buildings that were built in 2016 and 2017.
- [8] The Landlord submitted into evidence documents supporting the proposed rent increases, including letters to the Tenants (the "Letters") that accompanied the Applications. The Letters provide the following details regarding the Landlord's increasing costs:

"Between 2021 and 2024 examples of property related cost increases include: interest rates (100% plus), property taxes (27%), repair and maintenance costs (30%), insurance premiums (50%) etc.

CPI in PEI over this period has been: 2021 at 4.6%, 2022 at 9% and 2023 at 3.6% for a total of 17.2% or an average of: 5.7% per year.

During this same period allowable annual rent increases from Government were: 1% in 2021, 1% in 2022 and 0% in 2023 for a total of 2% or an average of 0.67%. This has done little to make up for increases in costs.

If the 6% increase is granted, the average increase over the 4 years of 2021-2024 will be 2% and far below the increases in costs that have taken place."

- [9] 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. The termination date of the current mortgage renewal term, at a 2.94% interest rate, is November 7, 2024. The mortgage renewal rates offered to the Landlord range from 6.95% to 10.05%.
- [10] The Statement provides details of the changes in the expenses for the Units. The Landlord's total operating expenses in the Statement increased by approximately \$15,000.00 from 2021 to 2023 while the rental income increase by only \$7,000.00.
- [11] The Statement does not include a deduction for mortgage principal payments. The Landlord's actual management fees are 7.5% but are capped in the Statement at 5.0%.
- [12] The Landlord's capital investment in the Statement is \$2,112,450.00 based on the purchase price and capital expenditures. The tax assessed value of the Units is \$1,761,400.00 and the current replacement value is \$4,320,000.00. The mortgage balance was \$1,259,504.00 as of June 2021 and was reduced to \$1,079,701.00 as of April 30, 2024.
- [13] The Landlord submits that the capital being utilized is the current value of the Units minus the current mortgage. The Landlord submits that higher mortgages involve higher risk which should be considered in a formula for calculating return on investment. Landlords take on risks such as vacancies, interest rates, inflation, repair, maintenance and unruly tenants.
- [14] The Landlord provided evidence regarding increases in CPP and OAS.
- [15] The Landlord submits that the low participation by the Tenants at the hearing and the Landlord's communications with the Tenants indicate that there is understanding the 6.0% rent increases are necessary.
- [16] The Landlord does not believe that there were earlier Rental Office rent increase decisions regarding the Units.

Tenants' Evidence and Submissions

- [17] The Tenants' evidence is summarized as follows.
- [18] The Tenant that attended the hearing stated that it is reasonable the Landlord is seeking a 6.0% rent increase this year. Most of the people the Tenant has spoken to agree that a 6.0% rent increases are fairly reasonable in this climate. The Tenant is concerned about above guideline rent increases in the future.

ANALYSIS

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

Adjustments to the Statement

- [19] The Officer's adjustments to the Statement are provided below and are reflected in Appendix "A".
- [20] The Landlord's current annual income and the incomes at 3.0% and 6.0% increases are provided in Appendix "B".
- [21] It appears that there is a typographical error in the Ledger regarding the rent for 72 KR. The monthly rent in the Ledger is \$1,545.00 from January to October 2023 and the rent is \$1,627.00 for November and December 2023. The Form 8 Notice and Application for 72 KR are based upon a current rent of \$1,545.00.

- [22] The Landlord's mortgage is set to renew shortly at a new, significantly higher interest rate. The Officer has calculated the Landlord's interest at the low end of the interest rate range provided by the Landlord, being 6.95%. The interest is calculated on a principal balance of \$1,049,701.00 (\$30,000.00 reduction) to adjust for the Landlord's average principal payments.
- [23] 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.
- [24] The term "capital investment" is undefined.
- [25] 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.
- [26] 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.
- [27] 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.
- [28] 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.
- [29] The Officer also notes that in Order LR23-80¹ the Commission referred to "equity" when calculating return on investment.
- [30] The Officer will calculate the Landlord's capital investment with a mortgage deduction.
- [31] The Landlord's capital investment is \$1,032,749.00 based upon the purchase price plus capital expenditures amount in the Statement minus the outstanding mortgage (\$2,112,450.00 minus \$1,079,701.00).
- [32] The Landlord's capital investment in the Statement is \$2,112,450.00 based on the purchase price and capital expenditures. The tax assessed value of the Units is \$1,761,400.00 and the current replacement value is \$4,320,000.00. The mortgage balance was \$1,079,701.00 as of April 30, 2024.
- [33] The Landlord provided an alternate value of \$4,320,000.00 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 \$1,761,400.00 (see paragraph [41], below). The averaged value would be \$3,040,700.00. After deducting the mortgage (\$1,079,701.00), the Landlord's capital investment would be \$1,960,999.00.
- [34] The Landlord's return on investments are shown in Appendix "A" using both calculated values of capital investment.

¹ See paragraph 43 of Order LR23-80, available at: <https://irac.pe.ca/wp-content/uploads/Order-LR23-80.pdf>

Factors

- [35] 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.
- [36] 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 2016 and 2017.

Review and Weighing the Factors

- [37] The Landlord's rental income ledger shows that most of the last rent increases for the Units occurred over two years ago. The Landlord's operating costs and capital expenditures have increased by approximately \$13,000.00 from 2021 to 2023 while the rents have increased by approximately \$7,000.00. The Landlord's mortgage will be renewing shortly at approximately double the current interest rate. The Applications address 12 Units and none of the Tenants provided evidence disputing an above guideline rent increase. The Tenant that participated in the hearing provided evidence supporting the rent increases. These factors generally support rent increases above the 3.0% guideline for 2024.
- [38] In this case, the Landlord's return on investment also supports above guideline increases.
- [39] The Landlord's calculated return on capital investment with the current rents would be 5.0% based upon the original purchase price, capital expenditures and mortgage balance. This return would increase to 6.3% with rent increases of 6.0%.
- [40] The Landlord's return on capital investment with the current rents would be 2.6% based upon the current, averaged replacement cost and tax assessed value and mortgage balance. This return would increase to 3.3% with rent increases of 6.0%.
- [41] In a recent decision, Order LR24-27², the Commission stated as follows regarding a 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..."

² See paragraph 46 of Order LR24-27, available at: <https://irac.pe.ca/wp-content/uploads/Order-LR24-27.pdf>

[42] Therefore, the Landlord's expectation for a reasonable return on capital investment also supports the increases.

[43] For these reasons, the Officer finds that 6.0% rent increases are supported for the Units.

Effective Date

[44] 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.

[45] On April 16, 2024 the Applications were filed seeking 6.0% rent increases effective May 1, 2024.

[46] 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)).

[47] 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.

[48] 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).

[49] 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."

[50] The Officer finds that the appropriate effective date for the rent increases is September 1, 2024.

CONCLUSION

[51] The Landlord's Applications for above guideline rent increases are allowed. The rents for the Units are increased by 6.0% as provided below.

[52] **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>6% Increase</u>
50 KR	\$1,696.00
52 KR	\$1,708.00
54 KR	\$1,671.00
56 KR	\$1,696.00
60 KR	\$1,698.00
62 KR	\$1,638.00
64 KR	\$1,638.00
66 KR	\$1,696.00
70 KR	\$1,725.00
72 KR	\$1,638.00
74 KR	\$1,638.00
76 KR	\$1,696.00

DATED at Charlottetown, Prince Edward Island, this 28th 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)	\$227,952.00	\$234,768.00	\$241,656.00
Arrears (Line 2)	(\$2,279.52)	(\$2,347.68)	(\$2,416.56)
Net Income (Line 3)	\$225,672.48	\$232,420.32	\$239,239.44
Expenses			
1st Mortgage Interest (Line 4)	\$72,954.22	\$72,954.22	\$72,954.22
2nd Mortgage Interest (Line 5)	\$0.00	\$0.00	\$0.00
Fuel (Line 6)	\$0.00	\$0.00	\$0.00
Water & Sewer (Line 7)	\$5,145.00	\$5,145.00	\$5,145.00
Electricity (Line 8)	\$10,214.00	\$10,214.00	\$10,214.00
Insurance (Line 9)	\$8,049.00	\$8,049.00	\$8,049.00
Property Tax (Provincial) (Line 10)	\$16,013.91	\$16,013.91	\$16,013.91
Property Tax (Municipal) + IWMC (Line 11)	\$15,590.36	\$15,590.36	\$15,590.36
Management Fee (Line 12)	\$11,283.62	\$11,621.02	\$11,961.97
Maintenance Fee (Line 13)	\$17,139.00	\$17,139.00	\$17,139.00
Capital Expenditures (Line 14)	\$13,022.00	\$13,022.00	\$13,022.00
Other (Line 15)	\$4,576.00	\$4,576.00	\$4,576.00
Total Expenses	\$173,987.11	\$174,324.51	\$174,665.46
Annual Net Profit	\$51,685.37	\$58,095.81	\$64,573.98
Original Purchase Price Plus Capital Expenditures Minus Current Mortgage			
Value of Investment	\$1,032,749.00	\$1,032,749.00	\$1,032,749.00
Net Profit	\$51,685.37	\$58,095.81	\$64,573.98
Return on Capital Investment	5.0%	5.6%	6.3%
Average of Current Replacement Cost and Tax Assessed Value Minus Current Mortgage			
Value of Investment	\$1,960,999.00	\$1,960,999.00	\$1,960,999.00
Net Profit	\$51,685.37	\$58,095.81	\$64,573.98
Return on Capital Investment	2.6%	3.0%	3.3%

APPENDIX “B”

Rent

Unit	Current	3% Increase	6% Increase
50 KR	\$1,600.00	\$1,648.00	\$1,696.00
52 KR	\$1,611.00	\$1,659.00	\$1,708.00
54 KR	\$1,576.00	\$1,623.00	\$1,671.00
56 KR	\$1,600.00	\$1,648.00	\$1,696.00
60 KR	\$1,602.00	\$1,650.00	\$1,698.00
62 KR	\$1,545.00	\$1,591.00	\$1,638.00
64 KR	\$1,545.00	\$1,591.00	\$1,638.00
66 KR	\$1,600.00	\$1,648.00	\$1,696.00
70 KR	\$1,627.00	\$1,676.00	\$1,725.00
72 KR	\$1,545.00	\$1,591.00	\$1,638.00
74 KR	\$1,545.00	\$1,591.00	\$1,638.00
76 KR	\$1,600.00	\$1,648.00	\$1,696.00
	\$18,996.00	\$19,564.00	\$20,138.00
Annual Rent	\$227,952.00	\$234,768.00	\$241,656.00

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.