

INTRODUCTION

- [1] On September 28, 2023 the Landlord mailed the Tenants 5 *Notices of Annual Allowable Rent Increases* (the “Form 8 Notices”) which stated that the undiscounted rents for the Units would be increased by the annual guideline 3.0% effective January 1, 2024.
- [2] On April 18, 2024, the Landlord filed 5 *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 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 10:00 a.m. on July 2, 2024.
- [4] On June 25, 2024 the Rental Office provided the parties with a 35-page evidence package (“EP”), which included a *Landlord Statement of Income and Expenses* dated June 20, 2024 (the “Statement”).
- [5] On July 2, 2024 at 10:00 a.m. a teleconference hearing was held before the Residential Tenancy Officer (the “Officer”). Three representatives of the Landlord 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

- [6] The Landlord’s evidence is summarized as follows.
- [7] The 5 Units are located in a development of the Landlord containing a total of 21 rental units that were completed in 2020 and 2021.
- [8] The Landlord submitted into evidence documents supporting the proposed rent increases, including a rental income ledger (the “Ledger”) and letters to the Tenants (the “Letters”) that accompanied the Applications.
- [9] The Landlord made the following submissions regarding rent discounts. When rental units are built there is oftentimes obligations that are tied to draws. By times it is beneficial to take a lower rent amount with a tenant in order to get a unit rented. The Landlord has found that if tenants are going to make a commitment, then they do not want to get into year two and have a significant jump in rent payments. The Landlord does not remove the discount until the tenants move out. The Landlord communicates to its tenants the base, non-discounted rent in its documentation.
- [10] The Ledger (EP8) included the following comment regarding rent discounts for the Units:

“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 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.”

- [12] The Statement provides details of the changes in the expenses for the Units.
- [13] The mortgage maturity dates for two of the Units' buildings occurred in early 2024 and the interest rates increased to 7.30%. The maturity date for two of the buildings are on December 2, 2025 and March 2, 2026. These loans have interest rates of 2.00% and 1.99%.
- [14] The Landlord incurs property management fees of 7.5% but only 5.0% are permitted. The Statement does not include a deduction for mortgage principal payments or income taxes even though the Landlord must make these payments.
- [15] The Landlord provided capital investment evidence regarding the purchase price, capital expenditures and the replacement value. The Landlord provided the mortgage balance and property tax assessment documents.
- [16] In the Statement the Landlord's capital investment 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.
- [17] 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. The Landlord provided written submissions regarding capital investment which state in part:

“The capital being utilized by a landlord is the value of the current property less the current mortgage. This is capital that a Landlord would have access to if they were to sell the property. This capital if accessed could be used to produce a return on investment in other investments. One example today is a GIC at 5% which has no risk, no headaches, no management overhead. Taking on the risks associated with a rental property (vacancy, interest rates, inflation, repair and maintenance, unruly tenants etc).

If we need more housing on PEI then we need to make it reasonably attractive for investment...”

- [18] The Landlord submits that it is important for Government to continue reassessing its approach on rentals. There needs to be a financial return on these investments because the alternative is to have condos or other forms of housing. The Landlord stated that this is by no means a threat to the Tenants and the Landlord wants to keep the community the way it is.
- [19] The Landlord provided return on investment calculations based on different mortgage scenarios.
- [20] The Landlord is not aware of earlier Rental Office rent increase decisions regarding the Units.
- [21] The Landlord stated that IRAC's 2023 rent increase was supposed to be significant but was reduced to zero percent by Government.
- [22] The Landlord submits that through communications with the Tenants and no attendance by the Tenants at the hearing, the Landlord believes that many Tenants understand that the rent increases are reasonable and fair. The Landlord provided evidence regarding increases in CPP and OAS.

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?

- [23] For the reasons below, the Officer finds that the *RRPA* and the *Act* do not authorize rent discounts by written agreements.
- [24] 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.
- [25] 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]

- [26] 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>

[27] 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.”

[28] 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.”

[29] 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.

[30] 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).

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

[32] In this case, most of the Landlord's rent discounts are approximately \$250.00 in excess of the rents actually charged.

[33] However, the logical extension of rent discounts by 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>

- [34] 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.
- [35] 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.
- [36] With regard to the Units, there does not appear to be previous Rental Office or Commission orders authorizing phased in rents.
- [37] The Officer will determine the Applications based upon the rents actually charged as shown in the rental income ledger provided by the Landlord (EP8 to 9).

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

Adjustments to the Statement

- [38] The Officer's adjustments to the Statement are provided below and are reflected in Appendix "A".
- [39] The annual income, arrears, net income and management fees are calculated based upon the actual rents charged, as shown in the Ledger. The calculations of the annual incomes are provided in Appendix "B".
- [40] 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.
- [41] The term "capital investment" is undefined.
- [42] 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.
- [43] 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.
- [44] 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.
- [45] 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.
- [46] The Officer also notes that in Order LR23-80⁴ the Commission referred to "equity" when calculating return on investment.

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

- [47] The Officer will calculate the Landlord's capital investment with a mortgage deduction.
- [48] The Landlord's capital investment is \$273,423.00 based upon the purchase price plus capital expenditures amount in the Statement minus the outstanding mortgage (\$1,034,649.00 minus \$761,226.00).
- [49] The Landlord provided an alternate value of \$1,450,000.00 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 \$632,047.62 (5 units divided by 21 units of the total tax assessed value; see paragraph [57], below). The averaged value would be \$1,041,023.81. After deducting the mortgage (\$761,226.00), the Landlord's capital investment would be \$279,797.81.
- [50] The Landlord's return on investments are shown in Appendix "A" using both calculated values of capital investment.

Factors

- [51] 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.
- [52] 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 2020 and 2021.

Review and Weighing the Factors

- [53] The Landlord's rental income ledger shows that most of the last rent increases for the Units occurred about two years ago. The Landlord's operating costs and capital expenditures have increased by approximately \$8,000.00 since 2023 and the proposed 6.0% increase would cause an annual rent increase of \$5,736.00. None of the tenants provided evidence or submissions opposing the increases. These factors generally support rent increases above the 3.0% guideline for 2024.
- [54] It appears to the Officer that the Landlord's return on investment weighs heavily against above guideline rent increases.
- [55] The Landlord's calculated return on capital investment with the current rents would be 9.1% based upon the original purchase price plus capital expenditures minus the mortgage balance. This return would increase to 11.1% with rent increases of 6.0%.

- [56] The Landlord's return on capital investment with the current rents would be 8.9% based upon the current, averaged replacement cost and tax assessed value minus the mortgage balance. This return would increase to 10.8% with rent increases of 6.0%.
- [57] In a recent decision, Order LR24-27⁵, 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..."*
- [58] The Landlord would currently be making a return on investment 2.1% higher than the typical 7.0% based upon the first calculation using the original purchase price plus capital expenditures minus the mortgage balance.
- [59] The Landlord would be making a return on investment 4.9% higher than the typical 4.0% based upon the second calculation using blended replacement cost and tax assessed values minus the mortgage balance.
- [60] The Officer also notes that the Landlord's increased operating costs and capital expenditures have been factored into these two return on investment calculations.
- [61] 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

- [62] 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.
- [63] On April 18, 2024 the Applications were filed seeking 6.0% rent increases effective May 1, 2024.
- [64] 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)).
- [65] 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.
- [66] 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).
- [67] The Letters from the Landlord that accompanied the Applications sent to the Tenants state in part:

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

“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.”

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

CONCLUSION

[69] 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.

[70] **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>
3-27 RGL	\$1,616.00
4-23 RGL	\$1,586.00
3-17 RGL	\$1,664.00
4-17 RGL	\$1,664.00
5-11 RGL	\$1,690.00

DATED at Charlottetown, Prince Edward Island, this 29th day of August, 2024.

(sgd.) Andrew Cudmore
Andrew Cudmore
Residential Tenancy Officer

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

Rental Income	Current	3% Increase	6% Increase
Income (Line 1)	\$95,784.00	\$98,640.00	\$101,520.00
Arrears (Line 2)	(\$957.84)	(\$986.40)	(\$1,015.20)
Net Income (Line 3)	\$94,826.16	\$97,653.60	\$100,504.80

Expenses	Current	3% Increase	6% Increase
1st Mortgage Interest (Line 4)	\$33,851.00	\$33,851.00	\$33,851.00
2nd Mortgage Interest (Line 5)	\$0.00	\$0.00	\$0.00
Fuel (Line 6)	\$0.00	\$0.00	\$0.00
Water & Sewer (Line 7)	\$2,950.00	\$2,950.00	\$2,950.00
Electricity (Line 8)	\$48.00	\$48.00	\$48.00
Insurance (Line 9)	\$2,520.00	\$2,520.00	\$2,520.00
Property Tax (Provincial) (Line 10)	\$5,748.00	\$5,748.00	\$5,748.00
Property Tax (Municipal) + IWMC (Line 11)	\$5,742.00	\$5,742.00	\$5,742.00
Management Fee (Line 12)	\$4,741.31	\$4,882.68	\$5,025.24
Maintenance Fee (Line 13)	\$5,520.00	\$5,520.00	\$5,520.00
Capital Expenditures (Line 14)	\$5,100.00	\$5,100.00	\$5,100.00
Other (Line 15)	\$3,707.00	\$3,707.00	\$3,707.00
Total Expenses	\$69,927.31	\$70,068.68	\$70,211.24
Annual Net Profit	\$24,898.85	\$27,584.92	\$30,293.56

Original Purchase Price Plus Capital Expenditures Minus Current Mortgage

Value of Investment	\$273,423.00	\$273,423.00	\$273,423.00
Net Profit	\$24,898.85	\$27,584.92	\$30,293.56
Return on Capital Investment	9.1%	10.1%	11.1%

Average of Current Replacement Cost and Tax Assessed Value Minus Current Mortgage

Value of Investment	\$279,797.81	\$279,797.81	\$279,797.81
Net Profit	\$24,898.85	\$27,584.92	\$30,293.56
Return on Capital Investment	8.9%	9.9%	10.8%

APPENDIX “B”

Rent

Unit	Current	3% Increase	6% Increase
3-27 RGL	\$1,569.00	\$1,616.00	\$1,663.00
4-23 RGL	\$1,540.00	\$1,586.00	\$1,632.00
3-17 RGL	\$1,616.00	\$1,664.00	\$1,713.00
4-17 RGL	\$1,616.00	\$1,664.00	\$1,713.00
5-11 RGL	\$1,641.00	\$1,690.00	\$1,739.00
	\$7,982.00	\$8,220.00	\$8,460.00
Annual Rent	\$95,784.00	\$98,640.00	\$101,520.00

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.