

INTRODUCTION

- [1] On September 28, 2023 the Landlord mailed the Tenants 10 *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 10, 2024, the Landlord filed 10 *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 July 2, 2024.
- [4] On June 27, 2024 the Rental Office provided the parties with a 48-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 1:00 p.m. a teleconference hearing was held before the Residential Tenancy Officer (the "Officer"). Three representatives of the Landlord and two 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 10 Units are located in buildings containing 12 rental units, which the Landlord purchased in the Fall of 2018. The Statement was prepared using the income and expenses for the 12 units. There are a total of 24 rental units in the development.
- [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 increasing costs:

"Between 2021 and 2024: interest rates increased (100% plus), property taxes (30%), repair and maintenance costs (30%), insurance premiums (90%) 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 increases 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 still only 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 is September 2, 2026.
- [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 \$3,000.00 from 2021 to 2024.
- [11] The Statement does not include a deduction for mortgage principal payments. The Landlord's actual management fees are 7.5% but are capped at 5.0% in the Statement.
- [12] 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.
- [13] 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..."

- [14] The Landlord provided evidence regarding increases in CPP and OAS and the annual allowable increases.
- [15] The Landlord stated that it would have been better if larger rent increases were previously permitted over a number of years. The Landlord submits that if the Units cannot work as rentals, then they need to work as another type of product. The Landlord noted that there are stories in the media regarding rentals being converted to condos. The Landlord is not threatening to go down that road but the Landlord wants everyone to understand that there needs to be a reasonable outcome and return on investment.

Tenants' Evidence and Submissions

- [16] The Tenants' evidence is summarized as follows.
- [17] One of the Tenants stated that their Unit had an increase in 2020, which is not covered by the time period in the Statement. The Tenant understands that the Landlord's expenses have increased but the Tenant's daily living expenses have also increased.
- [18] One of the Tenants provided evidence regarding maintenance matters. The Tenant moved into their Unit in December of 2023. The Tenant stated that they did not believe that their rent could increase yet because they had not lived in their Unit for 12 months. The first page of the Tenant's agreement states in part as follows:

"Please note: The rental rate will increase on Jan 1/24 by 3%. The rental rate in January will be \$1317.00 monthly."

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] 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.
- [22] The term "capital investment" is undefined.
- [23] 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.
- [24] 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.
- [25] 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.
- [26] 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.
- [27] The Officer also notes that in Order LR23-80¹ the Commission referred to "equity" when calculating return on investment.
- [28] The Officer will calculate the Landlord's capital investment with a mortgage deduction.
- [29] The Landlord's capital investment is \$591,134.00 based upon the purchase price plus capital expenditures amount in the Statement minus the outstanding mortgage (\$1,703,312 minus \$1,112,178.00).
- [30] The Landlord provided an alternate value of \$3,600,000.00 based upon the current estimated replacement cost of the Units and the two other rental units included in the Statement that were increased by the 2024 guideline. 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 \$1,491,400.00 (see paragraph [42], below). The averaged value would be \$2,545,700.00. After deducting the mortgage (\$1,112,178.00), the Landlord's capital investment would be \$1,433,522.00.

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

[31] The Landlord's return on investments are shown in Appendix "A" using both calculated values of capital investment.

Factors

[32] 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.

[33] 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 purchased in 2018.

Review and Weighing the Factors

[34] For the determination of a rent increase above the 2024 guideline of 3.0%, the factor regarding the rent history of a unit is limited to a three-year period in the *Act*. This is the time period legislated in the *Act* by Government and the Officer does not have authority to extend this period.

[35] The Landlord's rental income ledger shows that most of the last rent increases for the Units occurred in 2021. This first factor regarding the rent history of the Units generally supports above guideline rent increases.

[36] Most of the Tenants did not participate in the Rental Office hearing or provide written submissions opposing rent increases above the 3.0% guideline. However, there was participation by two Tenants opposing above guideline rent increases. One of the Tenants had only expected a guideline rent increase based on the written tenancy agreement. The expectations of the two Tenants that participated in the hearing weighs against above guideline rental increases for their two units. The evidence presented by the Landlord provides some support for above guideline increases for the other eight Units.

[37] The second and fourth factors weigh against above guideline rent increases.

[38] With regard to the second factor, the Landlord's operating costs and capital expenditures have increased by approximately \$3,000.00 since 2021. The net income with 3.0% rent increases would be approximately \$13,500.00 higher than 2021 and 6.0% rent increases would be \$18,000.00 higher. The Landlord's mortgage renewal is not scheduled to occur for about two years and a possible rate increase this far away will not be considered by the Officer. As a result, the change in operating expenses and capital expenditures does not support above guideline rent increases.

[39] The Landlord's return on investment weighs against above guideline rent increases.

- [40] The Landlord's calculated return on capital investment with the current rents would be 12.1% based upon the original purchase price plus capital expenditures minus the mortgage balance. This return would increase to 13.8% with rent increases of 6.0%.
- [41] The Landlord's return on capital investment with the current rents would be 5.0% based upon the current, averaged replacement cost and tax assessed value minus the mortgage balance. This return would increase to 5.7% with rent increases of 6.0%.
- [42] 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..."*
- [43] With 6.0% rent increases, the Landlord would be making a return on investment 6.8% higher than the typical 7.0% based upon the first calculation using the original purchase price plus capital expenditures.
- [44] With 6.0% rent increases, the Landlord would be making a return on investment 1.7% higher than the typical 4.0% based upon the second calculation using blended replacement cost and tax assessed values.
- [45] As the Landlord's return on capital investment is significantly higher than the returns typically permitted for above guideline rent increases and the Landlord's operating costs and capital expenditures have not significantly increased, the Officer finds that these factors outweigh the other factors. As a result, the Officer finds that rent increases above the 3.0% guideline will not be authorized by this decision.

Effective Date

- [46] 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.
- [47] On April 10, 2024 the Applications were filed seeking 6.0% rent increases effective May 1, 2024.
- [48] 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)).
- [49] 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.
- [50] 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).

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

- [51] The Officer finds that the appropriate effective date for the rent increases is September 1, 2024.
- [52] For one of the Tenants that participated in the hearing this rent increase is within 12 months of when the Tenant moved in. However, this Tenant's written tenancy agreement incorporated the guideline 3.0% increase for 2024 as a term. Therefore, the Officer cannot find that there was a contractual restriction against a guideline increase based upon the tenancy agreement.
- [53] Further, the applicable rent increase restriction in subsection 48(1) of the *Act* is 12 months from the date of the last increase. This restriction against rent increases is tied to the Unit, not the person occupying the Unit.
- [54] In this case the Unit's rent was last increased on June 1, 2021. Therefore, this legislated restriction only prevented a rent increase for the Unit up to May 31, 2022.

CONCLUSION

- [55] 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.
- [56] **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:

Unit	3% Increase
119 EA	\$1,317.00
120 EA	\$1,317.00
121 EA	\$1,317.00
123 EA	\$1,230.00
124 EA	\$1,212.00
126 EA	\$1,317.00
127 EA	\$1,374.00
128 EA	\$1,212.00
129 EA	\$1,405.00
130 EA	\$1,317.00

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)

	Current	3% Increase	6% Increase*
Rental Income			
Income (Line 1)	\$186,492.00	\$192,072.00	\$196,680.00
Arrears (Line 2)	(\$1,864.92)	(\$1,920.72)	(\$1,966.80)
Net Income (Line 3)	\$184,627.08	\$190,151.28	\$194,713.20
 Expenses			
1st Mortgage Interest (Line 4)	\$33,626.00	\$33,626.00	\$33,626.00
2nd Mortgage Interest (Line 5)	\$0.00	\$0.00	\$0.00
Fuel (Line 6)	\$0.00	\$0.00	\$0.00
Water & Sewer (Line 7)	\$8,482.00	\$8,482.00	\$8,482.00
Electricity (Line 8)	\$113.00	\$113.00	\$113.00
Insurance (Line 9)	\$6,139.00	\$6,139.00	\$6,139.00
Property Tax (Provincial) (Line 10)	\$13,569.81	\$13,569.81	\$13,569.81
Property Tax (Municipal) + IWMC (Line 11)	\$13,592.00	\$13,592.00	\$13,592.00
Management Fee (Line 12)	\$9,231.35	\$9,507.56	\$9,735.66
Maintenance Fee (Line 13)	\$17,449.00	\$17,449.00	\$17,449.00
Capital Expenditures (Line 14)	\$5,451.00	\$5,451.00	\$5,451.00
Other (Line 15)	\$5,192.00	\$5,192.00	\$5,192.00
Total Expenses	\$112,845.16	\$113,121.37	\$113,349.47
 Annual Net Profit	\$71,781.92	\$77,029.91	\$81,363.73
 Original Purchase Price Plus Capital Expenditures Minus Current Mortgage			
Value of Investment	\$591,134.00	\$591,134.00	\$591,134.00
Net Profit	\$71,781.92	\$77,029.91	\$81,363.73
Return on Capital Investment	12.1%	13.0%	13.8%
 Average of Current Replacement Cost and Tax Assessed Value Minus Current Mortgage			
Value of Investment	\$1,433,522.00	\$1,433,522.00	\$1,433,522.00
Net Profit	\$71,781.92	\$77,029.91	\$81,363.73
Return on Capital Investment	5.0%	5.4%	5.7%

APPENDIX "B"

Unit	Rent		
	Current	3% Increase	6% Increase*
119 EA	\$1,279.00	\$1,317.00	\$1,356.00
120 EA	\$1,279.00	\$1,317.00	\$1,356.00
121 EA	\$1,279.00	\$1,317.00	\$1,356.00
122 EA*	\$1,450.00	\$1,494.00	\$1,494.00
123 EA	\$1,194.00	\$1,230.00	\$1,266.00
124 EA	\$1,177.00	\$1,212.00	\$1,248.00
125 EA*	\$1,450.00	\$1,494.00	\$1,494.00
126 EA	\$1,279.00	\$1,317.00	\$1,356.00
127 EA	\$1,334.00	\$1,374.00	\$1,414.00
128 EA	\$1,177.00	\$1,212.00	\$1,248.00
129 EA	\$1,364.00	\$1,405.00	\$1,446.00
130 EA	\$1,279.00	\$1,317.00	\$1,356.00
	\$15,541.00	\$16,006.00	\$16,390.00
Annual Rent	\$186,492.00	\$192,072.00	\$196,680.00

* 6.0% increases for the 10 Units; 122 EA and 125 EA are only guideline increases of 3.0%

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.