

**INTRODUCTION**

- [1] On September 28, 2023 the Landlord mailed the Tenants 16 *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 16 *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 17, 2024 the Rental Office mailed and emailed the parties notice of a teleconference hearing scheduled for 9:00 a.m. on July 4, 2024.
- [4] On June 27, 2024 the Rental Office provided the parties with a 36-page evidence package ("EP"), which included a *Landlord Statement of Income and Expenses* dated June 24, 2024 (the "Statement").
- [5] On July 4, 2024 at 9:00 a.m. a teleconference hearing was held before the Residential Tenancy Officer (the "Officer"). Three representatives of the Landlord participated in the hearing.

**ISSUE**

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 16 Units are located in four four-unit buildings that were constructed in 2014.
- [8] The Landlord submitted into evidence documents supporting the proposed rent increases. The Statement provides details of the changes in the expenses for the Units.
- [9] The former mortgage had a maturity date of June 1, 2024. The Landlord recently refinanced with a new lender and the interest rate increased from 2.41% to 6.95%. The current mortgage balance is approximately \$998,000.00. If the Landlord would have stayed with their former lender, then there would have been a higher interest rate.
- [10] The Landlord incurs property management fees of 7.5% but only 5.0% are permitted in the Statement. The Statement does not include a deduction for mortgage principal payments or income taxes even though the Landlord must make these payments.
- [11] The Landlord provided capital investment evidence regarding the purchase price, capital expenditures and the replacement value. The Landlord provided property tax assessment documents.
- [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. The Landlord submits that the formula in the Statement should align with the calculations completed in Rental Office decisions.
- [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 submits that, based upon communications with the Tenants and with no attendance by any of 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.
- [15] The Landlord submits that, if rent increases were tied to the tenant and not the rental unit, then it would be much easier to address increases in expenses without significantly increasing rents for current tenants.

## ANALYSIS

### Adjustments to the Statement

- [16] The Officer's adjustments to the Statement are provided below and are reflected in Appendix "A".
- [17] The Landlord's current annual income and the incomes at 3.0% and 6.0% increases are provided in Appendix "B".
- [18] The Landlord's mortgage balance for the Units is approximately \$998,000.00. The Landlord has paid down approximately \$72,000.00 per year of the mortgage principal. The Officer estimates the annual interest payment based on the current interest rate of 6.95% and a reduction of \$36,000.00 of the total principal balance to reflect the balance half way through the year. The annual interest payable for the Units with these adjustments would be \$66,859.00.
- [19] 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.
- [20] The term "capital investment" is undefined.
- [21] 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.
- [22] 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.

- [23] 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.
- [24] 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.
- [25] The Officer also notes that in Order LR23-80<sup>1</sup> the Commission referred to "equity" when calculating return on investment.
- [26] The Officer will calculate the Landlord's capital investment with a mortgage deduction.
- [27] The Landlord's capital investment is \$1,547,347.00 based upon the purchase price plus capital expenditures amount in the Statement minus the outstanding mortgage (\$2,545,347.00 minus \$998,000.00).
- [28] The Landlord provided an alternate value of \$5,760,000.00 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 \$2,009,300.00 (see paragraph [34], below). The averaged value would be \$3,884,650.00. After deducting the mortgage (\$998,000.00), the Landlord's capital investment would be \$2,886,650.00.
- [29] The Landlord's return on investments are shown in Appendix "A" using both calculated values of capital investment.

### Factors

- [30] 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.
- [31] 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 2014.

### Review and Weighing the Factors

- [32] The Landlord's rental income ledger shows that most of the last rent increases for the Units occurred approximately two years ago. Compared to the amounts in the Revised Statement, the Landlord's operating costs and capital expenditures have increased by approximately \$46,000.00

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

since 2021 while the rents have increased by approximately \$5,500.00. The Applications apply to 16 Units and none of the Tenants participated in the hearing to dispute the above guideline rent increases. These factors generally support rent increases above the 3.0% guideline for 2024.

[33] In this case, the Landlord's return on investment also supports above guideline increases.

[34] In a recent decision, Order LR24-27<sup>2</sup>, 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..."*

[35] The Landlord's calculated return on capital investment with the current rents would be 5.5% based upon the original purchase price, capital expenditures and mortgage balance. This return would increase to 6.5% with rent increases of 6.0%.

[36] The Landlord's return on capital investment with the current rents would be 2.9% based upon the current, averaged replacement cost and tax assessed value and mortgage balance. This return would increase to 3.5% with rent increases of 6.0%.

[37] Based upon these factors the Officer finds that 6.0% rent increases are supported for the Units.

#### **Effective Date**

[38] 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.

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

[40] 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)).

[41] 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.

[42] 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).

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

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

**CONCLUSION**

- [44] The Landlord's Applications for above guideline rent increases are allowed. The rents for the Units are increased by 6.0% as provided below.
- [45] **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>
1-19 SMD	\$1,617.00
2-19 SMD	\$1,708.00
3-19 SMD	\$1,569.00
4-19 SMD	\$1,621.00
5-19 SMD	\$1,628.00
6-19 SMD	\$1,410.00
7-19 SMD	\$1,531.00
8-19 SMD	\$1,632.00
9-19 SMD	\$1,490.00
10-19 SMD	\$1,601.00
11-19 SMD	\$1,569.00
12-19 SMD	\$1,490.00
13-19 SMD	\$1,644.00
14-19 SMD	\$1,617.00
15-19 SMD	\$1,490.00
16-19 SMD	\$1,672.00

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

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(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)	\$286,272.00	\$294,840.00	\$303,468.00
Arrears (Line 2)	(\$2,862.72)	(\$2,948.40)	(\$3,034.68)
Net Income (Line 3)	\$283,409.28	\$291,891.60	\$300,433.32
Expenses			
1st Mortgage Interest (Line 4)	\$66,859.00	\$66,859.00	\$66,859.00
2nd Mortgage Interest (Line 5)	\$0.00	\$0.00	\$0.00
Fuel (Line 6)	\$0.00	\$0.00	\$0.00
Water & Sewer (Line 7)	\$8,465.00	\$8,465.00	\$8,465.00
Electricity (Line 8)	\$18,868.00	\$18,868.00	\$18,868.00
Insurance (Line 9)	\$7,190.00	\$7,190.00	\$7,190.00
Property Tax (Provincial) (Line 10)	\$18,348.48	\$18,348.48	\$18,348.48
Property Tax (Municipal) + IWMC (Line 11)	\$16,669.38	\$16,669.38	\$16,669.38
Management Fee (Line 12)	\$14,170.46	\$14,594.58	\$15,021.67
Maintenance Fee (Line 13)	\$32,802.00	\$32,802.00	\$32,802.00
Capital Expenditures (Line 14)	\$8,656.00	\$8,656.00	\$8,656.00
Other (Line 15)	\$6,726.00	\$6,726.00	\$6,726.00
Total Expenses	\$198,754.32	\$199,178.44	\$199,605.53
Annual Net Profit	\$84,654.96	\$92,713.16	\$100,827.79
<b>Original Purchase Price Plus Capital Expenditures Minus Current Mortgage</b>			
Value of Investment	\$1,547,347.00	\$1,547,347.00	\$1,547,347.00
Net Profit	\$84,654.96	\$92,713.16	\$100,827.79
Return on Capital Investment	5.5%	6.0%	6.5%
<b>Average of Current Replacement Cost and Tax Assessed Value Minus Current Mortgage</b>			
Value of Investment	\$2,886,650.00	\$2,886,650.00	\$2,886,650.00
Net Profit	\$84,654.96	\$92,713.16	\$100,827.79
Return on Capital Investment	2.9%	3.2%	3.5%

**APPENDIX "B"****Rent**

Unit	Current	3% Increase	6% Increase
1-19 SMD	\$1,525.00	\$1,571.00	\$1,617.00
2-19 SMD	\$1,611.00	\$1,659.00	\$1,708.00
3-19 SMD	\$1,480.00	\$1,524.00	\$1,569.00
4-19 SMD	\$1,529.00	\$1,575.00	\$1,621.00
5-19 SMD	\$1,536.00	\$1,582.00	\$1,628.00
6-19 SMD	\$1,330.00	\$1,370.00	\$1,410.00
7-19 SMD	\$1,444.00	\$1,487.00	\$1,531.00
8-19 SMD	\$1,540.00	\$1,586.00	\$1,632.00
9-19 SMD	\$1,406.00	\$1,448.00	\$1,490.00
10-19 SMD	\$1,510.00	\$1,555.00	\$1,601.00
11-19 SMD	\$1,480.00	\$1,524.00	\$1,569.00
12-19 SMD	\$1,406.00	\$1,448.00	\$1,490.00
13-19 SMD	\$1,551.00	\$1,598.00	\$1,644.00
14-19 SMD	\$1,525.00	\$1,571.00	\$1,617.00
15-19 SMD	\$1,406.00	\$1,448.00	\$1,490.00
16-19 SMD	\$1,577.00	\$1,624.00	\$1,672.00
	\$23,856.00	\$24,570.00	\$25,289.00
Annual Rent	\$286,272.00	\$294,840.00	\$303,468.00

**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.