



Summary Report and Analysis: Allowable Percentage Rent Increase for 2012

**Pursuant to Section 23 of the
*Rental of Residential Property Act***

September 12, 2011

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I. INTRODUCTION

The following report has been prepared in order to provide the Commission with background information to establish the allowable percentage rent increase for 2012. This report contains information which outlines the statutory requirements pursuant to the *Rental of Residential Property Act (the “Act”)*, an overview of the current housing market situation, the average rent increase in other jurisdictions proposed for 2012, analysis of increase factors including an assessment of the Consumer Price Index (CPI), and analysis of projected operating cost increases for the 2012 allowable percentage rent increase.

II. STATUTORY REQUIREMENTS

A. Subsection 23(1) of the *Rental of Residential Property Act* indicates:

Except as provided in subsection (3) and notwithstanding the terms of any rental agreement, the amount of any rent increase between January 1 and December 31 of any year shall not exceed the percentage amount which is established by an order of the Commission and published in the Gazette.

B. The prescribed rent increase should be published in the Royal Gazette no later than September 30, 2011 in order that the lessor will have the minimum three (3) months notice period required for a rent increase to be effective January 1.

C. Pursuant to subsection 23(3) of the *Act*, the lessor has the opportunity to recover extraordinary costs incurred by making an application to the Director for approval of a rent increase greater than the annual prescribed percentage rent increase.

D. As required under subsection 23(2) of the *Act*, the Director has requested written representation from lessors and lessees to assist in establishing the recommendation of the prescribed rate for the coming year. The request

was advertised in *The Guardian, the Journal-Pioneer, La Voix Acadienne, Island Press (Eastern Graphic and West Prince Graphic)*, the Royal Gazette and the Commission's web site.

The Director received five letters from lessors/landlords and one from lessees/tenants. Landlords identified the following concerns:

1. Uncertainty concerning future prices of oil and electricity costs represents a major concern. Past approved rent increases did not cover the increased cost of electricity and heating oil.
2. In addition, costs associated with sewer and water infrastructure, waste management fees and property tax assessments have taken increases in past years and have not been adequately included in past rent allowances.
3. General cost increases for all aspects of operating a rental property.

The one tenant comment received suggested the 2012 rent increase should be 2.0% for heated premises and 1% for unheated premises and mobile home parks, although no justification for this recommendation was provided.

III. CURRENT SITUATION

PEI Housing Outlook

A review of CMHC Housing Market Outlook for PEI issued Spring 2011 confirms the increased activity related to multi-unit housing in Charlottetown and throughout PEI in the past couple of years. Strong government spending on schools, roads, and hospitals has driven employment the past couple of years and housing investments. There have been significant investments made in multi-unit housing in Charlottetown and to a lesser extent Summerside during the past two years.

The dominant characteristic about PEI housing market at present is the migration of people to the two major urban centers, Charlottetown and Summerside. This growth in the urban housing market is attributed to both the Province's international immigration initiative and the movement of rural Islanders to urban centres. However, international immigration may have peaked in 2011 due to government program changes. Rural migration continues and the improved economic situation in western Canada is, again, attracting younger Islanders to relocate in Western Canada. This 18-24 year old demographic is a significant market for rental properties.

As noted above, the Charlottetown rental market has seen significant construction over the past two years. New rental property construction starts for 2009 and 2010 far exceeded the preceding 10 year average. The increased supply of rental units from this construction, which more than offsets the demand, can be attributed to Charlottetown’s increasing vacancy rates.

Vacancy rates

The most recent CMHC Rental Market Report indicates the provincial overall average vacancy rate has increased to 4.5 per cent in April 2011 from 3.3 per cent for the same period last year. Charlottetown experienced a higher vacancy rate at 4.9 per cent than the provincial average.

The CMHC survey states the average Charlottetown two-bedroom unit in April 2011 was \$770 as compared to \$722 in 2010. In Summerside the average two-bedroom rental was \$660 in 2011 as compared to \$633 in 2010.

Statistical Overview

Statistical information (as shown on Table 1) provided by CMHC indicates the following vacancy rates for the Charlottetown and Summerside area from 1992 - 2011:

TABLE 1

<i>YEAR</i>	<i>CHARLOTTETOWN</i>	<i>SUMMERSIDE</i>
1992	6.40	4.90
1993	6.40	9.30
1994	6.20	7.90
1995	7.10	7.60
1996	4.00	7.50
1997	4.10	6.90
1998	6.10	8.80
1999	5.00	5.50
2000	2.60	5.50
2001	1.80	5.50
2002	2.10	6.00
2003	3.40	4.60
2004	4.20	4.20
2005	4.40	4.40
2006	4.80	7.80
2007	4.30	7.80
2008	5.20	3.60
2009	3.40	3.20
2010	2.70	6.70
2011	4.90	2.30

IV. ECONOMIC OUTLOOK

The most recent pronouncement from the Bank of Canada, to maintain overnight target interest rates at current levels, noted the deterioration in the global economy which has occurred since early summer 2011. The European Union countries are experiencing debt refinancing difficulties and cuts to government services have not been easily accepted by citizens. The American economy shows stalling in growth with consumer spending weakening. American households are burdened with debt and the labor market for job creation is weak. Canada’s economic numbers show economic growth stalled in the second quarter of 2011. Canada’s economy will not be immune to the effects of a slowing global economy. The Bank of Canada expects Canada’s inflation will return to the target 2 percent rate as a result of the slowing economy.

The Royal Bank of Canada announced on September 12 that its 2011 forecast of economic growth for Canada has been reduced by 0.8% to 2.4%. This is the highest prediction of economic growth from any of Canada’s major banks. The Royal Bank of Canada notes the slowing global economy, the financial situation in Europe, and the uncertainties associated with US job creation as reasons of concern for the Canadian economy.

The Royal Bank’s recent economic commentary states the PEI economy has been shielded from the effects of the slowing economy due to it’s significant public infrastructure investments and low interest rates for private sector development. The PEI export economy has seen positive results in the agri-food industries with improving prices, however, poor prices in the lobster industry and low tourism numbers have limited overall growth. The Royal Bank predicts PEI growth of 2.2 percent for 2011 and 1.9 percent for 2012.

V. OTHER JURISDICTIONS

Across Canada, the only other provinces with rent control are Ontario, Manitoba and British Columbia.

A. Ontario

The 2012 rent increase guideline is calculated under the *Ontario Residential Tenancies Act*, which created a system of rent regulation that links the annual rent increase to the Ontario Consumer Price Index. This calculation results in a rent control guideline for 2012 of 3.1%. Past rent increases are listed below.

Year	% Rent Increase
2011	0.7
2010	2.1
2009	1.8
2008	1.4

2007	2.6
2006	2.1
2005	1.5

B. Manitoba

The rent increase guideline for 2012 is 1.0%. This guideline applies to apartments or houses renting for less than \$1,120.00 a month as of December 31, 2010. Past rent increases are listed below.

Year	% Rent Increase
2011	1.5
2010	1.0
2009	2.5
2008	2.0
2007	2.5
2006	2.5
2005	1.5

C. British Columbia

The rent increase guideline for 2012 is 4.3%. Past rent increases are listed below.

Year	% Rent Increase
2011	2.3
2010	3.2
2009	3.7
2008	3.7
2007	4.0
2006	4.0
2005	3.8

VI. ANALYSIS

In determining the annual percentage rent increase, two main factors were taken into consideration. The first involved an assessment of the CPI All Items and CPI Shelter indexes for the 2011 period.

The second set of factors included an assessment of the specific operating expenses and anticipated component cost increases for rental units.

A. CPI Analysis

A **consumer price index** (CPI) is a measure estimating the average price of consumer goods and services purchased by households. A consumer price index measures a price change for a constant market basket of goods and services from one period to the next within the same area. The percent change in the CPI is a measure estimating inflation or price changes.

Although somewhat simplified, an analysis of CPI changes should reflect anticipated changes in building operating costs as measured by price changes.

Tables 3 and 4 provide additional detail on the actual percentage change in the CPI for Prince Edward Island for 2005 to July 2011, as well as the most recent various sub indexes measured by Statistics Canada.

TABLE 3

Year	CPI
2005	3.1%
2006	2.3%
2007	1.8%
2008	3.4%
2009	-0.2%
2010	1.8%
2011	3.2% (July 2010 to July 2011)

TABLE 4

Consumer Price Index, by province (monthly)					
(Prince Edward Island)					
	July 2010	June 2011	July 2011	June 2011 to July 2011	July 2010 to July 2011
	2002=100			% change	
P.E.I.					
All-items	119.5	123.3	123.3	0.0	3.2
Food	127.4	131.7	133.2	1.1	4.6
Shelter	124.8	129.3	129.3	0.0	3.6
Household operations, furnishings and equipment	112.8	114.3	114.0	-0.3	1.1
Clothing and footwear	101.0	99.0	98.3	-0.7	-2.7
Transportation	116.6	125.5	124.4	-0.9	6.7
Health and personal care	113.3	114.4	115.1	0.6	1.6
Recreation, education and reading	108.6	107.9	108.0	0.1	-0.6
Alcoholic beverages and tobacco products	149.3	159.5	160.2	0.4	7.3
Special aggregates					
All items excluding food	117.9	121.6	121.3	-0.2	2.9
All items excluding energy	115.2	116.4	116.5	0.1	1.1
Energy	156.1	183.0	181.6	-0.8	16.3
Source: Statistics Canada, CANSIM, table (for fee) 326-0020 and Catalogue nos. 62-001-X and 62-010-X . Last modified: 2011-08-19.					

The Bank of Canada's monetary policy and Government of Canada's policy is to target inflation at 2.0%. The July 2011 national inflation rate was 2.7% as reported by Statistics Canada. The most recent Bank of Canada interest rate decision to hold the line on rates noted the deteriorating global economic situation. The Bank of Canada also commented that it expects core inflation rates to moderate due to this economic uncertainty.

B. Key Rental Cost Components

Heating Costs

The impact of heating costs either from electricity or petroleum products continue to be a significant factor for landlords. In past and present submissions, many landlords have suggested to the Commission previously approved increases have not covered their actual energy cost increases.

Many energy forecasters are suggesting that energy prices will remain at current rates over the next year. The US Energy Information Administration (EIA) Short Term Energy Outlook Report issued September 7, 2011 is forecasting a 5.7% heating fuel price increase in the 2011/12 heating season over the previous year. However, EIA suggests that historical price volatility of petroleum product prices due to supply and demand dynamics makes price forecasting difficult.

Property Taxes

The Department of Finance and Municipal Affairs manages the property tax system. Property taxes on non-owner occupied residential properties increase annually based on the market assessed value of these properties. It is anticipated that these increases will be within CPI level increases.

Waste Watch

There was a slight increase in these fees of \$4.85 per residential unit/year in 2010. Unsorted residential material drop off tippage fees were proposed to increase, however, this was deferred by Commission Order WM09-01. IWMC and the residential rental community were to review the issue and return to the Commission with a proposal. No such submission has been received by the Commission as of this report date. There was no increase in IWMC rates during 2011.

Electricity

Although not a major factor for many landlords, as most property owners do not provide electricity except for common areas. The PEI Energy Accord resulted in a 14% decrease in rates for residential customers including those heating by electricity.

Maintenance Costs

These are rising associated with CPI increases and the rising cost of energy overall. At a minimum, a CPI level of increase can be expected.

Interest

Interest rates have not changed significantly over the past year and pronouncements from the Bank of Canada indicate rates will not change in the foreseeable future.

VIII. CRITERIA FOR INCREASE

The statutory criteria to be considered in approving a rent increase are set out pursuant to subsection 23(8) of the *Act*:

(a) whether the increase in rent is necessary in order to prevent the lessor sustaining a financial loss in the operation of the building in which the premises are situate;

(b) increased operating costs or capital expenditures as advised by the lessor;

(c) the expectation of the lessor to have a reasonable return on his capital investment;

(d) such other matters as may be prescribed by the regulations.

Key factors to be considered include:

- information regarding the current state of the housing and rental unit industry,
- the change in operating costs for a residential rental building during the year, and
- uncertainty in the cost of heating oil.

Once the allowable percentage rent increase for 2012 has been determined by the Commission, the allowable increase shall be published in the *Royal Gazette*, advertised in the local newspapers and inserted on the Commission's web site.