

Everything old is new again:

Will the return of a broader rent control regime haunt the Ontario real estate bar?

For decades the existence of rent control has posed a risk to Ontario real estate lawyers acting on the purchase and mortgaging of residential rental property. The range of affected properties is immense: From a basement apartment to a rented single family house to the largest multi-residential complexes in the province, many real estate files can involve residential rental issues like rent control.

The *Rental Fairness Act, 2017* introduced amendments to the *Residential Tenancies Act, 2006* (“RTA”). The amendments were largely focused on expanding rent control and ensuring the continued availability of affordable and predictable rentals in Ontario. The changes forced many landlords of small and large residential real estate properties to pay attention to rent control for the first time from an operational perspective. They also constitute a red flag for lawyers involved in the conveyancing of residential real estate where tenancies are in place or anticipated.

Exemptions disappear and lawyer risk increases

The primary element of the *Rental Fairness Act* was a removal of the exemptions to rent control for private rental units. Under the earlier legislation, the following rental units were not generally subject to rent control (except for rules related to increase notices and anniversary dates):

- (1) unit in a building no part of which was occupied for residential purposes before November 1, 1991,
- (2) unit never occupied before June 17, 1998, or
- (3) unit never previously rented since July 29, 1975.

Those exemptions are now repealed, and such units are subject to the rent increase guidelines that dictate how much a landlord can increase the rent charged to a tenant. For 2018, the guideline amount is 1.8 per cent.

A property’s cash flow has a direct effect on its value and the ability of its owner to finance the property. Although it is tempting to argue that obtaining good title to the land is the only obligation of a real estate lawyer, case law suggests that there is also an obligation to investigate the reliability of the cash flow from a legal perspective for a rent controlled property, at least in some circumstances.¹ Lawyers should make sure clients planning to become landlords are aware of the expansion of rent control and any impact it may have on the ability to generate revenue. Purchasing clients may even be liable when assuming residential tenants who were previously

charged illegal rents, such as amounts above the guideline increase or resulting from increases at a rate more frequent than every 12 months. Lawful rents can even be automatically reduced if there have been property tax decreases (RTA, ss. 131(1)).

Two aspects of the RTA moderate, to some extent, the extreme potential impact of illegal rents: (a) the concept of vacancy decontrol, meaning that a new lawful rent can be set when there is a new tenant (RTA, s. 113); and (b) a one-year limitation period applicable in some cases to tenant applications for rent reductions and refunds of money collected or retained in contravention of the RTA (e.g., ss. 130(5) or 135(4)), although if the landlord fails to meet the 90-day rent increase notice requirement, there is an argument that the increase is totally void and not saved by the one year limitation period (RTA, ss. 116(4)).

What’s a real estate lawyer to do?

Of course, advising a client about the risks may be the easy part of the lawyer’s job. Actually determining whether the rents are legal can be a complicated exercise. For a period of years in the past Ontario had a rent registry where one could search for information on maximum rents. That has not been re-introduced. So, any investigation of rent legality will likely have to depend heavily on a review of the vendor’s records, to the extent such records exist and production can be required under the terms of the agreement of purchase and sale. Landlord and Tenant Board files are considered private by the Board and there is no information publicly available from the Board about past or pending proceedings affecting a property. That means the only source is the Canadian Legal Information Institute (CanLII) website, where some Board decisions are posted.

If a lawyer is retained before the agreement of purchase and sale is finalized, it is prudent to seek protection for the purchaser by inserting the following, at a minimum:

- a right to terminate the agreement if the purchaser is not satisfied as to the legality of the rents, currently and in the past (unless rebates have already been paid and rents rolled back); and

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¹ For example, see 669283 *Ontario Ltd. v. Reilly*, [1996] O.J. No. 273 (Gen. Div.); affirmed on appeal, [1998] O.J. No. 2780 (C.A.).



- a requirement that the vendor produce documentation that demonstrates the legality of the rents.

For larger complexes, there may be a need for extensive representations and warranties in the agreement, along perhaps with security to stand behind them and obligations to co-operate post-closing if rent legality issues emerge.

A prudent lawyer may want to exclude rent legality from the purchase or mortgage retainer if they are not providing an opinion on the legality of the property's current rents. This should be done as early in the transaction as possible and be in writing to ensure no confusion at a later stage of the process.

However, when implementing such a limitation on the lawyer's retainer, it is good practice to consider clients' ability to satisfy themselves about rent legality. For less sophisticated purchasers and first-time buyers, the lawyer may need to explain the ways rent could be illegal and the possible negative repercussions for the purchaser, both in terms of building value and exposure for rent rebates. It is preferable that lawyers engage in a discussion with each client about the options available, recording the details of the conversation and the client's choice in their files. There are lawyers and paralegals who specialize in rent control law – for some clients that may be a good path to take.

Mortgage documents (including the instructions to solicitor) often have very broad statements to the effect that the property complies in all ways with the RTA (or all applicable laws). Be careful when advising the borrower or lender if such requirements are present. Who is assuming the responsibility to the lender for this issue? Should the lawyer for the lender be carefully circumscribing the terms of the opinion that can be given, in light of what is known about the rents and/or the lawyer's personal comfort with this area of the law?

Other pitfalls to be avoided

Though the expanded applicability of the annual rent control guideline was the most widely publicized change to the RTA, there are other new and modified provisions that are relevant to the real estate bar.

As of January 1, 2018, landlords can no longer apply for rent increases above the guideline amount because of an increase in utility costs (e.g., hydro, water, or heat). Landlords can still apply for an increase above the guideline amount where there is an "extraordinary" increase in municipal tax costs (RTA, ss. 126 (1)). For real estate purchases where clients are assuming existing tenancies, lawyers should review whether utility costs are already included in the rents and advise their clients of the inability to raise the rent if utility prices increase.

For purchasing clients who require vacant possession on closing, there could be additional liability. If the client requires vacant possession of the property and the vendor serves the tenant with

60 days' notice on behalf of the purchaser, the purchaser will be liable if he/she chooses not to occupy the unit within a reasonable time (RTA, ss. 57(1)). Additionally, if the purchaser lists any units for rent to new tenants, enters into a tenancy agreement with a new person, advertises the unit or building for sale, demolishes the unit or the building, or takes any steps to convert the unit or building to a non-residential use, the landlord is presumed to have given notice in bad faith (RTA, ss. 57(5)). Conveyancing lawyers should ensure clients are aware of the associated penalties (RTA, ss. 57(3)) and any related timelines or prohibitions if the client is intending to occupy the property on or after closing.

There will soon be a standard lease applicable to most residential tenancies in Ontario. The impetus for this change is to decrease landlord-tenant disputes and bring Ontario in line with most other provinces. Landlords will still be free to negotiate and include additional clauses, but if these conflict with the legislation or the standard form, they will not be enforceable. Landlords will be required to provide the standard lease within 21 days of receiving a tenant's written request, after which the tenant can withhold a month's rent (RTA, ss. 12.1(6)). If the landlord does not provide the lease within 30 days, the tenant does not have to pay the withheld rent (RTA, ss. 12.1(9)). Lawyers would do well to notify their purchasing clients about this additional legal obligation and the potential associated financial burden. Lawyers who are asked to assist a client with a form of residential lease also need to be up-to-date on this requirement. The form, which can be found on the Ontario government's Central Forms Repository at forms.ssb.gov.on.ca, is mandatory for private residential leases signed on or after April 30, 2018 and applies to tenancies in single and semi-detached houses, apartment buildings, rented condominiums, and secondary units (e.g., basement apartments).

Time to update office systems and precedents

Conveyancing lawyers should use this change in the law as an opportunity to review and update any checklists or systems they may have in place for real estate files. Residential tenancies present unique complications for lawyers and landlords when compared to other types of residential real estate transactions. The possibility of financial success and a great return on investment are not typically elements of a solicitor's opinion, but when legislation directly affects the value and cash flow of a property, it is risky for the real estate bar to blithely assume that the impact of the statutory regime is beyond the scope of the purchase or mortgage retainer. It is important to be clear with clients from the start of a transaction about what can and cannot be assured as a part of the retainer. Real estate lawyers in the past have been on the frontlines when it comes to rent control and its impact on a wide range of residential properties – staying aware of any updates helps ensure your clients are receiving the best possible advice. ■

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