The Dark Side of Residential Landlording

Sample Chapters

Why This Book and What to Expect from It?

This book will be an invaluable guide to would-be and first-time investors, realtors unfamiliar with residential investment properties, and to aspiring neophyte property managers considering a career in managing residential rental investment properties.

Niccolo Machiavelli, author of *The Prince*, wrote, "A deceiver will always find someone willing to be deceived."

Thousands of books have been written on real estate investing. I've found perhaps a handful of books about the practical business challenges of being a residential landlord but I have yet to find one comprehensive book that scrapes away the gold and silver electroplating of guaranteed happy returns from "hands-off" passive real estate investing, to expose the rough copper base of what an investor must suffer to reap the pot of gold at the end of the real estate guru's painted rainbow. *The Dark Side of Residential Landlording* attempts to fill that void.

In case you missed the earlier disclaimer page, I'm not a lawyer or financial expert. Everything in this book is based on my own experiences and is, for the most part, self-learned.

Aside from uncommon risks that the average residential landlord may not be aware of, this book also includes myriad examples of deception, exploitation, deliberate and unintended abuse, and other assaults on residential landlords by a gallery of self-serving, self-righteous, self-absorbed, self-centred, tenant-pandering autocrats, automatons, rogues, scalawags, and ne'er-do-wells who undertake dirty, disgusting, distasteful, deceitful and sometimes even disturbing practices against unrepresented and uncoordinated residential who they believe are easy targets in order to further their hidden agendas, often at the residential landlord's expense.

After all, "landlords are rich" and all tenants are comparatively poor. This prejudicial misperception is so pervasive worldwide that there's a thread woven into the fabric of society that makes landlord-bashing socially acceptable behaviour. This prejudice is such a stumbling block in certain relationship arenas that I sign all of my residential rental business correspondences as a "Residential Housing Provider." I like to believe, probably naively, that it gives recipients pause to ask why I would sign it that way and to reflect on the role I provide, while distancing me from the malignant perception of a feudal tyrant imposing their unbridled will upon a powerless serf.

This book is not sensationalistic, a rant or filled with conspiracy theories although I do take literary license to accentuate points with rich and sometimes unflattering adjectives to emphasize a point.

If you deem a particular story inflammatory or sensationalistic, it is nevertheless my opinion of what I sincerely believe to be true to the best of my knowledge, backed by over 175 footnoted citations or otherwise a statement

that I'm in possession of the supporting evidence necessary to defend what I've said, especially if it's an accusation of malfeasance, deliberate intent to harm a landlord, or a conflict of interest.

It's entirely likely that you may not even know some of the entities I discuss who are bent on taking a piece of you as a residential landlord for one reason or another.

The above scope of the book is ambitious and I don't think I've covered everyone that might be out to abuse or exploit a residential landlord but hopefully you at least appreciate what it is that I'm trying to accomplish by writing this chronicle.

I leave the description of the rewards from the *business* of residential landlording to the thousands of gurus, pundits, realtors and other sages of investing who routinely push forward the bittersweet elixir of blissful passive income and worry-free operations.

This book is as much more about 'how to' as it is about 'watch out.' It speaks about the many entities competing to strip away small pieces of your hide. In less graphic terms it's really about identifying the risks you may have to face or undertake to become a successful residential landlord.

If you type into a Google online search the keywords words "risks of being a landlord" it returns with 11,600,000 results. That doesn't include synonyms for "risk" such as pitfalls, pros and cons, dangers, hazards, perils, liabilities, misfortunes, and more.

But I don't just leave you a map of where the minefields are. I also try, where possible, to provide you remedies and techniques for defusing some of those mines or at least how to minimize the number of body parts you'll lose if they explode near you.

Veteran landlords will be intimately familiar with some of the accounts, stories and experiences discussed in this book but I would hazard to say that even they will not have run into everything that you'll read here.

We each have strengths that serve us well. Our personalities, values, moral compass and other factors help us to capitalize on those strengths. Your strengths and mine will be different. Therefore, my problem solving and management style may be different from yours. It's possible you might handle a particular situation quite differently than I did.

One might even argue that I'm too black-and-white. However, I don't believe the last point is true. I teach in my course that there's a thick grey line between doing all the things that every legislative entity and policy maker tells you must be done which I'm convinced substantially increases your risk of bankruptcy, versus operating at odds with society and perhaps technically even outside the law, which can put you in the company of slumlords, without a doubt a person highly deserving of society's contempt.

What I can assure you of is that you'll learn things that you didn't know … you didn't know. You may wonder why some of these policies, legislation, by-laws, judicial processes and other government constructs would be inflicted

upon good-intentioned and socially-responsible people. Landlords by and large are willing to assume extraordinary financial and legal risks to provide safe, reliable, comfortable and healthy housing for people who can't afford, or choose not, to purchase their own home, in exchange for a payment that generates a reasonable profit.

This Book's Applicability to Other Geographies

The exploitation of, and resentment towards, residential landlords seems to be fairly universal and for as long as anyone can remember.

Every geography and jurisdiction has its own flavour of tenancy laws and associated problems. While this book generally speaks to the issues I've experienced as a residential landlord in the province of Ontario (so much so that I call our province Ontari-oh-oh!), Canada, arguably one of the most heavily regulated, tenant-biased geographies in the western world, variations on many of the topics and issues discussed in this book can be found everywhere.

I've watched many television programs, read newspaper articles and even visited different geographies—from London, U.K., Mumbai, India, and Geneva, Switzerland to San Francisco, USA and Vancouver, Canada. They all seem to carry an almost universal thread of an "us-versus-them" mindset of residential landlords being hung out to dry by all manner of other parties in those geographies.

I can't speak or read any other language but I'd wager that most of the threats, risks and experiences presented in this book are universally mirrored throughout the western world.

A specific unjust law (and there are many) that I discuss in this book may be municipal, provincial or federal, and they may not apply where you live. Nevertheless, I'm absolutely certain that your own investigations and research will discover equally unjust laws in your area. I believe much of this judicial injustice is equally universal and rooted in short-sighted politicians everywhere pandering for easy tenant votes and giving little thought to the consequences.

Use what I write here to encourage yourself to be proactive and do the research to find out what kinds of unjust residential landlording issues exist in your locale.

If you Love Pina-PIPEDA

In my experience with the landlord association, many smaller, and a few larger, residential landlords don't realize the obligations they have under PIPEDA, the *Personal Information Protection and Electronic Documents Act*.

PIPEDA is often confused with the *Freedom of Information and Protection of Privacy Act* since both address the protection of personal information. The *Privacy Act* is federal legislation that came into effect on July 1st, 1983. It sets out the rules for how *institutions of the Government of Canada* must deal with personal information of individuals.

PIPEDA became law on April 13th, 2000 and sets out the rules for how *private sector organizations* collect, use and disclose personal information in their commercial businesses as well as to facilitate the use of electronic documents and promote consumer trust in electronic commerce. The Act was significantly amended November 01, 2018.

The following is not an abuse by the federal government but you'll feel like someone reamed you if a tenant files a PIPEDA complaint and you learn the hard way that what you think should be reasonable and proper is anything but that.

Limited Time and Use of Information

Several key points directly affect residential landlords. You should already know that you must obtain a tenant's consent to collect, use or disclose the tenant's personal information. This might be implied by the act of a tenant filling out a rental application form but it would better if you had a statement specifically ("expressly") addressing the point.

You have to detail the reason(s) for collecting the tenant's personal information before collecting it and you can only ask for the limited information needed for what a reasonable person would consider appropriate to applying for a residential tenancy.

You can only use a tenant's personal information for the specific purpose(s) for which it was collected, which is typically to determine whether the applicant meets your qualification criteria for tenancy.

The following surprised me and I suspect it will surprise some of you too. Once the specified use is satisfied, for example, when the applicant has been accepted or declined, you must delete all of the collected information. That didn't sit well with me because I've often had to go back to the application form for information of one kind or another and for one reason or another. I always hold on to the tenant's information until about one year after the tenant has moved out. This is because I may be contacted by a next of kin, the police or even the tenant themselves for some kind of inquiry. But you can't hold on to the information that long unless you have the applicant's permission.

Calling the Second-Last Landlord

Many landlords preach, as I did at one time too, that your rental application should ask for the contact information of the current and prior landlord.

Business sense tells you that when you call the tenant's current landlord, they may not be completely honest with you, especially if they're trying to get rid of the tenant or they know that the problem tenant is having a difficult time finding another place to live.

Oh? You thought landlords stick together? I've met landlords and investors who see nothing wrong with foisting their problems onto someone else. In fact, some people take perverse pride in doing that, hence the phrase *caveat emptor*—buyer beware.

The prior or second-last landlord has nothing to lose and may be looking for a way to balance the scales of justice with a previously troublesome tenant. That landlord is very likely to tell you matter-of-factly whether a tenant was good or not.

You'd think this was a great way to minimize the chances that you'd inherit a tenant with a history of causing problems. It also seems only morally right that a tenant should be held accountable for their past actions and behaviour —what goes around, comes around. That same wisdom also says you should reciprocate the service to landlords who call you so that tenants become more cognizant of the consequences of their actions over the long term.

A "you-got-to-be-kidding" moment came when I learned that a previous landlord cannot provide a reference, especially a negative one, to a new landlord inquiring about a prospective tenant. Regardless of the tenant's behaviour, rent payment tardiness, or any other negative trait, PIPEDA says, "you can't shame a tenant."[1]

As the past landlord you must also have the tenant's permission to give that reference. Therefore, if a landlord calls you for a reference, you're required to obtain proof from that landlord that they have permission from the tenant to call you and ask about the tenant's past history. Otherwise you, who no longer have anything to do with the past tenant, could be held accountable by the tenant for speaking about their personal and private rental history without their permission.

Social Media Isn't Public Information… Whaaat!?

If the above was a surprise, then stand back because the following one may knock you off your feet. You know all that public information that's floating around on the Internet and posted on various social media by tenants for all to see? It's public information, right? Right; until you pull the information from various media and combine them. PIPEDA considers that to be compiling a

[1] https://www.priv.gc.ca/en/privacy-topics/landlords-and-tenants/02_05_d_66_tips/

profile of the tenant whereby assembling the information provides you additional "collective" information that you weren't given permission to know.

Protecting Tenant Data

PIPEDA requires all businesses, including landlords of every size, to ensure that a tenant's personal information is protected by appropriate safeguards including (a) physical measures such as locked filing cabinets, restricting access to offices, and alarm systems, (b) technological tools such as passwords, encryption and firewalls, and (c) organizational controls such as security clearances, limiting access on a need-to-know basis, agreements, staff training, and so on.

If you lose your phone or laptop with tenant information on it and, for example, a tenant can trace back their identity theft to you, you're going to be chewed up and spit out by the Office of the Privacy Commissioner of Canada (OPCC).

Taking Photos

Next surprise: what if you and a tenant had a verbal tenancy agreement, which is permitted under the RTA—I can't state strongly enough *not* to do this—where you allowed the tenant to grow up to four cannabis plants but then you discover the tenant has 60 plants? Can you take pictures of the plants to prove your case? When I asked this question of many smaller landlords, the answer was almost always no. Wrong again. For once the law seemed reasonable and made sense.

The OPCC website had such a case dated June 17th, 2014 (Report of Findings #2014-006).[2] The report cites, "In certain instances, however, individual knowledge and consent are not required. For example, under paragraph 7(1)(b), an organization may collect personal information without the knowledge or consent of the individual (i) if it is reasonable to expect that the collection with the knowledge or consent of the individual would compromise the availability or the accuracy of the information, and (ii) the collection is reasonable for the purposes related to investigating a breach of an agreement or a contravention of the laws of Canada or a province."

Be very careful with this section though. The OPCC keeps a very tight rein on this exception. "The precise circumstances of each situation should be analyzed beforehand to determine if paragraph 7(1)(b) is applicable to the situation. Certain conditions that remove the requirement of obtaining the consent of the individuals must first be met."[3]

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[2] https://www.priv.gc.ca/en/opc-actions-and-decisions/investigations/investigations-into-businesses/2014/pipeda-2014-006/

[3] ditto

What Else Can't You Do or Say?

Other things you should know about PIPEDA: you can't demand a tenant's Social Insurance Number (SIN), you can't use it in your accounting books for example as a tenant identifier among other things, and you definitely can't deny a tenancy applicant because they didn't give you their SIN number.

You should get every tenant's permission before you set up surveillance cameras in your building. Anything that captures a tenant's face may be a PIPEDA violation. However, implicit consent may be possible but I'm not a lawyer and that's beyond the scope of this book.

There are also specific rules for disclosing information to the police. If they show up and ask you for information about a current or past tenant, you're *not permitted* to give them that information unless they provide you with specific documentation that compels you under the law to do so or they declare it an emergency. Generally, a warrant is usually required or 24-hours' notice is given to the tenant. Strict rules apply.

Remedy: I significantly extended the Personal Information Consent clause in my Tenancy Application form and added a 6-paragraph clause to my Appendix B of Ontario's Standard Tenancy Agreement (STA).

The clause states that credit and reference checks, and other relevant investigations will be undertaken to determine a tenant's rental, court, criminal, credit, employment and financial histories as well as their ability to pay the rent. It includes the tenant's permission to use the information the tenant provided as well as the tenant's personal information collected from other sources *including social media websites* to obtain a consumer report, to contact employers, previous landlords, references as provided, and agencies that provide landlord information. I explain that the collected personal information will be used to determine the tenant's creditworthiness and suitability for the renting of the premises. It also allows me to *collect further personal information as I may require from time to time to enforce the terms, conditions, obligations and responsibilities of the tenant* for the duration of the Tenancy Agreement plus one year. I further require permission to pass on certain personal information of the tenant to third party service and utility providers.

Sewage Treatment

You should take the same high interest as a lender does in monitoring and controlling utility costs of your property, especially if any of the utilities are included in a tenant's rent, and again especially if the utility company is owned by a municipality.

Here are some of the ways some municipally-owned utility companies exploit and abuse residential landlords.

Water

Getting "Hosed" No. 1 - Water Meter Lease Only

The Regional Municipality of Durham (Ontario, Canada) forces every one of its customers to lease their water meter forever. They disguise this charge as a "Water Service Charge."

They claim that this charge also includes maintenance and related management fees but then what is the companion "Water Consumption" fee for?

When have you ever had a maintenance call on a water meter? Being semi-mechanical they can start to lose a bit of accuracy over time. An article in "Water & Wastes Digest" magazine[4] reported a detailed actuarial study that computed accuracy loss. A 16 year-old water meter was estimated to be 0.992 accurate and only then was the meter replacement economically justified based on the difference in cost of lost water income from inaccurate water flow metering and the cost of buying and installing a new water meter.

Other studies I found had some replacement estimates as low as 10 years.

I have purchased water meters for about $425 each. Parry Sound in Ontario requires each customer to buy their water meter, then have it installed by a certified plumber, and then have the town's water operator inspect it.[5] The purchase prices of different meters range from $462 to $1,240.[6]

By example then, the average lease cost of a 1.5" (38 mm) meter is about $160/month or $960/year (billed bi-monthly). The meters may cost Durham Water maybe $1,500 including installation in the most conservative case. Maintenance costs are next to zero for the next 10 to 15 years. Water treatment and delivery costs are a separate line item on the bill.

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[4] https://www.wwdmag.com/meters/determining-economical-optimum-life-residential-water-meters

[5] https://www.parrysound.ca/en/live-here/water-meters.asp

[6] https://www.parrysound.ca/en/live-here/resources/2019-Water-Meter-Price-List-with-Town-Admin-Fees.pdf

Durham Water will drain from my pockets $9,600 over the next 10 years or $14,400 over the next 15 years, all for making a $1,500 investment that they denied me the right to make myself.

And that's without factoring in annual increases. I reviewed all my electricity and water bills when I evaluated whether to install separate hot water tanks in every rental unit. My Durham Water bills increased 45% over a five-year period. So roughly speaking, divide the numbers I gave you above and add it to those same numbers, that is, $14,400 and $21,600 respectively.

According to a 2018 Information Report[7] published by Durham Region based on 2016 census data, there were 184,965 owner households in Durham and 42,930 renter households. My bills were based on a 11-plex apartment building but just doing a "sanity check" calculation: assume each household is 1/10th of my billing (but probably higher) and average out my lifespan "siphoned" amount above ($14,400 and $21,600) at $18,000 so a household might be drained $1,800 over the same period. Now multiply that by 228,000 combined renter and owner households (I had to get another calculator with a larger display) = $410,000,000,000.

Talk about being hosed!! This is just the forced-leasing portion. If that's not a monopolistic anti-competition case I don't know what is.

Remedy: There is none. It's a government monopoly and every customer is paying a massive surcharge. I filed a formal complaint with the federal Competition Bureau. They replied, "The Bureau takes all allegations of anti-competitive conduct and deceptive marketing practices seriously. The information you have provided will be recorded and entered into our database and it may be used to develop or support future enforcement activities under the laws we enforce. As a law enforcement agency, the Bureau is required to conduct its work in private. A Bureau representative may contact you if further information is needed." No one's ever contacted me.

Getting "Hosed" No. 2 - Size Matters

The same Durham Water agency installed an oversized meter in one of my buildings and charged a substantially higher fee for the oversized meter.

How did I know this? When I purchased my fifth property, an 11-plex, I received bills with the same murky water service charge, which ranged from $110 to about $180 for a 38 mm (1.5") sized meter, referring to the diameter of the water pipe entering the building.

I compared the bill to another 11-plex property that I owned literally kitty-corner to the first; same size building, number of units, area, etc. The second

[7] https://www.durham.ca/en/living-here/resources/Documents/2018-INFO-53-2016-Census-of-Population.pdf

building had a 25 mm (1") meter and the water service charge was in the $75 to $80 range.

However, the second building had some time earlier been the subject of a running toilet, as I later discovered after investigating a literal doubling of the dollar amount and cubic metres of water consumed from one bill to the next. The second property's meter was able to handle double the flow-through capacity without an issue so why was the larger meter required in the first building?

The difference in cost between a 1" (25 mm) and a 1.5" (38 mm) meter was roughly $85 every two months = $510/year.

There's no way to know what percentage of buildings in Durham have oversized meters installed in them so there's no way to estimate the potentially fraudulent or at the very least grossly negligent overcharges.

However, I think it's safe to say that if this practice was done to me than it's almost certainly been done to other businesses, and apartment buildings would be an ideal target since landlords generally wouldn't dissect an invoice like this or be in a position to do an apples-to-apples comparison.

"Wait … what're saying? I'm some kind of bean-countin' nerd with nothing better to do than look for penny savings wherever I can find them?"

Well, yeah, maybe I am a paranoid schizophrenic conspiracy nut-job looking for every act of abuse, exploitation, mismanagement, misconduct and perhaps even corruption I can find.

You'll have a better answer after reading this book and determining for yourself whether you've validated or experienced anything I've written.

Remedy: You can do something about this issue if you can prove in some way that it exists and you know what to ask for.

When I called Durham Water and explained the discrepancy, they took a month or two to investigate the issue. I had to follow up a couple of times (like that's a surprise for a government monopoly).

Eventually, they offered the proper-sized smaller meter but I had to have a licensed plumber install it (about $850) and they then had to certify the installation. Given that it was their "mistake" and that I had been overcharged for as long as I owned the property I figured they should have paid for the installation and reimbursed me for the overages but their reply was a diplomatic variation of "take it or leave it."

It took about four months for the new charge to take effect but they did adjust the water service charge back to the date of the certification of the new meter.

The question remains though, how many other customers have been the victim of this hidden overcharge that will run in perpetuity?

Here's a side note tip: modern water meters have a little red arrow that moves when water flows throw the meter. Arrange with your tenants to turn off all faucets and to not use the shower or toilet for a few minutes. If the

triangle is still moving after everything is turned off then you have a running toilet, dripping faucet or possibly a water leak somewhere that hasn't shown itself yet.

Getting "Hosed" No. 3 – Landlords Held Accountable for Tenant Arrears

Many municipally-owned utility companies deliberately exploit an unintended loophole in the Municipal Act that permits an uncollected water bill to be added to a landlord's property tax bill.

The original intention of the clause was to ensure that the water bill is paid by you as the existing property owner before you sell the property.

However, municipal utility companies have perverted the good intention of the legislation by applying any water bill arrears to the property tax even if the landlord's tenancy agreement explicitly states that the tenant pays the bill.

Municipal water companies don't allow a property owner to transfer the responsibility to pay the water bill to anyone other than another property owner. When I asked my water company why they think this is a fair practice, they replied that it's just their policy—more extortionist rot.

Landlords are easier to collect from and they'll have the money, even if the landlord didn't create the water bill and even if the landlord did everything right to ensure that the tenant wrote a binding utility payment agreement.

If you refuse to pay the water bill arrears, the municipality shrugs its shoulders with their proverbial, condescending, "We … don't … care" message and promptly sends the arrears to the property tax department to be added to your next property tax bill.

The worst part is that you may not learn that the water bill is delinquent for many months or until you get a whopping surcharge on your property tax bill.

If you don't pay the property tax bill, the municipality will take you to court. You'll likely lose and you'll likely pay a substantial delinquency charge.

The whole situation is a sham and a scam. No other utility companies do this and it's downright unethical. Yet, here we are with the law on "their" side.

No e-Billing Old-school Time-waster

This is petty abuse but still makes it into this book because only a government monopoly would not have implemented e-billing as we enter the third decade of the 21st century.

Out of the estimated 40 or more different bills I pay every month and the several annual bills, there are still two bills that I still receive in snail mail; the Regional Municipality of Durham water and sanitary sewer bill and the Oshawa municipal property tax bill. Every other bill of every kind offers me paperless e-billing.

This is what you get when a municipality, or just about any level of government, has a monopoly—no incentive to save trees or money, reduce

bureaucracy or improve service levels. Here we are into the third decade of the 21st century and still these government agencies haven't discovered, but more likely don't care about, what everyone else already knows: they'd save oodles of the taxpayers' money or in this case perhaps reduce operating costs and pass some of that savings back to their customers.

Remedy: As an individual there's not much you can do. A citizen's affirmative action committee or some similar grassroots movement might make some progress but residential landlords probably don't have the time for something that's so obvious that should have been done a decade ago.

Getting Gas is Good, Ain't It?

It's fairly common knowledge that heating a building with gas is usually significantly more cost effective at the net operating income level than heating with electric baseboards, although electric furnaces have many positive attributes.

Compared to gas, an electric furnace is more efficient, cheaper to purchase, install and fix, doesn't require a special fuel line source, generally easier to repair, arguably runs more quietly, and doesn't emit carbon monoxide (CO) (the odourless killer). Then add in the cost of purchasing and maintaining CO detectors in each rental unit.

Electric furnaces can reach about 98.5% efficiency while current gas furnaces never reach that level of efficiency since some energy is always lost through the chimney flue.

Here's the inevitable "however." Just because an electric furnace is more efficient doesn't mean it's cheaper to operate. In fact, in Ontario it's not.

Natural gas-fired furnaces generally take less time to reach target temperatures than their electric counterparts, so gas furnaces generally require less fuel to operate.

So why wouldn't you convert all your electric baseboard heat to gas?

You may think the cost is prohibitive but if that $50,000 conversion of a 15-unit rental property results in a $4,000/year reduction in your overall heating costs that would add $80,000 to the value of your property. If you factor in the exponential rising costs of utilities then the returns become even more persuasive. I discussed how suite metering electricity added about $200,000 to the value of one of my properties.

The simple answer is that if the tenant is paying for the electrical heat then there's probably little upside for you.

Notwithstanding that though, if all your rents included electricity, and you decided for some reason to keep it that way, you now face a serious financial decision.

Previous Owners

One could argue that it's the human condition or at least an implied understanding of the rules of free trade, that a seller will rarely own up to any shortcomings if there are no legal consequences to any defect in whatever it is they're selling, while extolling the virtues of the thing being sold.

The premise of *caveat emptor* or buyer beware has long been the warning of master tradesmen to their apprentices but real progress has been made in developing ethical standards in business and trade. Ontario's Sale of Goods Act (1990) has taken great steps to reduce the consequences of caveat emptor in consumer products.

However, the doctrine of caveat emptor still plays a significant role in real estate transactions. Particularly hot topics involving caveat emptor include stigmatisms and defects. Various provincial high courts have developed clear distinctions between patent and latent defects.

Stigmatisms have traditionally not been disclosed in real estate although, again, the regulatory authorities in particular have adopted the position that anything that affects whether an offer is made or affects the price of the offer must be disclosed. They preach, "When in doubt, disclose."

Buying real estate is still a minefield of anti-personnel *caveat emptor* mines ready to blow up in your face. In short, it's highly likely that you will inherit the previous landlord's problems.

You need to find out what they are as part of your due diligence. The seller's unlikely to tell you about any shortcomings unless the law forces them to. Even then, the law and its punishments don't seem to be enough of a deterrent. For example, out of the 1,336 claims reported in 2018 to the Real Estate Council of Ontario's (RECO) real estate insurance program, 800 (59.9%) involved miscommunication or non-disclosure.[8]

After discovering the previous owner's undisclosed problems, you may have legal recourse but you'll still end up financing the repairs until you can collect, if you can collect, when you can collect, and after knocking off a couple of years of your life and maybe losing a spouse or friend in the process.

Misrepresented Tenant Rents

I purchased a property where I later came to believe a fraud had being perpetrated. I was counseled by my lender and lawyer that the following situation might be found after I bought the property.

The property owner wanted to sell a property that they had found challenging to rent up. The owner was not a competent operator and looked for every shortcut to save a penny, irrespective of what it cost to save that

[8] https://www.reco.on.ca/wp-content/uploads/RECO-Annual-Report-2018-vF-web.pdf

penny. The owner created a nightmare of bad tenancies because they didn't do any tenant screening so they were have a difficult time attracting quality tenants to the building.

In such a situation an owner might be tempted to make deals with new tenants to sign bogus rental agreements about when they moved in and how much rent they paid.

Tenant applicants were told that the owner was trying to sell the apartment building. The owner offered applicants a one-bedroom rental unit for $750/month provided the applicant signed a tenancy agreement that stated the lawful rent was $1,100/month, and that the tenant paid cash for their rent.

Even the tenant confirmation letters we sent out to each tenant to confirm their rent amount (among other things) would have to be completed by the tenants with the false rent amounts.

Once the property was sold, the tenant had to pay the new landlord $1,100/month rent going forward or provide immediate notice to move out.

To appear legitimate the owner would have had to permit the Last Month Rent (LMR) deposits to appear on the closing statement of adjustments so, for example, if they reported LMR of $1,100 per unit for 3 units but actually only collected $750, they had to pay $1,050 ($1,1,00 - $750 = $350 x 3 units) extra to perpetuate the fraud.

But this is a one-time "cost" to strengthen the fraud whereas they were adding $1,050/month x 12 months = $12,600/year to the NOI. At a 5 cap, $1 of NOI = $20 of joy so capitalizing the $12,600 NOI added $252,000 of inflated value to the property.

Immediately after I closed on the property, three tenants gave notice. All of them were at the highest rent rate. Two more vacated soon after but they were in the $750 to $800 range.

I also went through the most brutal tenant eviction process in my landlording experience up to that time. At one point I had six vacancies out of 25 units within six months.

Remedy: You might be asking why I would have allowed myself to be potentially swindled by the owner, even after being cautioned by my advisors.

More importantly, why would the lender still advance me the financing if they thought there was the potential for a steep drop in the income, notwithstanding that I was providing a personal guarantee in any event?

The lender knew as well as me that finding income-producing properties at a price that can be financed was an increasingly uncommon event in Ontario.

I analyzed and assessed the risk. In a perfect world of all at-market rents, I'd have an additional $57,500 NOI. I felt I could bring 50% of that below-market rent up to market rates within the five-year term of the mortgage adding about $28,750 "real" NOI.

All the tenants have electricity included in the rent, which is a yearly operational expense of about $30,500. If I suite-metered the units and

converted one-third of the tenants through turnover to pay their own electricity within the same five years, I'd add $10,170 NOI.

The hot water tanks and boiler were leased at about $310/month = $3,720/year.

The above three actions alone would add $41,640 NOI. At a 5.5% cap rate, that equaled $757,000 in property value. And that was before realizing the benefits of other identified cost saving and revenue enhancing measures.

So, yes, I might be potentially overpaying for the property by $250,000 but within five years, I would recover that "loss" and add $500,000 to the value of the property. And that was a conservative case, which I also demonstrated to my lender.

The only other major concern was under what conditions might the unit cash flow negative? In other words, how much money could the property afford to lose monthly and still meet all of its operational costs and financing obligations (called the breakeven ratio or BER)? I was able to show that we could temporarily withstand the loss of income from seven current units for a few months. With vacancy rates below 0.5% in most Ontario municipalities, we were confident that we wouldn't have vacancies for very long, even if it meant getting less than our target market rent.

There was always the option as well that, if we gathered evidence from the tenants who participated in the con in exchange for not pressing charges[9] or providing some other benefit, we could file a court action against the owner.

Hiding Defects

In December 2014, I won an Ontario Small Claims Court (SCC) judgment against a seller who had not disclosed a defect that had repeatedly occurred over many years prior to him selling the property to me, and despite a specific clause in my Agreement of Purchase and Sale (APS).

Tenants had earlier reported substantial deterioration of in-suite walls, which bubbled because water had entered into the plaster walls and swelled.

I also observed sometime after purchasing the property several areas of uncharacteristic white stains on the external brick walls.

As water moves through brick, it picks up salt in the mortar that didn't bind with the brick. The salty water that evaporates at the brick's surface leaves behind a white flakey-looking deposit called "efflorescence."

Specialists I hired determined that the cause was condensation forming between the walls, a problem common with buildings built before vapour barriers were mandated in the Building Code. I then learned from a long-term tenant that the wall problems were a regularly recurring event. The tenant swore an affidavit that was admitted into evidence in the trial.

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[9] I'm not sure if this is legal in Canada since fraud is a criminal action and the Crown prosecutes all criminal trials.

The Agreement of Purchase and Sale (APS) included a clause, "The Seller states that, to the best of the Seller's knowledge and belief, there is no known damage to the basement, roof, or elsewhere in or on the property caused by water seepage or flooding."

The Ontario Limitations Act (2002) generally adheres to the premise of caveat emptor or "buyer beware." A buyer can only file a claim of defect within two years from the date of purchase, with generally no recourse after that.

However, the Act differentiates between two types of defects.

A patent defect is one that can be discovered by observation ("obviousness") or inspection using generally accepted industry-standard practices.

A latent defect is one that is present but is not obvious, visible, apparent or actualized and can't be discovered by industry-standard inspection practices.

A seller has no obligation to disclose a defect that's obvious, such as a clearly-visible water-soaked crack in a foundation wall.

The buyer must also be able to prove that the seller knew about the latent defect. This is usually the most difficult nut to crack in a latent defect case. If the defect is proved to have existed prior to selling the property but the seller didn't know about it (perhaps the defect didn't appear while the seller owned the property), then the seller can't be held liable, even innocently.

In my case, my tenant's affidavit substantially strengthened my case. The judge determined the seller knew, or ought to have known, that there was recurring water damage caused by an untreated defect in the property. The judge stated he "… sympathized with the Defendant …" but the Defendant clearly breached the "no water damage" clause in the fully-executed APS.

SCC can't award punitive damages, and "betterment" costs are excluded, that is, repairs that improved the property. For example, if the original roof was 10 years old with a 20-year life expectancy, the court might rule that the buyer received a betterment of 10 years and then award only half the new roof's cost. I was also not permitted to recover my personal expenses related to attending meetings, overseeing repairs, travel etc. Presumably this is because the value of one's time is highly subjective and would inevitably be contested. It could also be a source of considerable abuse in inflating costs.

There are several cases in law regarding the responsibility to disclose material facts: McGrath v. MacLean (1979), Krawchuck v. Scherbak (2011), and Dennis v. Gray (2011).

In Krawchuck v. Scherbak, the real estate agent was found to be 50% at fault for their lack of diligence in reconciling misleading statements made by their client, failing to inform their client of the implications of their false statements, and failing to bring these issues to the attention of the purchaser.

In a decision released in May 2014, a deputy Judge of the Barrie (Ontario) Small Claims Court said in his judgement that a seller must disclose to the buyer anything they know about a defect that has caused any loss of use or enjoyment of a meaningful part of the premises.

Since the case of McLean v. MacGrath, and in light of Dennis v. Gray, the principle of *caveat emptor* appears to be either becoming more specifically defined or more exceptions are occurring. The evolving principle appears to be that if a seller properly discloses an actual or perceived defect in a property, then this should protect them from the risk of litigation and the accusation that the seller didn't comply with their duty to disclose.

Perhaps this will mean the seller has to provide a price discount or perhaps it will lead to sellers pricing their properties as they should have been in the first place. Either way, it'll still likely be less expensive that settling a court action.

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