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Market Rent Reports for Secondary Units



Appraisal Institute of Canada

Presentation Outline

- Background
- Legal vs illegal
- AIC's position
- Inspections
- What if...scenarios
- What CAN Members do?
- Q&A



Why are market rents popular?

- OSFI increases the mortgage “stress tests” for lenders in 2018
- OSFI now considering even more stress tests (LTI, DTI, DSC)
- Passing stress tests means getting a loan or lower interest rates
- Rental income is included in the test
- OSFI expects FRFIs (regulated lenders) to exercise due diligence and “rigorous” efforts to verify income by an independent source (including Members) especially for investment properties
- If a borrower has no leases, proof of income from a T1, T4, T776, Notice of Assessment, financial statements or if the rent is questionable, “market rent” is used

What are lenders saying?

- OSFI regulated lenders at a senior level say they do not want “illegal” rents
- May not be entirely the case on the front lines

What does “illegal” mean?

- “illegal” or “unauthorized”, “not permitted” have similar meaning
- “illegal” means not allowed under zoning or approved by municipality
- basement suite or apartments most common, but includes garden suites, carriage homes, laneway, accessory dwellings, etc.

What is AIC’s position?

- “illegal” market rents should NOT be provided
- Insurance policy does NOT cover wilful violation of any law, statute, ordinance, rule or regulation, rules, by-laws, regulations and CUSPAP
- Members and Consumers can file complaints (Complaint Resolution Process)

Why?

- Unless a property is new, borrowers provide proof of rental income and can demonstrate ability to pay to the lender
- Some borrowers hope to beat the stress test by using market rent to maximize or even misrepresent income
- AIC's role is to protect the public interest within the lending industry, not directly help borrowers qualify for mortgages or beat a stress test
- AIC Members are the eyes and ears of and can't be seen to assume an income stream from a legal suite when a suite is illegal or even unsafe
- Market Rents should not be a workaround to pass OSFI Principles of income verification unless a property is new construction

Where is the harm of "illegal" suites?

Living in an illegal basement suite? Here's how to spot and report them in Calgary



This Calgarian is afraid others will turn to illegal suites in tight rental market

 Karina Zapata - CBC News

Posted: January 06, 2023
Last Updated: January 06, 2023

OSFI launches public consultation on guideline B-20: Underwriting Practices and Procedures

News release
For immediate release

OTTAWA – January 12, 2023 – Office of the Superintendent of Financial Institutions

News / Local News

Some Grey councillors wary of secondary units as tool to add housing

Rob Gowan

Published Feb 10, 2023 • Last updated 23 hours ago • 5 minute read

VANCOUVER | News

Surrey homeowners fined for continuing to rent out illegal suites despite court order

Homeowners in Surrey who turned a single-family home into an "unauthorized and unpermitted" four-plex could be on the hook for as much as \$19,000 after defying a court order telling them to stop renting out the suites, a judge has ruled. He also agreed with the City of Surrey that there are potential safety consequences to flouting building codes and the permitting process – even if these particular suites did not present any immediate danger. "The practice of offering unlawful suites for rent and inviting members of the public to occupy uninspected buildings without occupancy permits to my mind poses at least a theoretical risk to the health and safety of the community," he wrote. ... "To think otherwise would render the municipal building and occupancy bylaws meaningless."

Landlords fined \$89K for fatal basement fire

Marketplace | MARKETPLACE

Mortgage fraud caught on camera: Undercover Investigation



More on our investigation

CBC News

Posted: October 14, 2022

Last Updated: October 17, 2022

Mortgage fraud is a growing problem, according to Carl Davies, head of fraud and identity at Equifax Canada. The credit bureau flags between 15,000 and 24,000 suspicious mortgage applications each month, for lenders.

"Sixty-seven per cent of the applications that we find, or are tagged by our members as fraudulent, are actually related to that kind of misrepresentation," he said. "It's by far and away the biggest indicator of fraud or biggest risk of fraud we see in that space today."

Ontario real estate regulator ineffective at protecting homebuyers, sellers, audit finds



RECO 'not delivering on its mandate by a long shot,' says expert



Tiffany Foxcroft - CBC News · Posted: Dec 08, 2022 3:40 PM CST | Last Updated: December 9, 2022

Rental registry bylaw passes first reading at council

The proposed bylaw would require all rental housing units in HRM to be registered by April 1, 2024



Meghan Groff

Jan 25, 2023 5:45 PM



Halifax South Downtown Councillor Wayne Mason said this is about making sure buildings are meeting minimum standards.

"We've had people jacking up buildings without a permit, putting in an illegal basement suite, not putting fire-rated drywall, not being worried about having a secondary egress so if the place is on fire, people can get out," Mason said.

"This is a real and present danger. These things actually are happening in our community."

Steps to check if “legal”

3 important steps

1. Check if Zoning allows suites. If no, no market rent.
2. Inspect for self-contained suite. If not, no market rent.
3. Contact municipality for permit.

Some municipalities have an online registry for legal suites.

Ask the owner - many owners, investors or borrowers know if a suite has an application or approved permit

Advise the Client/AMC more time is needed for market rents.

If unable to confirm if a building permit is pending/approved from a municipality in a reasonable time, note steps in your report and include an EA



Inspecting a suite

- An inspection is required by CUSPAP
- Members must take steps to confirm the suite
 - actually exists
 - has own kitchen, bathroom, living, sleeping area, separate access, etc.
- Members are NOT expected to inspect for building code compliance (measure window sizes, firewall, test smoke/CO² detectors or all occupancy, health, safety, fire, electrical codes)

Looking to create a secondary suite in your home?



Long-term rentals are a great way to earn extra income while helping to provide additional housing for the people of Vancouver.

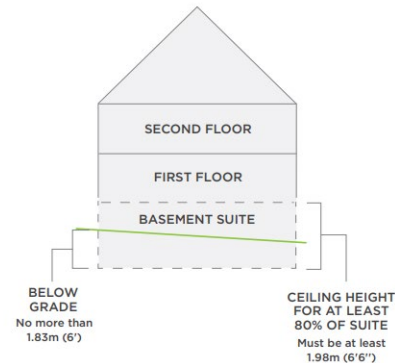
This guide provides information on how to obtain the permits you need to either create a new suite in your existing house, or ensure an existing suite that wasn't previously permitted or inspected by the City is suitable to be lived in.

STEP 1

To either rent out or allow someone (such as family or friends) to live in your suite, it must;

- Have a floor area of at least 37m² (400ft²) (but it cannot be bigger than the main part of the house).
- Have a minimum ceiling height of 1.98m (6'6") in all exit routes and in 80% of the suite.
- Be no more than 1.83m (6') below ground.
- Have a 900mm (3') wide, hard surface, unobstructed emergency responder access path from the street to the suite entrance.

Note: Anything that sticks out over this access path (such as a bay window or a chimney) must be at least 1.98m (6'6") above it to create sufficient headroom clearance.



Note: Only one suite is allowed per primary dwelling unit.

What if...?

- What if the Zoning is unknown or unclear?
 - Most zoning bylaws are available online
 - If zoning is mixed, unclear or unknown, contact the municipality
 - If uncertain, considering declining market rents
- What if Provincial legislation overrides municipal zoning?
 - Typically new provincial rules allowing more suites is for new construction, in-fill and on a go-forward basis
 - Explain in the Land Use Controls and HBU section
 - Suites must still meet building codes (occupancy, health and safety, fire, electrical standards)
 - Member must still follow steps 2 (inspection) and 3 (building permit)

What if...?

- What if a municipality has a service or registration fee – is it legal?
 - No, municipalities can charge extra utility fees for “illegal” suites
 - Not necessarily legal or in compliance with any municipal bylaws or code
 - Confirm whether a registry is “approved/legal” suites or only for fee reasons
- What if a municipality does nothing about “illegal” suites?
 - No enforcement does not make it legal
 - Many municipalities respond on a complaint system, may result in:
 - No action
 - Compliance officer inspection
 - Remove or legalize the suite
 - Fines
 - Signing declaration that the suite is or will not be occupied

What if...?

- What if the zoning does not allow a garden suite/carriage/laneway or accessory dwelling?
 - No market rent unless Province has overridden
- What if the market rent is for proposed/new construction with suites?
 - Plans must show suite
 - Invoke Hypothetical
- What if the municipality refuses or takes too long to respond?
 - Give clients/amcs advance notice that market rents take time
 - Request more time
 - Note steps taken within the report
 - EA must be included

What CAN I provide?

- Actual contract or reported rent, not market rent and not a market rent assignment (see PN 4.13.5)
- Hypothetical Market Rent only for proposed construction allowed by zoning and plans show secondary suite details
- Market Rent if the property is actively going through a rezoning, variance and permitting process – change should be imminent, not years (see CUSPAP 9.3.2.)
- Market Rent if all 3 steps are completed and unable to wait for confirmation from municipality about the permit

Resources

- Practice Notes 4.13

- 4.13.3 The only basis for valuation under an existing illegal use would be where a variance to existing land use controls could reasonably be expected, thereby resulting in either a conforming or legal non-conforming use.
- 4.13.4 Providing an analysis of market rent for an illegal suite is contrary to CUSPAP and may invalidate a member's insurance coverage.
- 4.13.5 A Member may note what rent the illegal suite currently receives.
- 4.13.5.i.** This is not an opinion of market rent, but a note of the suite's factual current rent.
- 4.13.6 If the Member disregards the illegal improvements, the appraisal will have to be premised on the Hypothetical Condition that the illegal improvements do not exist when in fact they do.

Resources

- Market Rent FAQs

17. Market Rent Report FAQs ^

1. Can I complete a Market Rent Report on an illegal suite?

Members are reminded that providing an analysis of market rent for an illegal suite is contrary to CUSPAP and will invalidate a member's insurance coverage.

2. Do I have to inspect the suite?

Yes, CUSPAP requires an inspection. If a complete personal interior inspection is not possible, a Member should discuss this with the Client, modify the Scope, provide an explanation in the report and invoke a limiting condition.

Any reason not to inspect must meet the Reasonable Appraiser test.

3. Can I use "legal" suite rents as comparables for "illegal" suites?

No, "illegal" suites should normally not be appraised as they do not meet the legal permissibility test. It is also not acceptable practice to compare apples (illegal suites) and oranges (legal suites).

4. If Zoning allows a suite, can I complete a market rent?

Checking the Zoning By-law is only one of the steps – the Member must also research rental data, inspect the property and should confirm whether the suite meets building code by checking with the municipality if a building permit exists.

A property's zoning can also change or a variance or exception is granted to allow suites. Normally the property owner or the municipality will have a copy of this change.

5. The property owner says the suite is legal, is that sufficient?

If the owner can provide a copy of the building permit to show the suite is authorized, that is sufficient.

The appraiser must indicate how this information was obtained and include assumptions and limiting conditions relating to reliance on this information in the report. If the owner does not have a copy, the Member should contact the municipality authority to confirm.

6. If the Zoning By-Law does not allow suites, but the property has a zoning variance or exemption can I complete a market rent?

Yes, if a suite is a legal non-conforming use, market rent can be completed provided all other steps are followed.

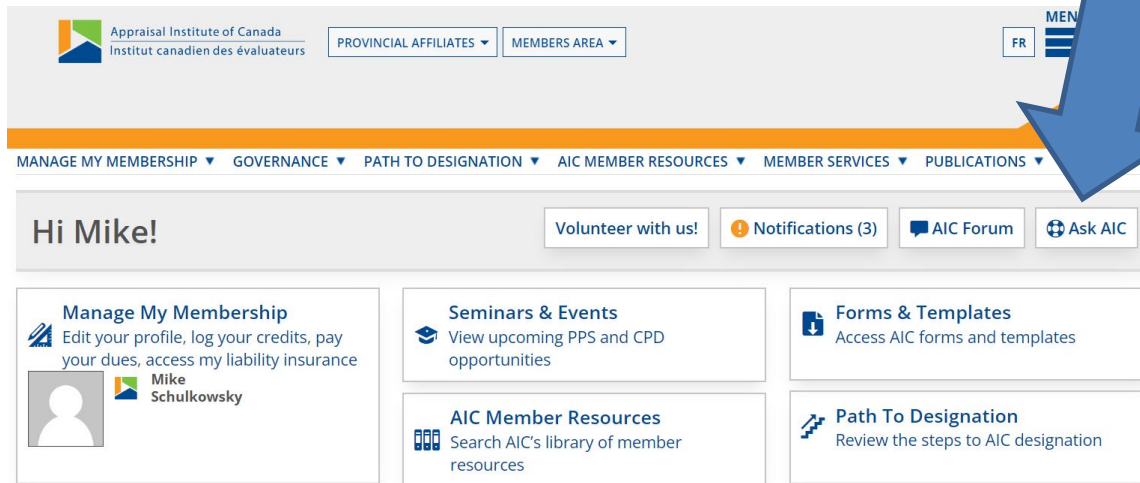


Resources

- Lum Library “Market Rent and Highest and Best Use: Joined at the Hip?” (The Appraisal Journal 2022)
- Knowing when to say NO (CPV)
- UBC Sauder
 - CPD 106 Multi-Family Property Valuation
 - CPD 109 Lease Analysis
 - CPD 110 Real Estate Consulting
 - CPD 124 Residential Appraisal: Challenges and Opportunities
 - CPD 132 More than Just Form-Filling
 - BUSI 352 Case Studies in Residential Appraisal
 - BUSI 425 Land Use Regulation

Q&A

For questions anytime, please use
ASK AIC ticketing system



The screenshot shows the AIC Canada website interface. At the top left is the logo for the Appraisal Institute of Canada (Institut canadien des évaluateurs). To the right are dropdown menus for 'PROVINCIAL AFFILIATES' and 'MEMBERS AREA'. Further right are language options for 'FR' and 'EN'. Below this is a navigation bar with links: 'MANAGE MY MEMBERSHIP', 'GOVERNANCE', 'PATH TO DESIGNATION', 'AIC MEMBER RESOURCES', 'MEMBER SERVICES', and 'PUBLICATIONS'. A personalized greeting 'Hi Mike!' is displayed, followed by buttons for 'Volunteer with us!', 'Notifications (3)', 'AIC Forum', and 'Ask AIC'. A large blue arrow points to the 'Ask AIC' button. Below the greeting are several service tiles: 'Manage My Membership' (with a user profile for Mike Schulkowsky), 'Seminars & Events', 'Forms & Templates', 'AIC Member Resources', and 'Path To Designation'.

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