Crunch point for London council housing finances

LONDON COUNCILS

Key points:

- Boroughs' council housing finances are under immense and growing pressure at a time when there is a desperate need for investment to improve housing conditions and deliver the 88,000 homes needed every year in London.
- Current social rent policy is failing to deliver the funding London boroughs require. Boroughs face a 'black hole' of £700m in their council housing finances between 2023/24 and 2027/28. Five boroughs could completely exhaust their reserves before 2027/28.
- London boroughs will need to reduce their council housing spending by £264m in real terms over the next three years to avoid their Housing Revenue Accounts going bust.
- London boroughs are calling for urgent action at a national policy level, including a reintroduction of a rent convergence policy to help restore fairness and stability to council housing finances.
- Failure to reform the social rent settlement will have dire consequences for boroughs' ability to deliver the safe, decent and affordable homes London's communities need. Without action to restore HRAs to a healthier position, boroughs fear the collapse of their council housing finances.

The importance of London council housing

London boroughs are proud social landlords. There are over 700,000 social rented homes in London – accounting for 20% of the capital's 3,671,000 homes. London local authorities own and let around 390,000 of those social homes – housing more than one in 10 London households – and have a crucial role as providers of social housing in the capital.

Social housing is a fundamental factor in the capital's success. Through ensuring secure, affordable homes for Londoners on low incomes, social housing helps tackle inequalities. With one in 50 Londoners living in temporary accommodation and record numbers on social housing waiting lists, expanding the provision of social housing is critical for addressing London's homelessness emergency. Recent research produced for a coalition of partners, including London Councils, also highlights the importance of housing affordability in promoting stronger and inclusive economic growth.

As well as wanting to deliver new homes for social rent, boroughs are determined to raise standards in their existing social housing stock. Too many social homes are in inadequate condition and boroughs know their tenants deserve better. Improving building safety and making faster progress towards net zero goals are also priorities for London local authority landlords.

This work requires significant investment. However, the cumulative impact of various government policy decisions over recent decades and challenging structural conditions mean that boroughs' social housing finances are under extreme pressure – with the situation deteriorating rapidly.

Council housing finances are being pushed to the brink in London

Of the 33 local authorities in the capital, 29 own social housing stock. These stock-owning councils each have a Housing Revenue Account (HRA) through which all income and spending related to council housing must be managed. HRAs are mandated by the 1989 Local Government and Housing Act, ensuring that money from council tenants' rent can only be spent on activity relating to the local authority's stock. They also prevent the council from investing in its housing from other funding sources.

An HRA is therefore a borough's ring-fenced budget for managing its council housing stock, which includes paying for repairs and maintenance as well as building new homes for social rent.

A survey undertaken by the Society of London Treasurers and London Housing Directors' Group has revealed the increasing threat of financial insecurity and lack of resilience in London HRAs.

This has been brought about by the combination of fast-rising costs and government policy limiting social rent increases below inflation – or reducing rents altogether – which have led to the chronic under-resourcing of HRAs.

The challenge is exacerbated in London because management of tower blocks and other high-density housing is more expensive and the rent formula does not reflect regional variations in running an HRA. These factors have particularly impacted London local authority landlords.

Boroughs therefore find themselves forced to take increasingly drastic action to maintain balanced HRA budgets, as is their legal duty. The majority of boroughs forecast they will be unable to balance their HRA in at least one of the next three years without reducing spending.

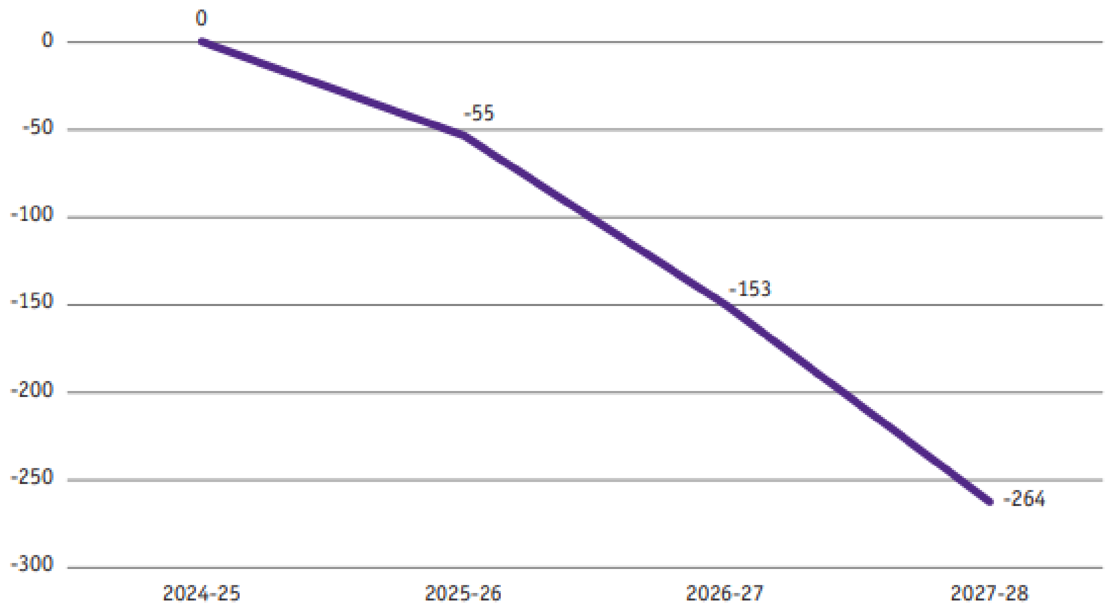
The current approach of requiring councils to seek Exceptional Financial Support (EFS) from the government to meet the immediate needs of their HRA does not provide a sustainable solution, and only places further debt burdens on councils and their HRAs.

Using inflation forecasts for social housing costs, London Councils estimates that boroughs will need to make up to £264m in reductions to their HRA spending over the next three years – including in maintenance and repairs – unless additional revenue becomes available.

Services like repairs are demand led and spending is difficult to control without creating backlogs. Increasing costs of labour and materials also mean that repairs contracts are being exhausted far quicker than budgeted for. This in turn gives rise to lowering resident satisfaction and failures to meet regulatory standards.

London is not in a position to maintain spending in real terms, let alone increase it, despite the urgent need for investment in raising standards, decarbonisation, developing new homes, tackling building safety concerns, meeting reforms such as Awaab's Law, and responding to the requirements of the new housing regulator.

Accumulated change in real-terms spending on repair and management (£m)



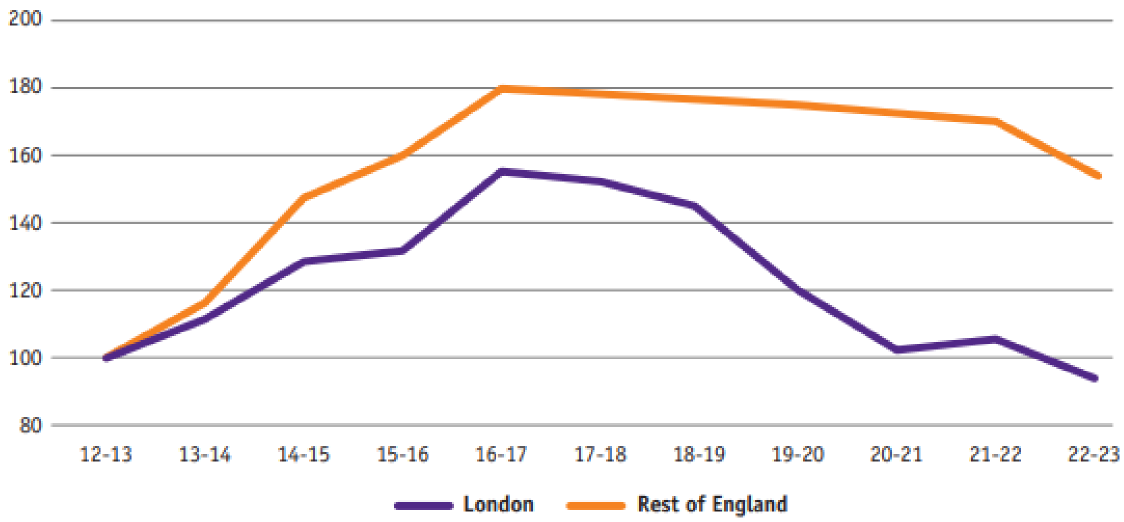
Based on average unit costs collected from London local authorities, the total cost to meet the investment needs of all council homes across London could total over £25.8 billion (2024 prices). Over the medium term, councils need to increase spending on key issues, including an estimated spending need of £4.3 billion in damp and mould.

At the same time, there is evidence of increased spending on legal disrepair claims in London. Data previously collected by London Councils highlighted that for six London boroughs, the cost to HRAs of legal disrepair increased from £5.3m in 2020/21 to £6.5m in 2022/23.

The financial insecurity facing London local authority landlords has seen a significant reduction in HRA reserves. Reserves began to decline in 2016/17, coinciding with the government's four-year social rent reduction. As of early 2024, more than half of London boroughs with an HRA forecast reserves of less than 10% of income. For five boroughs, reserves are predicted to be less than 5%.

The Society of London Treasurers' survey showed that three boroughs expect to completely exceed their reserves before 2027/28 without deeper spending cuts to services and maintenance. Further London Councils analysis, based on more recent inflation forecasts, suggests this could rise to five councils.

Housing Revenue Account reserves, inflation adjusted, 2012-13 to 2022-23 (indexed to 2012)



Key factors driving financial insecurity in London HRAs

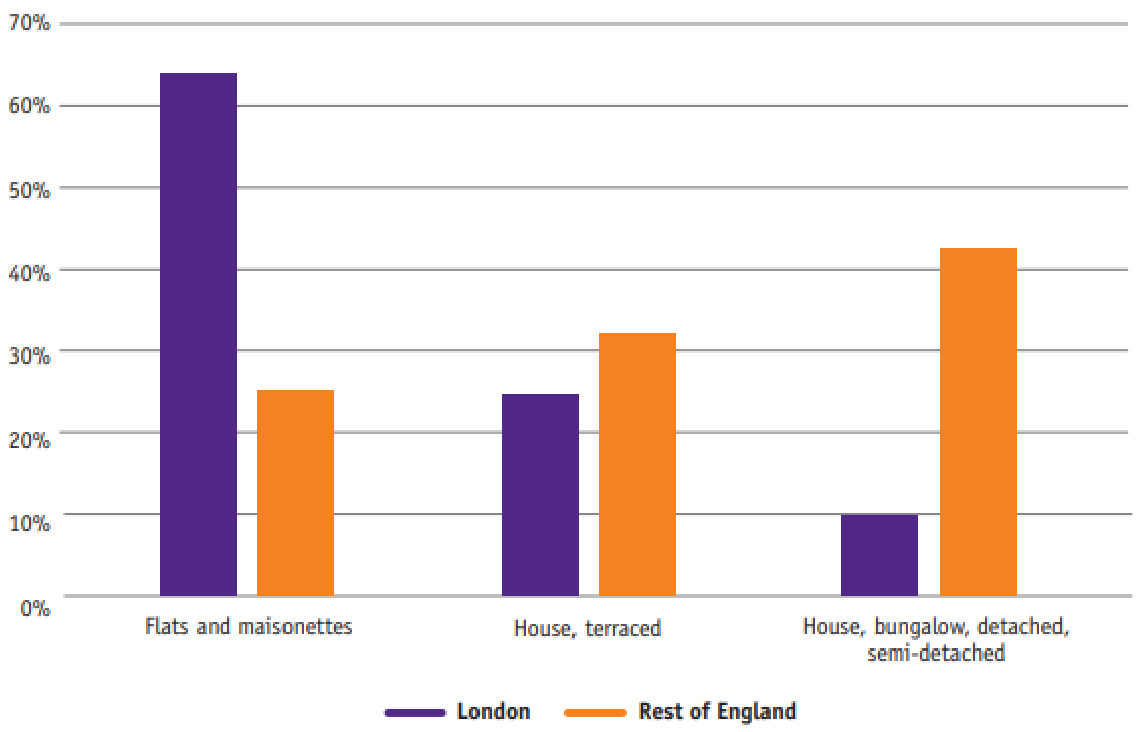
- Impact of rent policy interventions: 1% annual rent reduction (2016/17-2019/20) plus the 7% rent cap (2023/24)
- Costs of maintaining HRA services rising above CPI+1%
- Additional regulatory requirements. While these are welcome, they create new costs that are not funded by national government. These include the implementation of Awaab's Law and new qualification requirements for managers of social housing services. In 2025/26, it is anticipated that the typical London local authority landlord will pay fees of £111,781 to the Housing Ombudsman and £105,100 to the Regulator of Social Housing as part of the requirement that these regulatory services are self-funded. Further costs are also incurred through obtaining building safety certification for higher risk residential buildings (HRRBs) by the Building Safety Regulator plus the ongoing costs of obtaining work approvals.

London's housing is more expensive to maintain

The financial insecurity facing HRAs is a national problem requiring national interventions. However, London faces unique challenges. In particular, a considerably higher share of London social housing comprises flats and maisonettes. These types of properties are associated with higher repair and management costs than, for example, detached houses or bungalows.

Simply put, it is more difficult and expensive to fix a water pipe on the sixth floor of an apartment, than it is on the ground floor of a semi-detached house. Much of London's social housing apartments are legacy stock from the 1960s and 70s, which has significantly deteriorated over time in the absence of funding to support the intensive maintenance requirements.

Estimated profile of social housing stock type



Management costs also tend to be higher for flats compared with other types of housing. Flats have more shared common areas and services, and residents living closer together may necessitate more proactive and intensive management from the social landlord.

London also has the largest proportion of households living in overcrowded accommodation within the social rented sector (19.4% of households). Again, overcrowding is a factor contributing to higher repair and maintenance costs.

Impact of Right to Buy

Over 316,000 council homes have been sold in London since the Right to Buy (RtB) was introduced in 1980. Based on figures for the past five years, on average 1,500 RtB sales are made in London annually.

Boroughs want to build new affordable homes to replace these properties, but strict government rules on the use of RtB sales receipts were in place for many years. These restrictions and other challenges facing social housing finances meant one-for-one replacement has generally not been feasible. The total number of council homes in London has fallen from 715,000 in 1980 to 390,000 in 2024 – a 45% decrease.

Boroughs welcome the government's reforms of RtB, which are anticipated to bolster boroughs' ability to maintain and expand their stock.

However, in response to the reduction to RtB discounts there has also been a significant increase in RtB applications. This is contributing to the immediate pressures on social housing budgets.

Social rent formula fails to reflect London's costs

London HRAs' higher operating costs are not reflected in the national social rent formula.

Rent for a social home is based on the average weekly rent in England in 1999 and includes multipliers for local earnings and property value in 1999 relative to the England average. This is then updated each year according to national metrics, such as CPI.

This formula therefore no longer captures the current relative costs underpinning HRA operations and in particular the rapidly growing cost of housing in London over the last twenty years. An updated formula rent would be roughly 13% higher in London.

Indicative change in weekly formula rent for a two bed property (£)

The government's upcoming decision on future rent policy

The government has consulted on a proposed five-year settlement for social rent, as well as longer-term options, that would allow housing associations and stock-owning councils to raise social rents by the Consumer Price Index (CPI) plus 1% each year.

A final decision is expected soon and will come into force from 1 April 2026.

Although London Councils welcomes the government's commitment to long-term rent certainty for the social housing sector, analysis shows that CPI+1% on its own will not address the financial pressures facing HRAs in the capital.

Research undertaken by Savills for London Councils suggests London HRA accounts would remain in deficit for roughly 20 years under CPI+1%.

This is the result of cost pressures projected to rise above headline CPI until at least 2024/25. A cumulative financial 'black hole' in London HRAs of £700m is therefore forecast between 2023/24 and 2027/28, with a deficit enduring until 2043.

The case for a new debt settlement

London local authorities were allocated £7.7 billion of debt under the HRA self-financing agreement in 2012. This agreement with the government gave local authorities more control over their social housing but in return transferred debt to their HRAs.

The amount of debt transferred was intended to be sustainable. However, it was based on many assumptions about future policies affecting HRA finances that did not materialise.

For example, since the debt settlement in 2012 the government has introduced policies on rent reductions and below-inflation rent changes (in 2016/17-2019/20 and 2023/24), and reinvigorated Right to Buy. These have reduced rental income below what was expected. Changes in borrowing costs and rising capital costs have also contributed to the debt settlement being unsustainable.

Reassessing and lowering the debt settlement is not just a matter of fairness. Analysis by Savills shows that an updated debt settlement that accounted for changes in national government policy would reduce debt servicing costs and enable up to £4.34 billion of new HRA borrowing. This can better support investment that raises housing standards and delivers more affordable homes across the city.

Reintroducing rent convergence is critical

Given the scale of financial pressures, London Councils is clear that rent convergence should be a top government priority. This position is supported by stakeholders across the social housing sector – mostly notably the recommendations of the recent *Securing the Future of Council Housing* report endorsed by over 100 of England's largest council landlords.

The withdrawal of the rent convergence policy in 2015 has been a pivotal factor in the weakening of London HRAs. Due to the higher costs of maintaining and managing social housing, London has been disproportionately affected by the end of rent convergence.

Analysis by Savills (commissioned by the London Housing Directors' Group and London Councils) shows that the re-introduction of rent convergence could generate an additional £1.8 billion over ten years as London boroughs would regain the ability to charge social rents in line with formula rent.

This would represent vital additional income for social housing when finances are facing so many challenges. Restoring the policy is therefore a key step on the path towards the sector's future sustainability.

What does 'rent convergence' mean?

Rent convergence means that tenants in similar properties pay a similar rent.

Rent convergence was first introduced by the government in 2002, with the aim of aligning social housing rents in similar properties within an area.

The government wanted an end to apparently arbitrary differences between rents for social housing properties, while maintaining substantial discounts compared to market rents.

A rent formula was established that took into account local earnings and property values. A 'bedroom weighting' was then used to help ensure local rents reflected local property values.

Rent convergence helped bring greater clarity for social housing tenants, as there was fairness in rent charges for similar properties across a region. Crucially, it enabled social housing providers to gradually increase rents across their portfolio to a standardised level, which supported their financial stability.

However, the government ended rent convergence in 2015, arguing that sufficient convergence had been achieved.

London has been badly affected by this decision, since the gap between target rents and average rents remained relatively high. The loss of the rent convergence policy undermined London boroughs' social housing income and the financial viability of HRAs.

Conclusion

How best to sustain London's social housing finances

The current challenges facing London council housing finances are unsustainable.

One London local authority has already applied for Exceptional Financial Support for its HRA, and London Councils' analysis suggests others will follow unless they make further significant cuts to their spending plans.

Without action to restore HRAs to a healthier position, boroughs fear the collapse of their council housing finances.

Boroughs are already severely impeded from making progress on their social housing priorities. Ending the crisis in HRAs is crucial for enabling boroughs to invest in raising standards, developing new homes for social rent, addressing building safety concerns, and achieving net zero ambitions – all priorities shared with the government.

London Councils' Policy asks for supporting social housing finances and securing a better future for the sector:

- Reintroduce rent convergence to provide councils with the revenue they need and reduce increasing inequities.
- Set out a 10-year settlement with rent increases tagged to CPI+1% over this period.
- Update the HRA debt settlement to account for government policy interventions, the realities of higher costs, and investment pressures (e.g., building safety).
- Boost capital funding through a new Green & Decent Homes Grant to meet the demands of the sector for investment in housing conditions, including an impending revision to the Decent Homes Programme and wider access to building safety funds.
- A guarantee to compensate for lost revenue or additional costs that may result from national government policy changes (similar to the way councils are compensated within business rates retention or through the 'new burdens' principle).
- Enable Right to Buy receipts to be fully combined with grant funding to maximise funding available for housebuilding.
- Further increase grant funding via the Affordable Homes Programme to improve viability of new council housing, including longer-term grant arrangements to enable more complex development, and provide more investment for housing renewal.

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design: pinsentdesign.com
images: iStock
publication date: May 2025