



Our ref 001
Date 7th September 2022

Subject OFWAT PR24 – Nutrient Neutrality

1.0 Introduction

- 1.1 OFWAT is currently consulting on its 2024 price review (PR24). The purpose of this is to set out how it might “*deliver better outcomes for customers, the environment, and wider society.*” The document recognises the impacts of climate change, increasing customer expectations and concerns about the affordability of utilities. It states that there is a “*need to work in new ways to meet these ambitions*” and declares that “*this is the moment for fresh thinking and real change.*” The document goes on to state that OFWAT will “*collaborate with others inside and outside the sector to deliver better, more sustainable outcomes.*” The house building industry is keen to do this in order to ensure that a balance can be achieved between the importance of delivering much-needed new homes and the aspiration of realising the identified objectives of the water sector.
- 1.2 One particular area which affects the water and house building industries is the issue of nutrient neutrality. This has become increasingly important in large parts of England and Wales where there is a concern about the impacts of the discharge of nutrients on sensitive protected habitats and bird species. It is in respect of this matter that the potential for conflict appears to arise between PR24 and government policy.

2.0 The key causes of nutrient discharge

- 2.1 The Environment Agency (EA) has recognised that agriculture and rural land management has now overtaken waste water treatment works as the most common cause of water bodies not achieving good status for nutrients¹. The EA Summary Document, *Phosphorus and Freshwater Eutrophication Pressure Narrative* noted that “*This is a significant change from second cycle of the river basin management plans when water industry sewage works were the most common cause.*” Given the continued reductions in phosphate that are planned by the water industry by 2027, the document anticipated that the contribution of agriculture to total phosphates loads in freshwaters will be increasingly significant:
- “*Our latest analysis suggests that, without further agricultural P load reductions, the agricultural contribution to national river P loadings will increase from around 25-30% at present to over 50% by 2027.*” (Page 4).
- 2.2 However, despite being the most common source of nutrient discharge into water bodies, it is important to recognise that the agricultural sector is not the sole contributor to the problem. This is illustrated in the following graphic which is contained in the EA Summary Document and based on an analysis of the 7,617 reasons for not achieving good status for phosphates. Agriculture is shown to be the primary cause, accounting for 49% of cases whilst

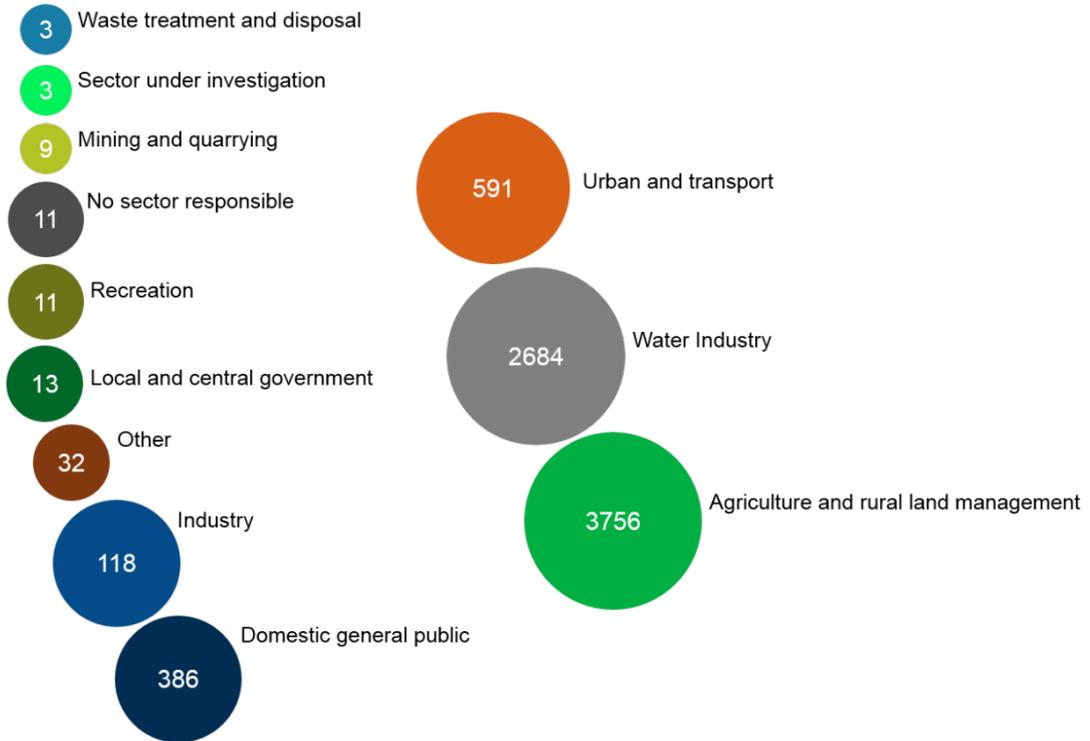
¹ Source: Phosphorus and Freshwater Eutrophication Pressure Narrative (October 2019) https://consult.environment-agency.gov.uk/environment-and-business/challenges-and-choices/user_uploads/phosphorus-pressure-rbmp-2021.pdf



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the water industry accounted for a further 35% of cases. It should be noted that this graphic does not seek to quantify the level of phosphate discharge from each source but it is important in highlighting the range of potential factors – and the dominance of agriculture and the water industry as considerations:

Figure 1 Counts of numbers of Reasons for Not Achieving Good Status (RNAG) (not numbers of water bodies)



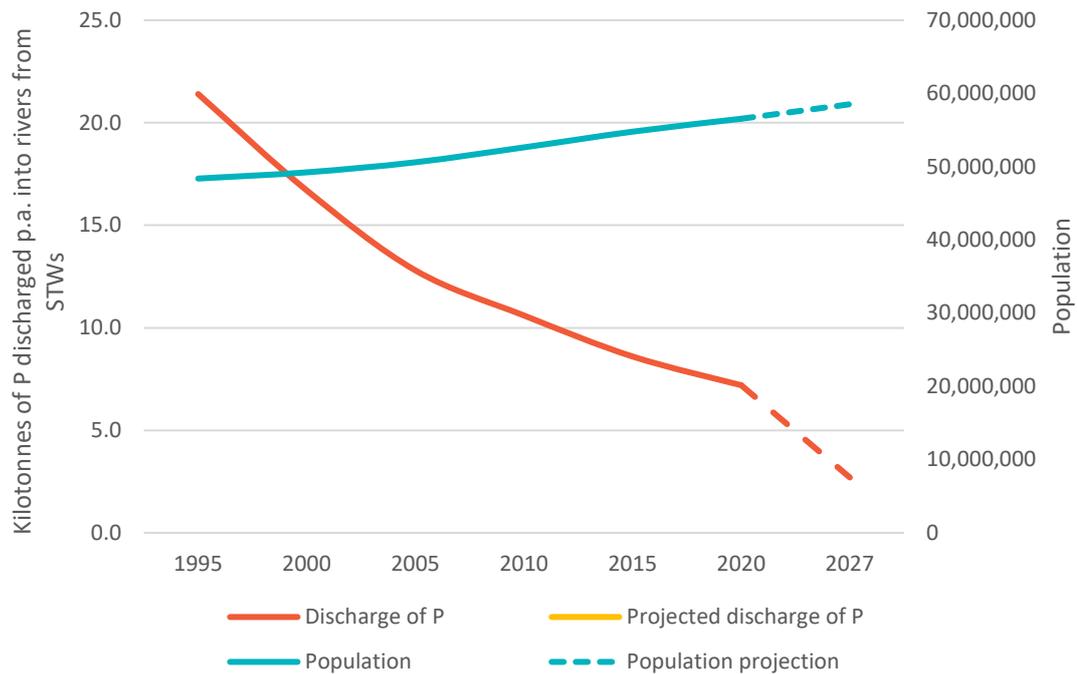
Source: Phosphorus and Freshwater Eutrophication Pressure Narrative (October 2019)

2.3

Water companies have delivered significant improvement in water quality in the past 25 years. Based on EA data between 1995 and 2020 there was a 66% reduction in the discharge of phosphates from waste water treatment works into rivers. By 2027 on-going investment by the water industry will lead to an 88% reduction in phosphate discharges from STW against the 1995 level. This reduction has been achieved in the context of a 16.9% increase in population and a 20.2% increase in the housing stock in England over the same period.



Figure 2 Past and projected future reduction in P discharge from STWs and population levels in England



Source: Phosphorus and freshwater eutrophication: challenges for the water environment, Environment Agency, October 2021; ONS Mid-Year Population Estimates; 2018-based Sub National Population Projections

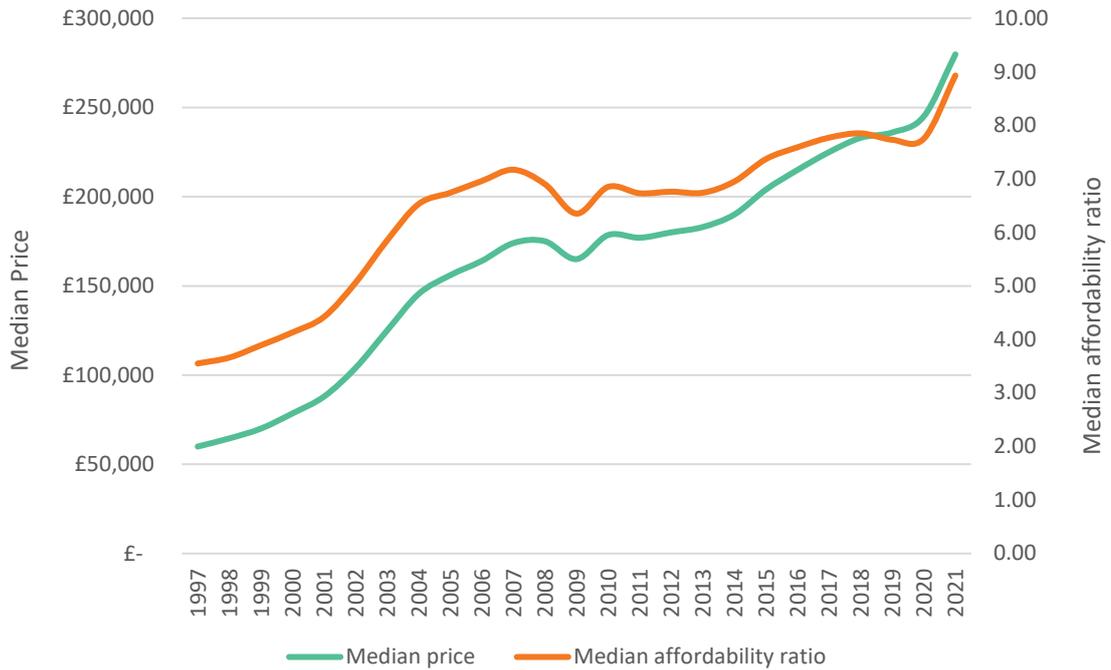
3.0 The role/impact of housebuilding

- 3.1 The house building industry is acting positively through measures such as reducing water consumption in new dwellings and incorporating sustainable drainage systems into developments where appropriate. It has engaged with trial mitigation measures and schemes across the country, but it is evident that too often the level of mitigation is beyond what can reasonably be expected on site and is based on an erroneous assessment of the potential nutrient load arising from new residential development. Going forwards, the water industry must work collaboratively with stakeholders such as the house building industry to address these problems.
- 3.2 However, to date, the house building industry has faced the weight of sanctions. Natural England has advised 76 local authorities in the 34 affected catchments that planning permission – including reserved matters and the discharge of conditions – cannot be legally granted for residential developments unless they are able to demonstrate nutrient neutrality. This has led to an effective moratorium on new housing delivery.
- 3.3 The Home Builders Federation (HBF) has calculated that the delivery of 100,000 new homes is being delayed as a result of this issue – at a time when, as shown below, the housing crisis continues with house prices and affordability ratios remaining at an all-time high.



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Figure 3 Median house prices and affordability in England and Wales



Source: ONS house price to work-pace earnings ratio, March 2022

- 3.4 The fact that the delivery of so many new homes is being held up testifies to the lack of credible credit trading schemes, wetland solutions and other methods of offsetting/mitigation.
- 3.5 The Government’s response to the House of Commons Environmental Audit Committee report on water quality in rivers (January 2022) was published in May 2022. This included a commitment to ongoing reduction in nutrient levels in our rivers whilst also recognising that agriculture and waste water treatment works are the primary causes of high nutrient levels.
- 3.6 Of particular note is the statement setting out the that:

“The Government is concerned by the stalling effect of nutrient neutrality on new housebuilding and the planning system. We will focus on reducing pollution at source as a priority, to ensure that sites can be recovered, as well as supporting sustainable development in catchment areas affected. The Government agrees that planners should understand risks to the water environment when considering granting permissions, but care should be taken in balancing the role of different public bodies in managing pollution risks. DLUHC have provided Local Planning Authorities (LPAs) with funding for a catchment officer to help identify nutrient mitigation to allow development to continue, and Natural England are proactively working with LPAs to ensure mitigation is appropriate and sufficient. We must ensure that planning authorities are not required to consider matters outside of their expertise or expected to become involved in regular farm management activities that could place a heavy additional burden on the planning system. The relevant regulator in this case is the Environment Agency.” (Page 8)
- 3.7 The Written Ministerial Statement issued by the Secretary of State for Environment, Food and Rural Affairs on 20 July 2022 accompanied the introduction of a package of measures to tackle nutrient pollution. The statement recognised that:



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“In the meantime, we know the impact of new housing is a small proportion of overall nutrient pollution, but mitigation requirements have a significant impact on overall house building. This amendment will improve water quality and in doing so will support housebuilding to continue in areas affected by nutrient pollution. We want these improvements to be factored in for the purposes of a Habitats Regulation Assessment.”

- 3.8 The small proportion of overall pollution arising from new housing can be understood by reference to:
- 1 The significant role of the agricultural industry in respect of nutrient pollution, as outlined above.
 - 2 The fact that between 2008 and 2021, new house building in England has accounted for between 0.5% and 1.0% of the total housing stock per annum – equivalent to a total of a 9.98% increase in stock over the 13 year period.
 - 3 The reality that new housing schemes are not generally permitted to connect to constrained combined sewers but instead are expected to have separate systems for surface water and foul water. Therefore, permitting new residential development should not result in an increase in the overflows that occur in exceptional circumstances as “safety valves”. The increase in the number of storm/flood events which are resulting in a greater level of phosphate discharge into rivers can be attributed to climate change rather than new house building.
 - 4 Preventing new houses from being built would not address the problems arising from the continued reliance on aging infrastructure that serves existing urban areas which instead, that requires a continuation of investment by the water industry. By contrast, new housing can sometimes assist in accelerating improvements to local infrastructure deficiencies to ensure capacity is available to deliver new homes.
- 3.9 Net additional dwelling completions in England between 2009 and 2021 averaged 181,700 – ranging from 124,700 in 2012-13 to 242,700 in 2019-20. Whilst there is no expectation that the 100,000 new homes that are estimated as being held up by the nutrient issue would have otherwise been delivered in a single year, this nevertheless indicates the magnitude of the problem and the potential impact of the moratorium on the future supply of housing across the country, and particularly in those authorities that fall within the affected catchments where:
- 1 A total of 532,000 new homes were built in the affected authorities between 2008-9 and 2020-21 – an average of 41,000 each year; and,
 - 2 Net additional dwelling completions in the affected local authorities ranged from 28,000 in 2012-13 to 55,300 in 2018-19.
- 3.10 In addition to a very substantial social cost arising from the under-delivery of new housing, the moratorium is predicted to create a significant risk to the national economy and the local economies of those areas that will be most affected. It could result in the loss of c.£30 billion of (direct and indirect) economic output and jeopardise almost 500,000 person years of construction employment. It could also result in the loss of £550 million of first occupation expenditure and £1.4 billion of expenditure by residents each year, not to mention the loss of £175.8 million through Council Tax payments each year and a total of c.£750 million new homes bonus revenue to individual local authorities.



Table 1 Estimate of economic impact of non-delivery of 100,000 new homes nationally

Construction Impacts	
Construction value	£13,810,000,000
Direct construction jobs (person years)	226,000
Supply chain jobs (person years)	264,500
Economic outputs (Construction GVA + Supply Chain GVA)	£29,924,000,000
Expenditure Impacts	
First occupation expenditure	£550,000,000
Jobs (via first occupation expenditure)	4,900
Resident expenditure p.a.	£1,418,000,000
Jobs (via resident expenditure)	18,400
Total jobs supported by expenditure	23,300
Fiscal Impacts	
Council tax p.a.	£175,800,000
NHB Payment (total over four years)	£750,000,000

Source: Lichfields analysis. Figures rounded

4.0 Proposed interventions to boost housing delivery

4.1 In response to its acknowledgement that new housebuilding makes a limited contribution to nutrient discharges, the Government has announced that it:

“will table an amendment to the Levelling Up and Regeneration Bill. This will place a new statutory duty on water and sewerage companies in England to upgrade wastewater treatment works to the highest technically achievable limits by 2030 in nutrient neutrality areas. Water companies will be required to undertake these upgrades in a way that tackles the dominant nutrient(s) causing pollution in the catchment of habitats sites. To ensure regard is had to the required WWTW upgrades, the Habitat Regulations will be clarified, so the measures are considered certain in the assessment provisions.”

4.2 The implication of this was detailed by the Chief Planner in her letter to chief planning officers of local authorities:

“The performance of WWTW is therefore the central factor in the level of nutrient pollution associated with existing homes and new development. It is therefore logical that effort on reducing nutrient pollution associated with housing focusses on upgrading WWTW. The statutory obligation for upgrading WWTW, which will be introduced into the LURB, will ensure that WWTW in nutrient neutrality catchments are operating at the highest level of performance, rectifying nutrient pollution at source. This will reduce the pollution from not only new development coming forward, but also from the majority of existing dwellings in affected catchments, representing a significant decrease in overall pollution from housing.



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“Under Natural England’s Nutrient Neutrality methodology, the permit limit is used, or where there is no permit limit on nutrient discharges from WWTW, a standard precautionary figure is used (8mg/l for phosphates (P) and 27mg/l for nitrates (N)). The statutory obligation from 2030 will require WWTW to operate at the technically achievable limit (TAL); for phosphates this is 0.25mg/l and nitrates 10mg/l. This action will ameliorate nutrient pollution and significantly reduce the mitigation burden for developments.

*“For developments this means that the current high level of mitigation will only be required up to the end of 2030. **After 2030, the pollution levels via WWTW will be much reduced and so a lower level of mitigation will be required. This reduces the overall mitigation burden on housing developments coming forward in nutrient neutrality catchments.**”*

4.3 The clear expectation of government is that the proposed improvements that are to be implemented to ensure conformity with the proposed amendment to the Levelling Up and Regeneration Bill will reduce the requirement for housebuilders to demonstrate nutrient neutrality mitigation.

4.4 **During** the campaign for leader of the Conservative party, the newly elected Prime Minister the RT honourable Liz Truss pledged to remove nutrient neutrality rules altogether. A spokeswoman for her campaign said *“we would remove Brussels red tape, such as nutrient neutrality, that has stalled housing projects without delivering on what it is designed to address.”*

4.5 It is not clear how or when this abolition of regulations would be introduced but the announcement points towards a clear intention to further reduce the impact of the issue on housing delivery and allow a greater focus on those sectors and activities that contribute more significantly to the problem.

5.0 PR24 proposals

5.1 Against the context we note that page 121 of Appendix 9 (*“setting expenditure allowances”*) sets out the proposed approach to nutrient neutrality expenditure in PR24, as follows:

“The starting point for considering the treatment of NN in the PR24 framework is how it fits in with companies’ wider environmental requirements to remove nutrients. This will define the scope of nutrient removal schemes that are ‘eligible’ for nutrient mitigation, which developers can use to demonstrate NN. Under Natural England’s guidance, planned environmental improvements in the 2025-30 period that would have happened in the absence of the NN requirement, but nonetheless would lead to an improvement in phosphorous or nitrogen standards, do not ‘count’ for NN mitigation. The key principle is that it would be inappropriate for developers to obtain NN mitigation from planned environmental improvements. NN mitigation needs to be separate and incremental to planned environmental improvements to ensure no net deterioration of the relevant site in unfavourable status.”

5.2 We are concerned that this position is contradictory with the approach set out in the July 2022 Written Ministerial Statement.

5.3 As set out above, the effect of the requirement arising from the Government’s proposed amendment to the Levelling Up and Regeneration Bill will be to lower the technically



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achievable limits at waste water treatment works. In this regard it would raise the baseline against which the need for mitigation would be assessed. This is reflected in the letter from the Chief Planning Officer which states that *“this action will ameliorate nutrient pollution and significantly reduce the mitigation burden for developments.”*

- 5.4 In the light of this, the required improvements to waste water treatment works would not be viewed as mitigation for nutrient neutrality but would instead constitute an adjustment to the baseline against which the impact of new development can be calculated, thereby reducing the need for mitigation.
- 5.5 Clarification is required in respect of this matter.
- 5.6 If it is not possible to reach agreement in this regard, we further note that the Appendix identifies two scenarios:
- 1 One in which the key driver for the programme that was planned in the 2025-2030 water industry national environmental programme (WINEP) was to achieve general environmental improvements – in this case Natural England would not allow the scheme to count as mitigation for nutrient neutrality and so developers would need to find an alternative unplanned scheme to demonstrate mitigation for nutrient neutrality; and,
 - 2 Another in which the key driver was compliance with nutrient neutrality – in this case the scheme can count as mitigation for nutrient neutrality as it would not have been part of the WINEP had it not been for the nutrient neutrality requirement.
- 5.7 Whilst the statutory duty on water and sewerage companies in England to upgrade waste water treatment works to the highest technically achievable limits by 2030 will facilitate environmental improvements, it will deliver nutrient neutrality. As such, we believe that it falls within Scenario 2 set out above and would therefore be eligible for developers to demonstrate Nutrient Neutrality mitigation. However, urgent clarification is required as to the position of OFWAT and Natural England in this regard – i.e. that the measures required by the WMS can be regarded as mitigation. This is important in order to remove the confusion and potential contradiction that has arisen.
- 5.8 The PR24 draft methodology was published on 7 July 2022 – two weeks before the Government announced its new measures in response to the nutrient pollution issue. This might explain the apparent confusion and inconsistency that exists. Furthermore, the proposed statutory requirement for improvements to waste water treatment works is dependent on an amendment to the Levelling Up and Regeneration Bill and the subsequent enactment of that bill (as amended) into law. It will therefore be some time before it represents a statutory requirement that must be taken into consideration.
- 5.9 However, a scenario should not be permitted whereby PR24 is inconsistent with – and threatens to undermine the achievement of – government policies and objectives in respect of the delivery of new housing.
- 5.10 Appendix 9 states at page 123:
- “If water companies are required by the UK government to go beyond current environmental permits for NN mitigation purposes, we will consult on a revised charging framework in relation to NN. We will do this in good time for companies to be able to set charges under the new charging rules from April 2025.”*



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5.11 This would appear to reflect the situation that has now arisen, and so further consultation would appear to be necessary to clarify matters and set out a revised charging framework that reflects the proposed statutory duty.

6.0 Alignment with strategic objectives and the 1991 Water Industry Act

6.1 The Government's strategic priorities and objectives for OFWAT (September 2017) state at paragraph 27 that:

“A resilient water sector must meet the needs of a growing population. The government is undertaking radical, lasting reform that will get more homes built right now and for many years to come. We expect that companies will contribute by achieving timely connections of new developments to water and wastewater systems, using innovative approaches within the charging regime where appropriate, so that this does not hold up getting homes built. Companies have signed up to a set of service standards and the timeliness of developer connections is improving. Ofwat should keep under review what it can do to make sure that company planning and delivery keeps pace with housebuilding and supports development across the country, taking account of its duty to contribute to the achievement of sustainable development.”

6.2 The approach that is now set out in PR24 would appear to undermine that strategic objective by continuing to threaten the delivery of new housing across England and Wales. OFWAT will have been aware of the Dutch Nutrients case that gave rise to the current requirement for nutrient neutrality and will have considered the implications of this in terms of statutory duty imposed on all sewerage companies under Section 94 of the 1991 Water Industries Act – which was upheld by the Supreme Court in 2009 in the case of Barratt Homes v Welsh Water:

“The burden of dealing with the consequences of this additional discharge falls directly upon the undertaker and the consequent expense is shared by all who pay sewerage charges to the undertaker.”

6.3 It is a matter of surprise that OFWAT did not ensure that water companies were equipped with the resources that they needed to respond to the requirement of Section 94 in the context of the Dutch N case. Essentially this should have necessitated the upgrading of waste water treatment works (as is now required by 2030) before now in order to ensure create sufficient headroom within the system to facilitate the achievement of nutrient neutrality by new residential development.

6.4 The fact that PR24 now appears to be contrary to the aim of contradicting with the requirement for water companies to keep pace with house building and support development across the country is a matter of grave concern.

7.0 Conclusion

7.1 We welcome the opportunity to engage with OFWAT regarding its proposals for meeting future water needs and overcoming the significant challenges that face the industry. It is clearly important to ensure that improvements to the quality and supply of water resources can be achieved, including the impact of the sector on the environment, but this should not be at the expense of other key elements of national infrastructure – including the delivery of new housing



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- 7.2 Significant improvements have been achieved in respect of the nutrient discharge from WWTW to protected waterways but the Government has set out proposals for more significant targets through the introduction of a statutory duty on water and sewerage companies in England to upgrade waste water treatment works to the highest technically achievable limits by 2030 in nutrient neutrality areas. This would reduce the burden of mitigation on the house building industry and would thereby overcome the current moratorium – which is exerting substantial economic and social costs – and help to ensure the delivery of much needed housing.
- 7.3 A careful review of PR24 raises concern regarding the potential for conflict with government objectives. In response, we would highlight the need for:
- 1 Urgent clarification in respect of the matters set out above – namely that:
 - a The proposed statutory duty would raise the baseline against which the need for mitigation would be assessed and, as such, would not constitute a form of mitigation;
 - b If OFWAT does consider that the statutory duty would constitute a form of mitigation, that this could be counted by housebuilders as eligible mitigation for nutrient neutrality – thereby facilitating the delivery of housing, as anticipated by government; and,
 - c The measures required by the WMS can be regarded as mitigation
 - 2 Further consultation on a revised charging framework that reflects the proposed statutory duty.
 - 3 Confirmation that PR24 will not increase the burden on housebuilders by way of requiring additional mitigation,
- 7.4 The wider house building industry, including ourselves, look forward to continuing to work with OFWAT and the wider water industry in order to address the issue of nutrient neutrality.