Expert view

Creating solutions

Penelope Biggs introduces Northern Trust's Retirement Solutions Practice

Every way you look at it, pension funds are in deficit to a tune of billions of pounds – and when you learn that the NAPF is launching a campaign to 'save our DB plans' you know its really tough. The fact is that sponsors do not have enough cash to fund their DB liabilities and it is weighing heavy on their share price. As a result employees are being moved to DC arrangements as DB schemes decline.

The background and heritage of our organisation is very much in defined benefit schemes and solutions, so the question we posed ourselves was whether, as the needs of sponsors and trustees change, we could be in a position to provide relevant solutions in this very challenging environment. We think of the predicament as 'VIM'; our clients need vision (V) to see where are going, the intention (I) to strike a path forwards and the means (M) to execute upon their strategy.

From this was born our new Retirement Solutions Practice. We are not trying to compete with professional advisors such as investment consultants who have a very different set of expertise, but in our asset servicing business we have a pool of experience and talent to understand the technical issues faced by pension funds and in our investment practice we have the asset management expertise to develop creative solutions.

> **"The fact is that sponsors do not have enough cash to fund their DB liabilities and it is weighing heavy on their share price"**

Here's an example of some of the solutions we are working on: firstly solutions to facilitate the "institutionalisation of defined contribution." One challenge here has been that the pools of DC assets alone are not big enough to generate economies of scale for the sponsor and ultimately the members. The question is can we create a structure that allows the pooling of DB and DC assets together to generate the economies of scale pension funds require. This is the type of pan-European solution we are exploring with a number of multinational firms.

Another concept we are investigating is whether our own cross border tax efficient pooled fund structures could be 'rented' out selectively to pension funds and asset managers as a "fund hosting platform". These are just some of the ideas we are working on, but we are keen to develop our lines of thought to help sponsors and trustees manage their pension schemes to make them more efficient and ultimately more viable for the future.

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Expert view

European pension plans

Multinationals are setting up truly cross-border pension pools, says Aaron Overy, pooling strategist at Northern Trust's Retirement Solutions Practice

Some of you may not realise it, but there are around 10,000 IORPS pension schemes in Europe and most of these are in the UK. IORPS are pension schemes set up under EU laws since 2003 to enable 'pension pooling' which means pan-European pension schemes. In an IORPS scheme employees in France, Germany, the UK and anywhere within the EU can contribute directly into the same pension fund.

The majority of UK schemes set up under IORPS have been, however, at pains to make sure they are not cross-border. This is because as soon as you have a German employee paying into an otherwise UK-only pension scheme you have to take account of German Social & Labour Law. Pension rules vary enormously from country to country and in Germany, for instance, contributions into a DC arrangement are guaranteed by the sponsor. So unless you are ready to track a truly European pension scheme, you need to ensure you only have local members.

The Directive was made in 2003 to allow you to pay into a scheme being run in any other country. Four countries have put themselves forward as bases for these schemes – Ireland, Luxembourg, Belgium and the Netherlands – and all are competing with each other to offer the most flexible regulation. But wherever these schemes are based, they will allow employers with staff in different countries to offer an attractive pension scheme without having to go to the trouble of creating local versions in each country.

IORPS schemes cover DB and DC arrangements, but we fully expect DC schemes to be more attractive. This is partly because the EU rules state that IORP schemes must be fully funded at all times. What exactly 'fully funded' means is being interpreted variously by countries – it could mean having a recovery period of three years, for instance – so it might not be as draconian as it sounds. But nevertheless, we expect the DC variant to take off quicker. There are some teething problems however. Although there is no tax discrimination in theory some countries are not entirely playing ball. But on the whole we believe international employers will jump at the chance of enrolling employees into one scheme – and it's not just for EU workers; you can have a Mexican section if you want to! And due to the flexibility of the rules you can really draw up some exciting benefit plans with the latest in fund ranges. One element we often find is that different national cultures have different investing habits, and a default fund for your German section (e.g. bonds) might look quite different from the one expected by British members (e.g. equities).

Setting up a pan-European pension scheme is something that a number of large schemes I know are considering right now, and they are using it at as an opportunity to offer best-in-class DC pensions. We may have been talking about this for years, but now the work is really happening.

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