



Options for Asset Allocation Disclosure on a Defined Benefit Plans Annual Funding Notice

ATTORNEYS

Jodi H. Epstein

Alexander Maged

PRACTICE AREAS

Benefits & Compensation

Retirement Plans

Benefits Bullets

February 14, 2025

Introduction

- Defined benefit plans are required to provide participants with an Annual Funding Notice, or "AFN."
- DOL regulations require that the AFN include the allocation of Plan investments, but do not dictate specific asset categories that must be listed for purposes of this disclosure.
- The AFN is usually prepared by the plan's actuary, then reviewed by the plan administrator.
- This Benefits Bullets is intended to assist the plan administrator's review. It provides background on the asset allocation disclosure requirement and presents several ways that defined benefit plans can meet it.
- Note that as of 2025, reporting requirements for the Annual Funding Notice are modified under Section 343 of the SECURE 2.0 Act.
- To date, however, the DOL has not released an updated model AFN to reflect these required modifications, and SECURE 2.0 does not modify the specific asset categories that need to be listed, which is our focus in this Benefits Bullets.
- If the DOL releases an updated model AFN, we will follow up with another update, and let you know if it changes our analysis below.

Background

- **DOL Regulation**



| 2 | Options for Asset Allocation Disclosure on a Defined Benefit Plans Annual Funding

- 29 CFR 2520.101-5(b)(5)(ii) requires that the AFN include "the asset allocation of investments under the plan (expressed as percentages of total assets) as of the end of the notice year."
- However, the regulation does not identify specific asset categories that need to be listed.
- **DOL Model AFN**
 - The DOL's current model AFN (for both single-employer plans and multiemployer plans) can be used to satisfy the requirements of 29 CFR 2520.101-5.
 - However, the introductory language emphasizes: "You may also develop your own notice, provided it contains all of the information required by 29 CFR 2520.101-5."
 - In its section on Funding & Investment Policies, the model AFN offers two alternatives for listing assets.
 - Alternative 1 is more complex. It includes seventeen categories for single-employer plans and sixteen categories for multiemployer plans (and several subcategories for both).
 - Alternative 2 is simpler. It includes only five categories for both single-employer and multiemployer plans:
 - Stocks
 - Investment grade debt instruments
 - High-yield debt instruments
 - Real estate
 - Other
 - The model AFN does not define each asset category.
 - Instead, it states: "Follow the instructions for the latest Schedule R to Form 5500 to allocate investments to one of the above asset classes."
- **Form 5500**
 - The Form 5500 Schedule R Line 19 asset categories are:
 - Public equity
 - Private equity
 - Investment-grade debt and interest rate hedging assets
 - High-yield debt
 - Real assets



Options for Asset Allocation Disclosure on a Defined Benefit Plans Annual Funding

- Cash or cash equivalents
- Other
- These categories are different than those listed on the model AFN.

Allocation Options

- Based on the above, defined benefit plans appear to have several options when disclosing asset allocation on their AFNs.
- **Use Independent Categories**
 - First, note that assets can technically be listed using a categorization scheme that appears neither on the Form 5500 nor on the DOL's model AFN.
 - This option is available under the regulation but is probably less favored than using a categorization scheme that reviewing agents are likely to recognize.
- **Use Form 5500 Categories**
 - Second, and perhaps most simply, assets could be listed in the same categories that appear on the plan's Form 5500.
 - This option avoids the need to re-categorize plan assets for purposes of the model AFN.
 - However, some plans may prefer to hew precisely to the asset categories listed on the model AFN (see next option).
- **Use DOL Model AFN Categories**
 - Third, of course, plans may decide to use the asset categories that appear on the model AFN.
 - Some plans may hesitate to use these asset categories because they are not clearly defined, and the plan likely does not have an existing record that allocates its assets into these specific categories.
 - However, it may be possible to map the Form 5500 Schedule R Line 19 categories onto the model AFN Alternative 2 asset categories without requiring additional information.
 - Below is a proposed alignment of the Form 5500 Schedule R Line 19 categories with the AFN Alternative 2 asset categories.

Form 5500 Schedule R Line 19 Asset Category



Notice of Options for Asset Allocation Disclosure on a Defined Benefit Plans Annual Funding

Definition of Form 5500 Schedule R Line 19 Asset Category (from Form Instructions)

Proposed Model AFN Alternative 2 Asset Category

Public Equity

Publicly traded U.S. and non-U.S. equity securities and the approximate portion of mutual funds or collective trusts invested in public equities.

Stocks

Private Equity

Direct ownership, co-investment, limited partnerships, fund of funds or other investments in equity ownership not included in the Public Equity category.

Other

Investment-Grade Debt and Interest Rate Hedging Assets

Investment-grade dollar denominated debt securities (fixed income) traded publicly or privately, and the approximate portion of the mutual funds or collective trusts invested in such securities. Investment-grade debt-instruments are those with an S&P rating of BBB- or higher, a Moody's rating of Baa3 or higher, an equivalent rating from another rating agency, or generally considered to be of equivalent credit quality. Include preferred equity in this category. Unrated debt with the backing of a government entity would be included in the "investment grade" category unless it is generally accepted that the debt should be considered as "high-yield." Use the ratings in effect as of the end of the plan year. Include the market value (not notional value) of interest rate swaps, futures and other derivatives designed to be interest rate sensitive in this category.

Investment grade debt instruments

High-Yield Debt

Debt securities not included in Investment Grade Debt as described above or in Cash and Cash Equivalents as described below. Include the approximate portion of the mutual funds or collective trusts invested in high yield debt securities.



Notice Options for Asset Allocation Disclosure on a Defined Benefit Plans Annual Funding

High-Yield Debt

Real Assets

Direct ownership, co-investments, or shares of funds with direct ownership in income-producing assets such as real estate, infrastructure, or land (e.g., farmland or timberland). Real estate investment trusts (REITs) should be included with Public Equity.

Real Estate

Cash and Cash Equivalents

Non-interest-bearing cash (Schedule H item 1(a)) and accounts at financial institutions that earn interest (Schedule H item 1(c)(1)).

Other

Other

Any investments not included in the categories as described above, such as hedge funds, commodities, and collectibles.

Other