What Happens to Your Benefits if Your Employer Goes Bankrupt?

As the economy works its way back from the brink, many companies are still going to be facing the possibility of bankruptcy. What if one of them is your employer, or the company you retired from?

The critical issues here are retirement and healthcare, but they might also extend toward other lesser company benefits. The first question to ask is what kind of bankruptcy has been filed. Under Chapter 11 bankruptcy, companies generally stay open and reorganize financially so they can continue to operate and fight their way back to health. Yet there may be some intermediate changes – the employer may cut or temporarily slash employer matching on 401(k) plans or modify certain elements of traditional defined benefit plans to ease its own cash concerns.

If the company is forced to file bankruptcy under Chapter 7 liquidation, employees and retirees are far more exposed to losing benefits altogether. As the company closes its doors, typically all company-sponsored retirement and health care plans and related benefits are terminated.

If you're uncertain how such a major change in your employer's financial future might affect you, a visit to a Certified Financial Planner™ professional might be a wise move. There, you can take a sweeping look at all the changes that have happened to your retirement investments in recent years and get a broader sense of how to plan for retirement going forward.

There are some critical federal protections in the case of either bankruptcy format for private employer retirement plans, but they do have limits. The Employee Retirement Income Security Act (ERISA) requires that any retirement plan assets, whether under a traditional pension (known as a defined benefit plan) or under a 401(k) (known as a defined contribution plan) be separate from corporate assets and thus secure from company creditors.

Traditional pension plans have an added protection – federal insurance. The Federal Pension Benefit Guaranty Corp. (PBGC) will essentially pay up if your employer goes under up to a maximum limit based on the kind of annuity that underlies your plan. Generally, the PBGC backs up most vested normal retirement benefits, early retirement benefits and certain survivors' benefits at the level in effect on the date of a pension plan's termination. However, the PBGC does not guarantee all types of benefits under covered plans. In 2009, the maximum monthly limit paid under PBGC for workers retiring at age 65 is $4,500, which may be fine for most workers. For workers who would receive a higher pension if they retired while the company was healthy, though, the income they had originally hoped for may be potentially lower. In case of bankruptcy – there is one added benefit –all employees in affected plans are automatically 100 percent vested.

The Federal government doesn't insure 401(k) s, though the ERISA requirements keep the wealth in those plans away from creditors. Obviously, if your company is publicly held and has lost significant stock value, that's something that can't be protected.

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Employees should be aware of one more risk. Deferred compensation plans are generally not protected from creditors and when bankruptcy comes, it's unlikely the company will be able to fund those plans.

Regarding healthcare for current workers and retirees, their group health plan must give notification within 60 days of any reduction in benefits. Current workers and retirees under age 65 are the most exposed if retiree health benefits are terminated through bankruptcy court. ERISA law protects pensions, but not retiree health benefits, against corporate bankruptcy.

If your retiree health benefits are terminated, you need to find out what other health coverage is available to you as soon as possible – see whether you have options with a spouse's plan or through private health insurance. It's not a bad idea to consult a financial planner or your independent insurance agent just to see what options might be available. Also keep in mind that if an employer cancels all of its health plans and you lose your job, you will not be able to buy continuing coverage through Consolidated Omnibus Budget Reconciliation Act (COBRA).

Retirees 65 or over are in much better shape. They are covered by Medicare and should consider purchasing Medicare supplemental insurance to cover prescriptions and other expenses not covered under Medicare.

Questions to ask now:

How much of my company 401(k) is invested in company stock? Granted, you might already have a sense of how your company's stock value might be affecting your plan – it's a reflection of your company's financial health. But it's important to know, if you haven't asked, how much of your retirement assets might be tied up in company shares.

Did my company continue making plan contributions and matching benefits right up to the bankruptcy filing? While this might not add up to much money when you do start receiving retirement benefits, you need to check whether the company was on time with its contributions right up until the bankruptcy filing date. Check with the company's plan administrator to check this status, and keep the phone number of the nearest office of the Pension and Welfare Benefits Administration to see how the company is doing with ERISA requirements and the Pension Benefits Guarantee Board to ask critical questions about the status of your defined benefit plan.

What are my health insurance options if my company cancels my plan? If you are under age 65 and are still working or retired, you should immediately check your health benefits status with the company and look for other independent insurance options if there is likelihood your coverage might be terminated.

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FPA FINANCIAL PLANNING PERSPECTIVES

New Credit Card Rules

Washington has now approved sweeping changes to the credit card industry that will allow credit card users a bit of breathing room. But even though those changes won't become effective until next February, it's a good idea to keep working on your debt issues because we're likely to be entering a less-liberal era of credit.

The new rules will change the way credit card companies increase interest rates and set their payment policies, but it's wise to spend this year doing the number one thing all people with outstanding debt should do – winnow it down. Recent changes to the major credit scoring system – FICO – penalize cardholders who keep high balances on their cards more extensively than before.

If you are wrestling with credit card debt and other debt besides, it's a good idea to discuss the matter with a trusted financial advisor such as a Certified Financial Planner ™ professional. A full examination of your financial challenges might help you better manage debt in the future.

In the meantime, here are some of the changes the new law will bring:

Good news for parents worried about their kids and plastic: According to United College Marketing Services, a company that markets credit cards to college students, the average college student receives between 25-50 credit card solicitations per semester. The new law will, among other things, keep credit card companies from offering free merchandise to college students in exchange for signing up for a credit card account from an offer made on or near campus. It will also keep issuers from sending new cards to students who haven't actually applied for cards.

More time to pay: The law states that issuers will have to give customers "a reasonable amount of time" to make their payments on monthly bills. When the law goes into effect, cardholders will now have due dates at least 21 days after they are mailed or delivered. The current requirement is only 14 days.

Double-cycle billing to end. Some issuers actually calculate finance charges for a current month's bill based on days in the previous billing cycle as well as the current one, which racks up the finance charges. That will stop once the new law starts.

You might see your rate go up, but at least you'll get notice: In the first year you have a card the credit card company needs to give you all the terms that will apply to your card in that first year, and they'll have to hold your rate steady unless you're more than 30 days late in making payment. For any card account held after that one-year anniversary, issuers can raise your interest rate as long as they give you 45 days' notice and any increase can only apply to new balances recorded after the start date of the new rate.

Your payment will go to high-interest debt first. If you have credit card balances at different rates on a single card, your payments are typically applied to the lowest-rate balance meaning your higher-rate balances will continue to accrue interest at that higher level. Once the law kicks in, the credit card companies will have two choices – to either apply your payment to the highest-rate balance or to divide the payment proportionally to each rate level. It might be worth a call to your issuer after the law becomes effective to find out which system they're using.

More disclosure on minimum payments: If you're making only minimum payments on credit card debt, it's like keeping your balances frozen indefinitely. Credit card issuers will have to tell cardholders how long it would take to pay off the entire balance if users only made the minimum monthly payment. Issuers must also provide information on how much users must pay each month if they want to pay off their balances in 36 months, including the amount of interest.

Fee relief for subprime cards: Credit cards awarded to people with subprime credit typically offer low spending limits with very high fees to the extent that some users may spend half their balance on fees alone. Under the new law, the initial fees can be no more than 25 percent of the card's credit limit, and in the first year, no more than 50 percent of the original credit limit can be used to cover fees.

Keep in mind that these provisions will likely come as a cost to more conservative users of credit. To make up the shortfalls in revenues these changes will bring, experts expect issuers to raise annual fees and cut back on rewards programs, particularly for customers who pay off their balance each month.

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FPA FINANCIAL PLANNING PERSPECTIVES

Setting New Spending, Savings and Borrowing Habits for the Post-Recession Age

No one can say for sure when the economic upturn will start to relieve the pressure on the nation's households, but one thing is certain – the landscape for consumer borrowing and spending will be different for years to come.

It's wise to look at this as an opportunity. Any recent efforts you've made to scrimp, save and pay off debt should become a permanent part of your financial philosophy. If you still haven't taken those steps, it might be wise implement the following:

Restart your finances with a thorough financial plan. If you've lost a job or have been struggling to get control of your debt, savings or investments, plan a visit now with a Certified Financial Planner™ professional. At the meeting you can also examine spending patterns and the emotional drivers behind many of your financial decisions. If you don't have a planner in mind, the Financial Planning Association has a Web site where you can search by location and specific planning issues.

Create a budget. If you've never tracked your spending before, make a commitment to do so for at least two months as you pull together financial statements, income sources and your bills. Start separating all your expenses into both fixed (amounts that don't change) and variable (amounts that may change, such as restaurant meals, gasoline expenditures and entertainment expenses). Take into account any major expenses that are coming up within the year. Total your monthly income and expenses and then start identifying the expenses that you can trim and figure out whether you can direct the money you save to spending or debt. Congratulations – you've created your first budget. Also, don't ignore planning for perks and vacations and make sure you plan ahead for big expenditures, such as cars and retirement.

Go cash or debit: Return credit cards to their correct status – a way to afford emergencies. Debit cards with a bankcard logo are typically welcome at most stores where credit cards are accepted. This way, you pay cash without carrying cash. If you don't have such a card, you can probably get one from your bank or credit union to replace your traditional ATM card, but remember to tell them to limit your buying power to the cash balance in your account. Also check to make sure what protections exist on that card if it is lost or stolen and if they will forgive the balance in the event of the cardholder's death. Be aware that some banks freeze your underlying checking account for your debit card until a disputed item from a stolen card is resolved.

Live off lists: Yes, everyone makes shopping lists from time to time so they don't forget to bring home milk and bananas. But the advantage of making very detailed shopping lists for everything – preferably on one page --- is that it's really a good way to keep impulse spending down. If, for example, you have a week of unexpected expenses (car repair, home repair, unexpected fees for your child at school), you can see what real priority items are and what you might be able to do without.

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Set a schedule for checking your credit report: This is not so much a spending issue as a way to monitor the ongoing safety of your accounts and your borrowing status. You have three credit reports to check – TransUnion, Equifax and Experian – and you have the right to get all three of these for free once a year. The best way to do this is to request each report at staggered points during the year at annualcreditreport.com, which is the only guaranteed free site to order these reports (if any credit report site requests a credit card number before it surrenders a report, chances are good that you'll be paying for that "free" report). Why stagger your reports? Because the same information travels between each agency and if there is an error or security breach, you may catch it faster if you're checking throughout the year rather than at one time only.

Comparison shop at your desk: Shopping online has its own risks – paying expensive shipping fees and overspending with a simple click among them -- but using the Internet to browse and compare prices can save time, gasoline and money. Websites like eBay, Amazon, mySimon.com or cheapuncle.com can help you determine general price ranges for gifts you need that are sold online. Once you have those ranges, get on the phone and determine whether you can buy the same items more affordably at retailers close to home.

Don't shop without coupons and discount codes: You don't have to buy a newspaper to get coupons anymore. If you know particular stores where you'll shop, sign up for their e-mail lists – you'll start receiving coupons and news of specials on a regular basis. Ditto for particular products you buy on a regular basis – go to the manufacturer's website and see if you can sign up for regular discounts online and in the mail. Also, if you do shop online, sites like BradsDeals.com and CouponCabin.com have promotional codes that you can type in for discounts before you hit the "total" button on an order – most often, these codes will buy free shipping, but they might also buy additional discounts on an order. Never complete an online order without searching for a promotional code.

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