



BANKRUPTCY BASICS:

A GUIDE FOR EMPLOYEES WHOSE EMPLOYER FILES FOR BANKRUPTCY

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Introduction

The filing of a Chapter 7 or Chapter 11 bankruptcy case by an employer can have devastating consequences for its employees. It can mean not only the loss of a job but the loss of pay and benefits that have been earned by the employees. While employees are not helpless in these situations, it is important that they act promptly in order to try and protect their rights.

This guide will provide some direction to employees on what steps they should take in order to protect their rights if their employer files. Employees are entitled to file claims against the debtor company for unpaid wages, salaries, commissions, vacation, sick and severance pay, as well as benefits owed. This is not a step-by-step guide on every aspect of the bankruptcy process. However, it will provide general information needed to help employees make an informed decision on how to proceed when their employer files bankruptcy. Business bankruptcy law and procedure is complex and while it is possible for an individual to proceed on his or her own, it is always better to consult an attorney familiar with bankruptcy laws and procedures. Unionized employees should consult with their union representatives.

The information contained in this guide applies primarily to people living in New York State. Residents of any other state should consult with legal advisors familiar with the laws of that state since applicable laws and procedures may vary.

Case Information

When an employer (referred to in this Guide as the company or the employer) files for bankruptcy, its employees are likely to receive a "Notice of Filing" from the bankruptcy court which contains important information about the case. The employer (now known as the Debtor) is required to list in its petition and schedules all of its creditors, including its employees. The Notice of Filing is sent to all of the employer's creditors, including employees. No matter how an employee learns about the bankruptcy, even by word-of-mouth, the employee should immediately request information about the case.

The Notice of Filing provides several important pieces of information:

- (1) the company's (Debtor's) name.
- (2) the bankruptcy case number.
- (3) the name and location of the bankruptcy court in which the company filed its case (for example, the US Bankruptcy Court for the Southern District of New York).

- (4) the type of bankruptcy filed: a liquidation under Chapter 7 or a reorganization under Chapter 11. The impact an employer's bankruptcy will have on the employees depends on the type of bankruptcy filed.

Chapter 7

In a Chapter 7 bankruptcy or "liquidation," the company ceases all operations and goes out of business. Employees are laid off, and those who are owed wages and benefits become creditors. A "case trustee" is appointed to liquidate (sell or otherwise reduce to cash) all of the company's assets and property and review the claims filed by the company's creditors. The trustee uses the cash that the company has, money generated by the sale of the assets and the proceeds of any litigation begun on behalf of the company, to pay the costs of administering the case and then, to the extent funds are available, make distribution payments to creditors with approved or allowed claims, including employees with unpaid wages and benefits, in the order of priority established in the Bankruptcy Code. Secured claims are paid first, then the expenses of administering the bankruptcy, then priority unsecured claims, which may include all or a portion of employee wage and benefit claims and, finally, general unsecured claims. The administration of a Chapter 7 case can take many months or even years to complete. Since the employer goes out of business, laid off employees should promptly begin to apply for temporary benefits, such as unemployment insurance, and seek new employment.

Chapter 11

In a Chapter 11 bankruptcy or "reorganization," the employer remains in business and tries to reorganize and emerge from bankruptcy as a financially sound company. Many employees may remain at work and continue to be paid and receive benefits. However, some may be laid off. If the laid-off employees are owed wages and benefits they become creditors of the company. The company's management typically stays in control, but it must obtain the bankruptcy court's approval for nearly all significant business decisions. If the employees are unionized and there is a collective bargaining agreement with the employer, the employer cannot modify the terms and conditions of their employment without bankruptcy court approval. In many cases, the United States Trustee appoints an official committee of unsecured creditors, which typically includes a cross-section of the largest creditors in the case. Committee members may include trade creditors, bondholders or other institutional creditors of the company and, if some of the company's employees are unionized, the employees' union or union pension and benefit funds. The committee represents the interests of all unsecured creditors and serves as another check on the company's conduct and decisions during the bankruptcy case.

The goal of Chapter 11 is for the company to take steps during the bankruptcy to turn itself around financially, for example, by selling assets and closing business locations, and then confirm a plan of reorganization that permits the company to emerge from bankruptcy with restructured debts and a financially healthy business. Creditors are given the opportunity to vote on the company's plan before the court considers its confirmation. Under certain

circumstances, the creditors' committee or even individual creditors may also propose competing plans if they do not agree with the company's plan proposal. If it becomes clear that the company will not be able to confirm a plan of reorganization, the company may propose a plan of liquidation or convert the case to Chapter 7. Like Chapter 7 cases, Chapter 11 cases can take many months or years or to resolve.

Employee claims for pre-bankruptcy wages, salaries, and vacation, sick and severance pay, as well as unpaid contributions by the employer to employee benefit plans, are given priority over other unsecured claims up to a maximum of \$12,475 per employee. The maximum per employee is adjusted for inflation every three years. In order to be confirmed by the bankruptcy court, the employer's plan of reorganization or liquidation must provide for the full payment of employee priority claims. At the beginning of a Chapter 11 case, if the employer has filed Chapter 11 in the middle of a pay period, the court usually uses the employee wage and benefit priority as a basis to give the employer authority to make certain that all wages and benefits relating to that pay period are promptly paid.

The Automatic Stay

The automatic stay is a statutory injunction that goes into effect as soon as the company files its bankruptcy petition. With certain limited exceptions, the automatic stay prevents creditors from taking any action to collect debts or filing lawsuits against the company. The automatic stay is intended to give the company a reasonable amount of breathing space to get its affairs in order, benefitting all parties with an interest in the company's successful turnaround. The filing of a Proof of Claim with the bankruptcy court or the company's bankruptcy claims agent by an employee for unpaid wages, salaries and benefits does not violate the automatic stay.

Filing a Proof of Claim

Employees who are owed wages, salaries, commissions, vacation pay, sick pay, severance pay or other benefits must promptly complete, sign and timely file a Proof of Claim form with the bankruptcy court where the case is pending or the company's claims agent to ensure that they will be eligible to participate in any distribution to creditors made under the terms of the company's plan.

The following information is needed to complete a Proof of Claim form:

- (1) the company's name;
- (2) the bankruptcy case number;
- (3) the location of the bankruptcy court in which the company filed its case;
- (4) the amount owed; and
- (5) any documents supporting the claim and showing how much is owed.

The most important step is to file a properly completed Proof of Claim form. If no proof of claim is filed, the employee may well lose the right to participate in the distributions

(payments) to creditors. (An employee is not required to file a proof of claim if the employee agrees with the amount listed for him/her in the company's schedules of assets and liabilities and that correct amount is not listed as disputed, contingent or unliquidated.) A claim is timely so long as it is filed before the deadline for filing proofs of claim, known as the "bar date." In a Chapter 11 case the proof of claim bar date is set by order of the bankruptcy court. The company is required to provide advance notice of the bar date to all known creditors with instructions on how, where and by when to file the proof of claim. In a Chapter 7 case, the claims bar date is 90 days after the first date set for the statutory meeting of creditors under the Bankruptcy Code. The Chapter 7 bar date is included in a notice from the court that includes the announcement of the filing of the Chapter 7 case and other information. The notice will include specific instructions for filing claims. Employees should not hesitate to contact the company's bankruptcy attorneys, the company's claims agent (if a Chapter 11 and the company has retained one; contact information for the agent will be on the bar date notice), the creditors' committee attorney (if a committee has been appointed) or employee's union representatives with any questions concerning filing their claims. Unions often file claims for wages and benefits on behalf of its member employees.

The official Proof of Claim form (410) is available on the United States Courts website:

<http://www.uscourts.gov/forms/bankruptcy-forms/proof-claim-0>

Employee Wage and Benefit Claims

When a company files for bankruptcy the pre-bankruptcy claims of its creditors are assigned different levels of priority depending on the nature of the debts. Employee wage and benefit claims are generally listed as "priority" unsecured debts. As a priority unsecured debt, it will be paid ahead of general unsecured debts (debts that have no statutory priority and are not secured by collateral), but after secured debts (debts secured by collateral such as real property) and the expenses of administering the case, including in a Chapter 11 case the expenses of doing business during the case. The Bankruptcy Code provides this priority status to claims for unpaid hourly wages, salaries, commissions, vacation, severance, and sick leave pay, if earned within 180 days of the company's bankruptcy filing or when the company ceased operating its business, whichever is earlier, up to \$12,475.00 per employee who files a claim. This amount is adjusted upward for inflation every three years, with the next adjustment due in early 2016. Claims for wages and benefits which were not earned within the time frame or exceed the dollar maximum are treated as general unsecured claims and do not have priority status.

Similarly, the Bankruptcy Code provides priority to claims for unpaid contributions to an employee benefit plan, such as a pension plan, earned within 180 days of the company's bankruptcy filing or when the company ceased operating its business, whichever is earlier, but only up to \$12,475.00 for each employee less other amounts that have already been paid to the employee for priority wages and benefits and for claims for contributions to other employee benefit plans. This \$12,475 maximum priority amount will also be adjusted for inflation early in 2016.

Wages, salaries, commissions, paid time off and benefits earned after the bankruptcy case is filed, to the extent unpaid, are administrative expense claims.

WARN Act Claims

The Workers Adjustment and Retraining Notification (WARN) Act mandates that larger employers (those with 100 or more employees) give 60 days' advanced notice of plant closings or mass layoffs. While there are exceptions to this requirement, if an employer fails to give the required notice then affected employees will be entitled to an additional claim for back pay and benefits for the number of days for which the required notice was not given. The failure to give notice and the employee's claims for back pay and benefits will become an issue in the bankruptcy case. Claims under the WARN Act (and under parallel state laws) are complex and are likely to be challenged.

New York State has a parallel statute which applies to employers with 50 or more employees and requires 90 days' notice of closings or mass layoffs, with exceptions. Employees who believe they may have WARN Act or claims under the New York (or other state) statute should consult and retain an experienced bankruptcy attorney.

Health Plans

The impact of a company's bankruptcy filing on health insurance plans varies in each case. The employee should immediately contact the administrator of the health plan or his or her union representatives to find out the following information:

- Will any benefits due to employees as of the bankruptcy filing date be paid? When?
- Will the health insurance plan continue or be terminated?
- Who will be administering the plan during the bankruptcy?
- Will COBRA continuation coverage be offered to employees who lose health plan coverage?
- If the health plan is to be terminated, how will outstanding health claims be paid?

If an employee is laid off but the company maintains its existing health insurance coverage the employee may be able to continue receiving coverage under the existing policy by seeking coverage under COBRA (Consolidated Omnibus Budget Reconciliation Act). This can be an expensive option. If the employee is married and the spouse is covered under a separate employer health insurance plan, the employee may want to see if he/she can convert to coverage under the spouse's plan. If the company terminates some, but not all, of its health coverage plans, an employee may be able to switch to one of the remaining plans under HIPAA (Health Insurance Portability Accountability Act). Employees should contact the New York State Dept of Health (www.health.ny.gov/health-care) to see what health insurance benefits they

may qualify for. If the company terminates all of its health insurance plans COBRA continuation coverage will not be available. The employee may have to apply for separate coverage under the Affordable Care Act or Medicaid. Information can be obtained about these options from the U.S. Department of Labor's Employee Benefits Security Administration (EBSA) at www.askebsa.dol.gov or call their **Hotline at 1-866-444-EBSA(3272)**.

Retirement Plans

Often, the assets of the retirement plans are held and administered separate and apart from the employer's assets and may not be used to pay the employer's creditors, or are insured by third-party entities not involved in the company's bankruptcy case. The assets of these plans will not be affected by the bankruptcy. However, while the retirement plan assets may be separate from the assets of the employer, the pension plan may not have enough assets to pay the benefits vested and due to be paid over time as employees retire. The pension plan, in that event, will have claims against the employer in bankruptcy for the amount of the underfunding (as well as for any unpaid contributions to the plan owed by the employer). The vested pension benefits of unionized employees in a multi-employer pension plan should not be at risk in their employer's bankruptcy.

401(k) plan assets are also held and administered separate and apart from the employer's assets and may not be used to pay the employer's creditors. However, the employee will need to file a proof of claim or take other steps if the employer has failed to pay to the 401(k) plan the employee's and/or the employer's share of any contributions due.

In any event, employees should immediately contact the health and pension plan administrators or union representatives about the status of their health, pension, retirement plans, and any other benefits. Employees should carefully follow the notices they receive from the bankruptcy court or the company to stay informed as the case progresses.

The U.S. Department of Labor's Employee Benefits Security Administration (EBSA) administers the Employee's Retirement Income Security Act (ERISA), which oversees retirement plans (including 401(k) plans) and welfare plans (such as health, disability, and life insurance plans). See the contact information for EBSA above.

If an employee's retirement plan is a defined benefit pension plan, some or all, of the plan's retirement benefits may be insured by the Pension Benefit Guarantee Corporation (PBGC) in Washington, DC. **1-800-400-7242**. If a pension is terminated due to the bankruptcy, the PBGC can take over the plan and pay out the employees' pensions up to certain limits.

Additional Resources

There are other resources an employee can look to if they have not been paid or have been laid off by an employer.

- *Retirement or pension plan.* Your retirement plan or benefits may be insured by the Pension Benefit Guaranty Corporation. You can contact them at: **Pension Benefit Guaranty Corporation**, Processing and Technical Assistance Branch 1200 K Street, NW Washington, DC 20005 Phone: (800) 400-7242
- *Unemployment Insurance.* A laid-off employee may be eligible for such benefits after the passage of a brief period of time. Go to the **New York State Department of Labor** website at www.labor.ny.gov for detailed information on how to apply.
- *Medicaid, Food Stamps (SNAP) and Cash and Rental Assistance.* A laid off employee may be eligible for some or all of this type of assistance. Go to the website for the **NYC Human Resources Administration** at www.nyc.gov/site/hra/help or call the HRA Info Line at **718-557-1399**.
- *Other city services.* NYC 311 is the official Website of the City of New York for additional information about the services offered by the various city agencies. Or call **311** directly.
- *Social Security Administration.* Depending on various circumstances a laid off employee may be entitled to retirement or other social security benefits They can contact their local **Social Security Office** or go to www.ssa.gov.
- *Bankruptcy Court Locations.*
 - **US Bankruptcy Court Southern District of New York** (for Manhattan, Bronx, Westchester, and several other upstate counties), One Bowling Green New York, NY 10004-1408. www.nysb.uscourts.gov or call (212) 668-2870.
 - **U.S. Bankruptcy Court Eastern District of N.Y.** (for Staten Island, Brooklyn, Queens, Nassau and Suffolk Counties), 271-C Cadman Plaza East, Brooklyn, NY 11201-1800. www.nyeb.uscourts.gov or call (347) 394-1700, press 6.
- *To Find Legal Help.*
 - **City Bar Justice Center** Legal Hotline 212-626-7383.
 - **New York City Bar Legal Referral Service** 212-626-7373.