You've Been Laid Off. Now What?

Lost your job in this economy—or afraid you will? Follow these four steps to keep your finances afloat

By Kate Ashford

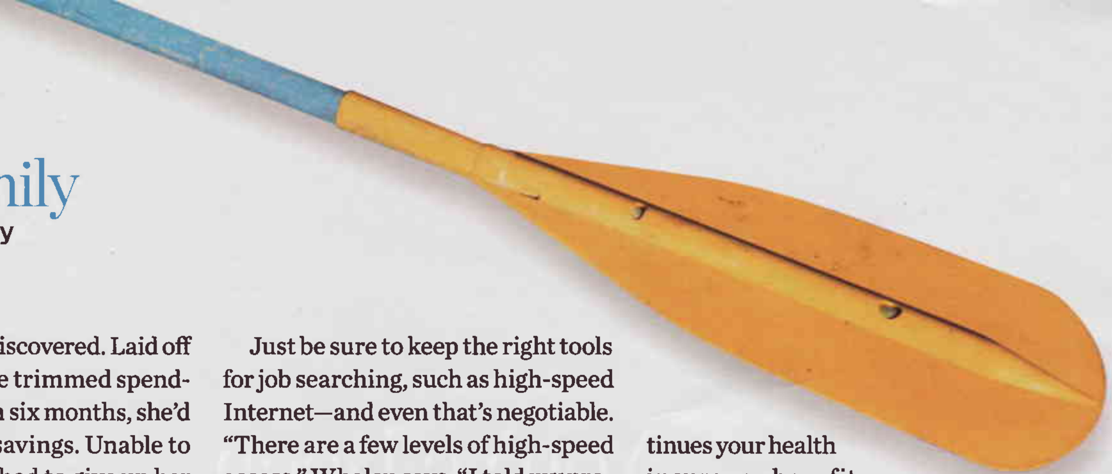
Photograph by Joseph Devenney/Getty Images

Maybe you've recently gotten the pink slip at work—or you fear you might be next: You are not as alone as you might feel; over 660,000 people lost their jobs in March alone. And since the economy isn't yet on the rebound, many of the newly unemployed are feeling stranded, with no prospects for a new paycheck. Financially speaking, cutting back on lattes isn't going to do the trick.

While times are tough, you can get through them if you make the right moves—knowing, say, when to cash in your 401(k) and when not to, and how to find discounted health insurance. Here, the latest, smartest strategies so you can keep your head above water.

OLD THINKING Cut back on eating out
NEW THINKING Cut back on everything

If you never had trouble finding employment in the past, you may not take a hatchet to your expenses the moment you lose your job. But in this economy, you'll want to rethink that. →



as Carla Milo, 34, discovered. Laid off in March 2008, she trimmed spending a bit, but within six months, she'd gone through her savings. Unable to pay her rent, Milo had to give up her Brooklyn apartment and move in with a friend in Texas, where she remained at press time. "Now I see I shouldn't have spent money unless I absolutely had to, right from the start," she says.

Do overhaul your expenses immediately after a layoff. "There are things people have never had to live without; they may not know basics from luxuries," says Susan Brown, a certified financial planner in Boston. "Cutting back requires fresh thinking." This isn't about signing up for a cheaper long-distance plan—it's about jettisoning your home phone. "Instead of $50 a month for a landline," says Don Whalen, a certified financial planner in Alpharetta, GA, "couldn't you use your cell phone?"

Think about it this way: If it doesn't feed you, keep you insured, or keep a roof over your head, you can probably live without it, at least for now. Shop around for home, auto, and life insurance to see if you can find a better deal. Cut back on your teenager's unlimited cell plan. Maybe you can drop your cable package and newspaper subscriptions; instead, get your TV fix from free sites such as hulu.com, and get your news from the Web, too. "If you save $60 a month here, $100 a month there, that will really add up," says Dylan Ross, a certified financial planner in East Windsor, NJ. "You'll be able to afford necessities for longer."

If it doesn't feed you, insure you, or keep a roof over you, maybe you can do without it

Just be sure to keep the right tools for job searching, such as high-speed Internet—and even that's negotiable. "There are a few levels of high-speed access," Whalen says. "I told my provider to reduce my service a notch. We now pay $19 a month, not $40, and haven't noticed a difference."

If you're really struggling, it's time to rethink bigger-ticket items. Maybe you don't need a second car—or perhaps "if you can't pay the mortgage, you aren't able to negotiate with your lender, and job prospects are grim, it's time to sell the house," says Ted Toal, a financial planner in Annapolis, MD. It's a drastic step, but if you're facing foreclosure, it's your best bet.

- **Who can help** If you've slashed expenses and are worried about staying afloat, talk to a counselor approved by HUD (U.S. Department of Housing and Urban Development); find one at hud.gov, or try the National Foundation for Credit Counseling (800-388-2227 or debtadvice.org).
- **Employed but worried** Fine-tune your withholding. Ask your HR department how to reduce your withholding a bit to boost your paychecks; sock the extra into a savings account. If you keep your job, use it to pay taxes. If you are laid off, you'll owe less in taxes anyway (since you'll be in a lower income bracket), so you can use this surplus for necessities.

OLD THINKING Sign up for COBRA, but find a cheaper plan ASAP
NEW THINKING Sign up for COBRA for at least nine months

When you've lost a job with a group health insurance plan, COBRA continues your health insurance benefits—but at full cost, plus a 2 percent administrative fee. A recent Families USA study found the average COBRA premium for family coverage is a whopping $1,069 per month. Since the average unemployment compensation is $1,278 per month, that doesn't leave any breathing room.

However, thanks to the stimulus package passed in February, if you've been laid off, you only have to pay 35 percent of the cost of COBRA health benefits for nine months—the government will pay the rest. It's not a forever fix, however, and it doesn't apply to everyone. To qualify, you must have been laid off between September 1, 2008, and the end of this year (if you declined COBRA initially, you may be able to jump back onto the plan retroactively to March 1, 2009), and the benefit starts to phase out sooner for former high-income earners. You also won't meet the criteria if you're eligible for coverage elsewhere—for instance, through your spouse's employer. Your former employer's HR rep can help you with all the necessary details. (Obviously, if your spouse is employed and has health insurance, join that—losing a job is considered a life event, so there's no need to wait until open enrollment.)

If you're still job-hunting after the nine months of subsidized COBRA coverage, or you were laid off prior to the cutoff date, you'll want to shop for cheaper insurance. Shannon,* 41, lost her job in October and quickly realized that it was going to cost $850 a month for basic medical coverage →

Photograph by Blend Image Photography/Veer

*Last names have been omitted to protect privacy.

for herself and her two children on COBRA. She found a plan for $380 a month—a savings of nearly $500.

One warning: If money's tight, you may be tempted to jettison comprehensive coverage in favor of hospitalization only. Don't: Hospitalization covers only that—the cost of being hospitalized. "If you need a procedure, there's so much outpatient prep work that's going to be done—lab work, MRIs," says Larry S. Harrison, a health insurance broker in Las Vegas. "You could have $150,000 worth of outpatient therapies." Instead, get a high-deductible plan, which offers lower premiums and covers medical expenses over an out-of-pocket amount (which you'll need to have on hand). Be sure you are not buying an indemnity plan or a discount medical plan but actual major medical insurance with a cap of at least $1 million, advises Whalen.

- **Who can help** While online comparison sites, such as ehealthinsurance.com, can provide a good overview, don't rely on them exclusively. "Find a good health insurance broker," Whalen says. "With a Web site, you do all the work and get no advice, and with an individual, they do all the work and you get to benefit from their expertise." (Brokers receive their commission from the insurers, not from you.) Word of mouth is the best reference, or your financial advisor may be able to refer you. Or try the Web site of the National Association of Health Underwriters, nahu.org; look for a broker who represents a broad array of carriers.
- **Other money-saving options** Check your state insurance department (find yours at naic.org) for lower-cost programs, especially if your income has dropped dramatically. Or visit the NAIC site for consumer info, insureuonline.org.
- **Employed but worried** Make sure your whole family schedules medical and dental checkups while you're still covered under your employer's health insurance plan.

OLD THINKING Tapping retirement funds should be a last resort
NEW THINKING If you're forced to do so, tap the Roth IRA first

If you've been a model citizen, you have at least six months of living expenses squirreled away. But only 39 percent of Americans have enough cash stashed to cover even three months, according to bankrate.com. Nikki Maxwell, 40, of North Hills, CA, knows that only too well, after she and her husband were both laid off—he for six months in 2008, and she starting last September. "We buzzed through our savings and retirement funds," she says. "There's no safety net at this point."

When you're short on cash, make sure you've looked everywhere before you touch your retirement funds. That means college savings for your kids, and taxable brokerage accounts. If you must tap your retirement accounts, access them in a way that will minimize the pain. If you have a Roth IRA, you can take out the amount you contributed penalty- and tax-free, since it was post-tax money to begin with. If, however, you have a traditional IRA, you'll most likely owe taxes on any money you withdraw. But you can avoid the 10 percent early-distribution penalty if you pull out funds to pay health insurance premiums after receiving unemployment benefits for at least twelve weeks, or for higher-education expenses. You can also take out up to $10,000 penalty-free for a first-time home purchase (meaning you haven't owned a home in at least two years), and there's also some penalty relief if you use the money to pay certain medical bills (go to irs.gov or call the IRS at 800-829-3676 and request publication 590 for more info). If you have a 401(k), after leaving your job, you can roll it into a traditional IRA; if you make withdrawals, the same taxes, penalties, and exceptions will hold true.

Perhaps none of these scenarios applies, and you're not yet 59½ years old. In that case, you'll pay taxes and a 10 percent early-distribution penalty for any taxable IRA withdrawals you make, so do the right math. Withdraw enough to cover the taxes you'll owe in April, plus the 10 percent penalty, plus your actual cash needs. Translation: You'll be taking a big hit; be sure you really need the money.

After a layoff, you may have to pay only 35% of COBRA premiums for the next 9 months

- **Employed but worried** Now, when you still have a steady source of income, is the time to apply for a home equity line of credit (HELOC). Look for a bank that doesn't charge an application fee or an annual fee. Get quotes from a few different institutions (try bankingmyway.com and bankrate.com for leads), as well as a mortgage broker—and check with your local credit unions, which may well offer better rates (see creditunion.coop for details). When you get the HELOC, access it only in case of →

emergency; don't let it become another debt zone.

OLD THINKING Put your credit cards away—period
NEW THINKING Get a 0 percent-interest card and use it responsibly
Credit cards can be a handy tool when you don't get a paycheck every two weeks, but it's easy to charge yourself into a black hole of debt. Jocelyn,* 37, knows that scenario firsthand: She was laid off in 2004 and ended up living on plastic to make ends meet. "I figured, in six months I'll have a job," she says. "It didn't turn out that way. I wound up with big balances on my credit cards—and I'm still carrying them."

That said, if you truly need credit to pay for the essentials (groceries, not movie tickets), apply for a credit card offering the longest 0 percent-interest introductory period you can find. Look for low-interest cards on bankrate.com—many offer six to 12 months at 0 percent interest. When applying, include your spouse's income, any severance, child support, the salary you received before the layoff, and expected unemployment payments. (Or have your employed spouse apply, if possible.) Then use the card only for true necessities, such as a burst pipe in the basement. Remember, when the introductory rate runs out, you'll have to pay interest on everything you buy–and that can add up quickly.

Given that 46 percent of credit card–holding families carry a balance, you're probably not starting from square one. If it's already hard to pay the minimums on other credit cards, you may be able to transfer the balance to a 0 percent–interest card. (Many cards charge a fee of 3 percent or so on balance transfers.)

- **Who can help** If you can't get a 0 percent rate, call your credit card's customer service line and say, "I'd like to request a lower rate [or, if you can't pay the minimum, a workout agreement]." Explain that you've lost your job, you've filed for unemployment, and you'd like the company to reduce your interest rate. If you aren't satisfied with the answer you get, ask to speak with a supervisor. Say that the last thing you want is to make a late payment or skip one.

  Know that settling your debt for less than you owe can hurt your credit. As an alternative, you can ask to have your monthly payments lowered or stopped for a few months to allow you to catch up. "Before committing to a plan, ask if and how it will be reported to the credit agencies," advises Gail Cunningham of the National Foundation for Credit Counseling, an umbrella organization of legitimate credit counseling services (call 800-388-2227 to be connected to one in your area). "If you don't like what you hear, you can simply say, 'No, thanks' to their offer and pursue any other options you may have."

- **Employed but worried** Check your credit score, in case you do land in the unemployment line. Potential employers will probably check your credit during the application process. Make sure your report has no errors by getting a free copy from annualcreditreport.com. Also know that any credit card minimum payments and interest are going to be an even bigger burden if you lose your paycheck. Make it a priority to pay down any balances as much as you can now, so you'll be in the best shape possible for the current economy. ■