

# Prioritizing Debt: Which bills do I pay first?

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## Credit Problems

Nearly everyone at one time or another has faced a problem with a creditor – e.g., the IRS, a credit card company or hospital. Often times, while individuals have money to pay some of their bills, they do not have enough to pay them all. Individuals in this position may find it difficult to know which bills to pay first.

This publication will define the different general types of debt you may have and then help you prioritize and determine which debts to pay first. Please note that this publication merely provides general advice. If you face serious debt issues, you should consult other resources, including an attorney. (The end of this publication contains information concerning helpful resources in this area.)

## Types of Creditors

When it comes to one's use of limited resources, the reality is that the basics, or "necessities," should be given priority. For example, someone most logically would choose to use their last dollar to pay for food or shelter, rather than for luxuries such as jewelry.

In addition to the idea of necessities, it can be very helpful in debt prioritizing to understand the different types of debt, and thus creditors that exist.

### Unsecured vs. Secured Creditors

A creditor is a person to whom you owe money. A creditor could be almost any entity – ranging from the government (the IRS concerning taxes; the local court concerning traffic or parking fines); credit card companies; local retailers (an appliance store); medical providers (doctors, dentists,

hospitals); or a collection agency collecting debt originally owed to another.

- **Unsecured Creditors** are those creditors that have either loaned you money or agreed to sell you something based solely on your promise to repay them under certain terms or conditions.
- **Secured Creditors** are creditors who agree to sell you something or give you a loan in exchange for your promise to repay PLUS the provision of some type of "collateral" as a guarantee. The collateral could be anything from a piece of furniture, your car, or your bank account, and often includes the property you purchased. Consequently, when collateral is involved, the creditor is entitled to take or repossess that collateral IF (and ONLY IF) you violate the terms of the contract (e.g., fail to make payments as required).

### Home Foreclosure and Eviction

Home foreclosure and eviction are two special instances of debt collection. If you fail to make your house payments, the creditor can foreclose on your home. This means that the creditor will be able to sell the home and you will have to leave. Similarly, a landlord can evict you if you do not pay rent and lack a valid defense. As in other instances, if someone is attempting to foreclose on your home or evict you, consult with an attorney.

### **Debt Prioritization**

As is evident from the above, the type of debt/creditor at issue can help determine which debt should be given priority. Simply put, payment of secured creditors should

generally be given priority over unsecured creditors for the simple reason that secured creditors can more easily and quickly take your property away to satisfy a debt. Moreover, payment of certain secured creditors should generally be given priority over other secured creditors based on the collateral or risks involved.

The checklist below attempts to incorporate the ideas discussed above in outlining an approach for debt prioritization.

### **Debt Priority Checklist**

**1. Always pay family necessities first.**

Usually this means food and essential medical expenses. You may want to look for ways to keep these expenses to a minimum.

**2. Next pay your housing-related bills.**

Keep up your mortgage or rent payments if at all possible. If you own your home, real estate taxes and insurance must also be paid unless they are included in the monthly mortgage payment. Similarly, any condo fees or mobile home lot payments should be considered a high priority. Failure to pay these debts can lead to loss of your home.

If you are having very serious problems that require you to move to a cheaper residence, you might choose to stop paying the mortgage or rent. Obviously, consultation with an attorney is highly advisable under these circumstances. However, if you choose to do so, you should not use that money to pay other debts, but rather save it as a fund to use for moving.

**3. Pay what you must to keep essential utility service.** While this may not always require full payment (such as during a winter moratorium on disconnections – see our publication "Public Utilities"), whatever payments are necessary

should be made whenever possible. Working hard to keep your house or apartment makes little sense if it is not livable because you have no utilities.

**4. Pay car loans or leases next if you really need your car.** If you need your car to get to work or for other essential transportation, you will usually make your car loan or lease payments next after food, housing costs, medical expenses, and utilities. You may even want to pay for the car first if the car is essential to holding onto your job.

If you do keep the car, it is important to stay current on your insurance payments as well. Otherwise, the creditor may buy for you at your expense even more costly collision and theft insurance that may give you much less protection. (In Washington State, it is illegal to not have automobile liability coverage.) If you can do without your car or one of your cars, you not only save on car payments, but you also save on gasoline, repairs, and insurance.

**5. You must pay child support debts.** These debts will not go away and can have serious consequences if not paid – including prison for nonpayment.

**6. Income tax debts are also high priority.** You must pay any income taxes you owe that are not automatically deducted from your wages. You must also file your federal income tax return, even if you cannot afford to pay any balance due. The government has many rights which other creditors do not have, particularly if you do not file your tax return. Remember, if you have lost income due to a change of circumstances, your tax obligations

will also be reduced. Pay only what is necessary.

(Also, if you are involved in a tax dispute with the IRS, you should call CLEAR at 1-888-201-1014 to find out more information on your rights and local low-income taxpayer clinics that may be able to assist you.)

7. **Loans without collateral are low priority.** Most credit card debts, attorney, doctor and hospital bills and other debts to professionals, open accounts with merchants and similar debts are low priority. You have not pledged any collateral for these loans, and there is rarely anything that these creditors can do to hurt you in the short-term.
8. **Loans with only household goods collateral are also low priority.** Occasionally a creditor requires you to put some of your household goods up as collateral on a loan. You should generally treat this loan the same as an unsecured debt and a low priority. Creditors rarely seize household goods because they have little market value, it is hard to seize them without court process, and it is time-consuming and expensive to use a court process to seize them.
9. **Do not move a debt up in priority in response to a creditor threatening suit.** Many threats to sue are not carried out. Even if the creditor does sue, it will take a while for the collector to be able to reach your property, bank account, or wages, and much of your property may be exempt from seizure. On the other hand, non-payment of rent, mortgage, and car debts may result in immediate loss of your home or car. (See our publications "[Debtor's Rights in a Lawsuit](#)" and "[How to](#)

[Answer a Lawsuit for Debt Collection.](#)")

10. **Do not pay when you have good legal defenses for repayment.** Some examples of legal defenses are that goods purchased were defective, or that the creditor is asking for more money than it is entitled to. If you have a legal defense, you should obtain legal advice to determine whether your defense will succeed. In evaluating these options, remember that it is especially dangerous to withhold mortgage or rent payments without legal advice. However, for all other debts you should consider fighting back when you have a valid defense.
11. **Court judgments against you should be taken seriously.** After a collector obtains a court judgment, that debt often should move up in priority because the creditor can enforce that judgment by asking the court to seize your property, or garnish your wages and/or bank account. Nevertheless, the seriousness of a threat depends on the applicable law, the value of your property, and your income. It may be that all of your property and wages are protected under state law, and then you should still pay this debt only after more pressing obligations.
12. **Student loans are medium priority debts.** Student loans should generally be paid ahead of low priority debts, but after top priority debts. Most delinquent student loans are backed by the United States and federal law provides special collection remedies against you that other creditors do not have, such as seizure of your tax refunds and denying you new student loans and grants. (See our publication "[What](#)

[Can I Do About a Defaulted Student Loan?](#)”) For some government student loans or debts, the Department of Education may attempt to garnish a portion of your government benefits to satisfy the debt. If this happens, you should consult with an attorney immediately as there are rules that limit the amount that may be garnished.

**13. Debt collection efforts should *never* move up a debt's priority.** Be polite to the collector, but make your own choices about which debts to pay based on what is best for your family. Debt collectors are unlikely to give you good advice and may be most aggressive to get you to pay debts that you should actually pay last. Moreover, you can easily stop debt collection contacts and you have legal remedies to deal with collection harassment. (See our publication "[Debtor's Rights – Collection Agencies.](#)")

**14. Threats to ruin your credit record should *never* move up a debt's priority.** In many cases, when a collector threatens to report your delinquency to a credit bureau, the creditor has already provided the credit bureau with the exact status of the account. And if the creditor has not done so, a collector hired by the creditor is very unlikely to do so. In fact, your mortgage lender, your car creditor, and other big creditors are much more likely to report your delinquency (without any threat) than is a debt collector that threatens you about your credit record.

**15. Co-signed debts should be treated like your other debts.** If you have put up your home or car as collateral on a loan, that is a high priority debt for you if the other co-signers are not keeping the debt current. If you have

not put up such collateral, treat co-signed debts as a lower priority. If others have co-signed for you and you are unable to pay the debt, you should tell your co-signer about your financial problems so that he or she can decide what to do about that debt.

**16. Refinancing is *rarely* the answer – Beware!** You should always be careful about refinancing. It can be very expensive and it can give creditors more opportunities to seize your important assets. For example, by refinancing unsecured credit card debt through a loan where your home is collateral (e.g., second mortgage), you have now put your home at risk if you default on the new loan. Consequently, what amounts to a short-term fix can lead to long-term problems. (See the National Consumer Law Center's (NCLC) publication "[What You Should Know About Refinancing.](#)")<sup>1</sup>

## Garnishment

Garnishment is a powerful tool for creditors who have obtained a court judgment mandating payment of a debt. Garnishment allows these creditors to be paid directly from your income or bank accounts. In Washington State, the law protects certain kinds of income and personal property from garnishment. (See our publication "[How to Claim Personal Property Exemptions.](#)") As in other instances, if someone is attempting to garnish your income or seize your

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<sup>1</sup> The preceding section was excerpted (edited) with permission from National Consumer Law Center (NCLC), *Surviving Debt: A Guide for Consumers* (1999 Third Edition). If you are interested in receiving a copy of this publication, or others provided by NCLC, you may contact them via their website @ [www.consumerlaw.org](http://www.consumerlaw.org) or by phone/mail @ National Consumer Law Center: 18 Tremont Street; Boston, MA; 02108-2336; (617)-523-8089.

property or bank account, you should consult with an attorney.

## **Other Resources**

If you are low-income, additional legal advice is available by calling the Northwest Justice Project's Coordinated Legal

Education and Referral (CLEAR) program @ **1.888.201.1014**. Legal publications covering a broad range of legal topics, including some of those mentioned above, are available online at [www.washingtonlawhelp.org](http://www.washingtonlawhelp.org).

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