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Principal reductions may be paid for by Hardest Hit Fund

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Florida's key foreclosure prevention program may use a portion of its $1 billion to pay down mortgage principal amounts for struggling homeowners, a controversial tactic that critics believe leads more people to default on their loans.

The Florida Housing Finance Corp., which oversees the federally-funded Hardest Hit program, is considering a plan that would reduce mortgage debt on home loans for an estimated 2,000 underwater borrowers as a way to stave off bank repossession.

The plan, as described at a board of directors meeting this month, would partner the corporation with the non-profit National Community Capital group to cut principal balances enough to leave borrowers with 5 percent equity in their home.

National Community Capital is a subsidiary of New Jersey Community Capital, which has purchased hundreds of defaulted Federal Housing Administration loans at a discount through a program announced in June. The program requires loan purchasers _ typically private investors _ to freeze foreclosures for at least six months while trying to work on a loan modification. The company recently bought 249 Tampa-area home loans.

Underwater homeowners whose loans are bought by the company would first have their mortgages reduced to where they owe 15 percent more on the loan than their home is worth. Up to $50,000 in Hardest Hit money would then be used per borrower to get to the 5 percent equity mark.

National Community Capital could make its money back years later by selling the loan on the secondary market.

More details are expected early next year, but nothing will be presented to Florida Housing Corp.'s board until mid-to-late February, said Cecka Green, communications director for the corporation.

Still, homeowner advocates who have been pushing the idea of principal reduction are excited about the proposal. About $50 million in Hardest Hit money would be allocated for the pilot program.

“We feel Florida Housing is doing the right thing and wants to do the right thing,” said Laura Johns, a community organizer with the Home Defenders League, a national organization whose Florida base is in Orlando. “If this is a good program we want to make sure it doesn’t take forever. We really can’t afford to wait for help.”

Announced in 2010, the Hardest Hit program has allocated $7.6 billion to 17 states and the District of Columbia to help homeowners while they look for a job or better-paying employment.

Florida’s program began statewide in April and expects to help 45,000 homeowners by 2017. Currently, homeowners receive Hardest Hit money to supplement their mortgage payments, and make back payments to bring a mortgage current.

As of Dec. 1, 8,094 homeowners were approved for funding and $205.7 million had been spent or allocated.

Johns said she expects there will be opposition to using taxpayer dollars to reduce principal amounts, even though it is one of the most effective ways to keep people in their homes long term.

Last year, Florida Attorney General Pam Bondi joined three other Republican state attorneys general to voice concern over including principal reductions in the $25 billion National Mortgage Settlement, saying it could create a “moral hazard.”

Federal mortgage backers Fannie Mae and Freddie Mac refuse to reduce principal amounts on defaulted loans because it would cost taxpayers money, said Edward DeMarco, acting director of the Federal Housing Finance Agency.

Florida International University real estate professor Ken H. Johnson said he understands people who are paying their mortgage may be angered over principal reductions for defaulted homeowners, but that everyone benefits from fewer foreclosures.

Still, he said the state’s principal reduction plan will only work if the homeowners can afford to pay the reduced mortgage.

“The sentimental choice is to give it to people most financially stressed, but that’s probably not sound for the program,” Johnson said. “If they get the money, and they can’t make the payments, it will just end up back in foreclosure down the line.”