***The Consumer Finance Podcast* –** Illinois Mortgage Foreclosure Shake-Up: Navigating Statute of Limitations Challenges

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Date Aired: September 4, 2025

Chris Willis:

Welcome to *The Consumer Finance Podcast*. I'm Chris Willis, the Co-Leader of Troutman Pepper Locke's Consumer Financial Services Regulatory Practice. Today, we're going to be talking about a very interesting set of developments related to the statute of limitations for mortgage foreclosures in Illinois state courts. But before we jump into that, let me remind you to visit and subscribe to our blogs, TroutmanFinancialServices.com and ConsumerFinancialServicesLawMonitor.com.

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Now, as I said, today, we're going to be talking about an unfolding story in the state of Illinois involving the very important subject of the statute of limitations for mortgage foreclosures. And joining me to talk about that is my colleague, Lou Manetti. Lou is a member of our Consumer Financial Services group in our Chicago office, which makes him very well situated to talk about this issue. So Lou, thanks for being on the podcast today.

Louis Manetti:

Hi, Chris. Thanks for having me.

Chris Willis:

So tell the audience what's going on with respect to the statute of limitations for foreclosures in Illinois.

Louis Manetti:

Right now, there are arguments being made in the Illinois appellate court that could drastically alter settled notions of how long the statute of limitations is for an Illinois mortgage foreclosure, and how it even operates. These arguments have bubbled up from the trial court and they're finally in a place with the Illinois appellate court where you could get some binding precedent, one way or the other. In Illinois as a bit of background, like most states, you have the mortgage loan that involves two distinct documents that kind of work in tandem. You have the mortgage, which establishes the lien interest, and you have the promissory note, which establishes the debt, the amount to be repaid.

You can also, under these two documents, get different remedies. You could have a mortgage foreclosure lawsuit, or you could have a separate lawsuit on the promissory note for money. And it's just generally been accepted in Illinois for years and years that the statute of limitations for foreclosures is 10 years. This hasn't really been disputed or tested in the ways that it has been now, because the statute of limitations for foreclosures sits alongside comfortably, the statute of limitations for recorded written documents and promissory notes. Those are also 10 years.

You had a generalized notion that you have 10 years to file a mortgage foreclosure, and it couldn't really diverge from other notions of statute of limitations for the note. But in the background of all this, is much older case law that holds that a mortgage is a mere incident to the debt, and it's barred when the debt is barred. There are cases from 1895 that express that. One case from 1878, the Illinois Supreme Court said, where an action on the note is barred by the statute of limitations, an action on the mortgage is also barred. So, you have this background notion that's very old, that if the statute of limitations is passed on the note, you're sunk with the mortgage. The mortgage is also barred, and you can't foreclose.

But it's been generally understood that you can't file a foreclosure if the note has passed the statute of limitations. But again, there's really been no point of divergence between what a statute of limitations on a note might be, versus a mortgage. They're both 10 years. That notion is currently being challenged. Let me say, that there was never any dispute that once a timely mortgage foreclosure was filed, you were fine. There was nothing else that could happen that could dislodge the case, or disrupt it, or cause its dismissal, no matter how long it was litigated. That notion is currently being challenged in Illinois courts and again, we're going to get some binding authority soon.

So, there is a growing trend in Illinois foreclosures among borrowers' counsel that they argue that the limitations on a note can cut off the statute of limitations for mortgage foreclosures, even during a timely filed foreclosure case that's being actively litigated. So this is the case. It's currently on appeal. It's the *Bartelstein* case in Cook County, and after nearly 16 years of litigation in Cook County, it was dismissed due to timeliness issues that arose during the case.

So in this case, you had a 2006 mortgage loan, was defaulted, borrowers stopped paying in August of 2007. In December of 2007, the foreclosure complaint was filed and the borrower answered and filed affirmative defenses. Litigation ensued. Litigation dragged on for a very long time with no clear win for either party. No substantive relief. Finally, in December of 2019, so 12 years into this active foreclosure case, the borrower filed a motion for summary judgment. He argued that the note has become unenforceable by operation of law as the result of the expiration of the applicable statute of limitations. So he argued that when the timely mortgage foreclosure, no one disputed that it was timely filed, but when the foreclosure case hit its 10-year birthday, it was subject to dismissal. Because the note was barred by the statute of limitations.

The court issued a very long and thorough memorandum opinion, and it cited those older cases that I mentioned earlier about the mortgage being a mere incident to a debt. And it held that when a promissory note is barred under the statute of limitations, the action on the mortgage is also barred. It characterized the issue in the foreclosure itself as a type of estoppel issue that was operating. And it held that this 16-year-old mortgage foreclosure case needed to be dismissed, because it had gotten so old that no action on the note was possible. So the action on the mortgage couldn't keep going. It had to be dismissed.

Chris Willis:

Lou, this seems like kind of a gotcha for the creditor in the case, because there's no dispute that the creditor filed a foreclosure action well within the statute of limitations for the note. And one would assume the foreclosure action was based on allegations that the borrower had not paid the note and therefore, foreclosure was appropriate. So like was there any discussion of, could the lender just amend its complaint and say, “Hey, I'm also suing on the note?”

Louis Manetti:

The court pointed that out. Yes. And yes, it did come as quite a shock to the lender during this case, that its active and litigated case for 16 years could just be subject to dismissal, because of the note. The court in its trial level opinion said, “You could have avoided this lender plaintiff by bringing another count for action on the note.” So it was a one count foreclosure, just for foreclosure. You could have brought a count under the promissory note or you could have obtained judgment during the 10 years. Because under Illinois law, when you get a judgment of foreclosure, the loan documents merge into the judgment. The only operative document at that point is the judgment. So the court said, if you had done either of those two things before the expiration of 10 years, you would have been safe. But you didn't and now your foreclosure is vulnerable.

Chris Willis:

Okay. So that case is currently on appeal.

Louis Manetti:

Correct.

Chris Willis:

There's another one too, though, isn't there?

Louis Manetti:

There is. The *Bartelstein* case is currently being briefed, and we'll get some direction on that from the appellate court. There's another case, the *Zbroszczyk* case. They approached this issue from a slightly different angle. They considered whether the life of the note could have consequences for a mortgage foreclosure lawsuit, even though foreclosures have their own 10-year statute of limitations. So this is where we really get to the divergence between, is the note still viable and does that impact the foreclosure? In *Zbroszczyk*, it was a home equity line of credit. That was the debt instrument, and it was originated in 2008. It wasn't a true conventional 30-year mortgage, where you get a lump sum and then you pay it back over 30 years. It was the type of loan instrument where there's a maximum cap you can borrow against over time periodically, and the term of the agreement lasted until February of 2018.

So in that case, the lender foreclosed in October of 2023, so five years and a couple months after the default, or the maturity of the loan, and they claimed that the outstanding balance was the maturity date of February of 2018. The borrower brought a motion to dismiss, and he argued that the default date was actually August of 2013 based on correspondence of default from the lender. And so the 10-year statute of limitations barred the foreclosure and it should be dismissed. On appeal, the appellate court took a slightly different analysis than the trial court. The appellate court held that the debt instrument at issue, because it was a revolving credit loan, had implications for the statute of limitations.

Now, again, I said it was just, there was no great dispute up until now about statute of limitations for mortgage foreclosures, because mortgage foreclosure statute of limitations is 10 years, and so is a written breach of contract, and so is breach of promissory note. What the court held is that this revolving credit agreement was more analogous to like a credit card agreement. It is not a written contract for statute of limitations purposes, because all the terms can't be gleaned from the face of the agreement. You need some parole evidence to prove the essential terms of the loan and most specifically, how much is due, how much was borrowed periodically. You can't get that from the face of the document, so it's not a written contract, so it doesn't have a 10-year statute of limitations.

The court held that this credit agreement had a five-year statute of limitations. And again, you have the court pointing to this earlier, from the 1800s case law, about mortgages being mere incidence to notes and being barred when the notes barred. And it noted in a footnote that, despite the age of these cases, they still appear to be valid. They haven't been explicitly overturned by the Illinois Supreme Court.

So in the *Zbroszczyk* case, the shorter statute of limitations for the note, because it was a revolving credit agreement, made the foreclosure subject to dismissal. It cut off the life of the mortgage, because of the statute of limitations for the note. These cases demonstrate that the older case law about a mortgage being just a mere incident to a debt being used in novel ways to cut off the statute of limitations for foreclosure, when you otherwise wouldn't really expect it. And, as the *Bartelstein* case shows, even during an active case.

Chris Willis:

So Lou, what's the status of the *Zbroszczyk* case?

Louis Manetti:

The *Zbroszczyk* case is a published appellate decision, so it is binding. There is more activity going on in that case. The lender has filed a petition for rehearing. So that might not be the final word on it, and we don't know if they're going to appeal to the Illinois Supreme Court if the petition for rehearing isn't granted and the opinion stays largely as it is. So there might be more on that case, but that is an official appellate case.

Chris Willis:

Okay. So we've heard about what these decisions are. And, presumably, borrowers counsel are invoking these arguments in a lot of other pending cases. So what are the lenders arguing back? What's the other side of this issue that we're going to see presumably presented to the appellate court in *Bartelstein*?

Louis Manetti:

Yes. You are seeing these arguments much more frequently in the trial court. So it's something that lenders' attorneys have to deal with, even though this new branch about statute of limitations is currently developing. So you're seeing arguments in *Bartelstein* and *Zbroszczyk* and it should be made in the trial court when it comes up. There are a couple arguments being made. The very simple one, and it's facially intuitive, is that there is a specific statute of limitations for mortgage foreclosures in the Illinois code. It's 10 years. The argument, essentially, is that basic statutory interpretation says that no section of a statute can be rendered meaningless, or superfluous. Also, that more specific sections of statutes govern over more general ones.

So the argument, essentially, is if the life of the note can diverge from the mortgage and cut off foreclosures, it essentially ignores the very clear 10-year statute of limitations for a mortgage foreclosure lawsuit. It renders that superfluous. All you have to do is look at the note. And if the note's still viable, you're good. And if it's not, you're not. That's an intuitive argument that just says, no. Foreclosures have their own statute of limitations. It's 10 years.

The other argument goes back to what's being argued in *Bartelstein*, where the court noted, it commented that this could have been avoided if you brought a separate count for the promissory note. It gets a bit more granular than that, because you can ask for monetary relief in an Illinois mortgage foreclosure. Just a foreclosure. You can ask for foreclosure of the property and a sale. You can also ask for any deficiency as a personal award against the borrower. And you don't need a separate account to ask for this. And how it normally presents in a foreclosure is in the prayer for relief. You ask for a personal deficiency if sought, or a personal deficiency if sought and appropriate.

There's a recent Supreme Court case called *Cobo*, in which the Illinois Supreme Court had – it was in the context of essentially, whether or not two cases are identical for preclusion purposes. But in its analysis, it said, when you file a foreclosure, just a single count foreclosure, and you ask for relief sounding in a personal deficiency, you're invoking rights under the note. You have made a claim under the note. And that was its purposes in its case for preclusion purposes, but the argument is essentially, you do not need to bring a second count under the promissory note to preserve your rights under the note, or to make a claim for it at the outset. And it's overwhelming that this relief is asked for in mortgage foreclosures, because at the outset of the case, you simply don't know if there's going to be a deficiency. So you want to preserve your ability to get one.

Chris Willis:

And that makes sense, Lou, because I've always understood the way the statute of limitations works is that once a complaint is filed, the statute's done, as long as whatever claim it might be involved that you might add later, like a claim under the note arises from the same facts and circumstances as the allegations in the complaint, which in this instance, it surely does.

Louis Manetti:

Correct. Yes. The way that most mortgage foreclosure complaints are drafted, there is a prayer for relief, unless there's something obvious like a bankruptcy discharge, or some clear operation where money can't be involved here, it's overwhelmingly common in mortgage foreclosures to seek relief for a personal deficiency, if that's appropriate. And you have this other Supreme Court case saying, that is a claim on the note. So the argument essentially, is you don't need a separate count under the promissory note to preserve this.

When you file a foreclosure and it asks for a personal deficiency, if that's appropriate, you are exercising rights under the note and that's preserved. What you also have is longstanding authority that basically says, statute of limitations concerns don't apply once a case is timely filed. If you meet your statute of limitation deadline with your lawsuit, there's nothing else that can happen that can dislodge the case mid-case. The case should remain active until it's resolved. So, you can't dismiss a foreclosure if it's timely, simply because the statute of limitations has since expired on the note, because litigation went on for so long.

Chris Willis:

That seems to make a lot more sense to me. Okay, so while we have this issue kicking around in the Illinois appellate system, what should banks and servicers consider doing in light of these pending arguments?

Louis Manetti:

There are a couple things they can do, particularly in light of the *Zbroszczyk* case, which again, there might be more to be said about the case, but it is currently a binding appellate decision. The first thing to do to get a clear sense of what type of debt instrument you're working with at the outset. So that you can't be surprised, like the lender surely was in *Zbroszczyk*. So are you dealing with a conventional 30-year mortgage loan with a set amortization schedule, which is clearly a written contract and that falls under the 10-year statute of limitations? Or is the debt instrument more like a revolving line of credit with a maximum cap that can be periodically drawn on?

If you're dealing with the latter, you should know that and adjust your deadlines accordingly. Because I'm sure the lender was not expecting the court to come down the way it did in *Zbroszczyk*. So know what kind of debt instrument you're dealing with, and the fact that it's a revolving line of credit might cut down the statute of limitations.

Lenders should also ensure that foreclosures are being litigated efficiently to prevent these statute of limitations from even occurring on the note. It can be tricky in Illinois, because by just the way that the Illinois mortgage foreclosure law is designed, it takes a while in a totally uncontested Illinois mortgage foreclosure case. It could take more than a year just based on redemption periods and things you need to do in court. So try and be efficient.

Also, if you're running up against the statute of limitations for the note during an actively litigated foreclosure, you can move to amend to include account for relief on the promissory note. That would certainly meet the trial judge's comments on what should be done to preserve this. Would be an option when a lender is really facing down that deadline, because a case for whatever reason has been litigated for a long time.

Chris Willis:

Okay. Well, all that makes sense. So Lou, let's close the podcast episode there. Thank you very much for being on and I assume we'll update the audience when we get some more clarity from the Illinois appellate courts, or maybe even the Illinois Supreme Court, on this issue. So everybody, stay tuned to the podcast and, of course, thanks to all of you for listening to today's episode.

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