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Real Property

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Case Summary: *Wilmington Savings Fund Society v. Herzog*

BY THOMAS M. OLSON, JR.

Summary

In *Wilmington Savings Fund Society v. Herzog*, 2024 IL App (1st 221467, the Illinois First District Appellate Court affirmed the circuit court's decision to grant summary judgment in favor of the mortgagee-plaintiff ("Wilmington Savings")—despite the prior mortgagee having executed and recorded a release of mortgage against the property several years prior—based upon a lack of consideration given in exchange for the release. The court reached its conclusion by analyzing the release of mortgage as any other contract which, in order to be valid, must contain: (1) an offer, (2) acceptance, and (3) consideration. Here,

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Case Summary: *Hundley v. WPD Management, LLC*

BY LAURA SKAAR

Introduction

The First District Appellate Court's November 2023 ruling in *Hundley v. WPD Management, LLC*, 2023 IL App (1st) 230075, is being praised as a rare common-sense win for landlords, under Chicago's Residential Landlord and Tenant Ordinance (RLTO), who do not use security deposits. Here's what you need to know.

Case Summary

A group of three tenants brought a class-action lawsuit against their landlord, WPD Management, LLC, seeking strict-liability damages against the landlord for failing to include a copy of the Chicago security deposit summary along with the lease, as required under the RLTO. The landlord did include the general RLTO summary (an overview of important rights of tenants, as compiled and periodically updated by the City of Chicago) with the lease, but did not include the additional security deposit summary, because no security deposit had been collected under the lease. The tenants argued that because the RLTO imposes

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the mortgagor failed to present evidence contradicting the mortgagee's evidence of a lack of consideration in exchange for releasing the mortgage. Accordingly, the First District affirmed the circuit court's ruling that the release of mortgage was not a valid contract and, therefore, the mortgagee held a valid, existing mortgage, and it was entitled to summary judgment.

The First District also concluded that the circuit court did not abuse its discretion in confirming the foreclosure sale and entering a deficiency judgment against the mortgagor-defendant (Herzog) without an evidentiary hearing.

Factual Background and Procedural History

In 2006, Herzog purchased the real property located in Cook County and commonly known as 9111 West 126th Street in Palos Park (the "property"), and he also executed a mortgage in the amount of $1,499,999 (the "mortgage") as security for the loan he obtained to fund the purchase. The original mortgagee, Wells Fargo, recorded the mortgage against the property on October 12, 2006. The loan was modified twice, first on March 31, 2008, and a second time on April 3, 2008. After the second modification, the amount of indebtedness was $1,728,798.05. On April 18, 2008, Wells Fargo executed a release of the original mortgage (the "release"), which was subsequently recorded against the property on May 6, 2008.

In 2010, Herzog defaulted on his obligation to make the necessary mortgage payments. As a result, in 2011, Wells Fargo filed its initial foreclosure complaint in this action. From 2011 until 2017, Wells Fargo continued pursuing its foreclosure action against Herzog. In 2016, Wells Fargo assigned the mortgage to Wilmington Savings. Around this same time in 2016, the mortgage was re-recorded against the property. In 2017, Wilmington Savings became the plaintiff and then the parties engaged in extensive motion practice and discovery regarding the 2008 release. Wilmington Savings eventually filed a motion for summary judgment against Herzog and in 2021, the circuit court granted the motion and entered summary judgment in favor of Wilmington Savings. Shortly thereafter, Herzog filed (i) a motion for a stay pending appeal, (ii) a motion for a final and appealable order finding, and (iii) a motion to reconsider the order granting summary judgment. All three motions were denied.

The property was sold at auction for $1,088,000. After the foreclosure sale, Wilmington Savings filed a motion for confirmation of the sale requesting a personal deficiency judgment and eviction order against Herzog. The circuit court granted the motion, approved the sale, and entered a deficiency judgment of $1,574,091.18 against Herzog. Thereafter, Herzog filed his appeal.

Issues on Appeal

1. Herzog argued that the circuit court erred in granting summary judgment in favor of Wilmington Savings because the release of the mortgage barred its foreclosure and Wilmington Savings did not provide evidence of fraud, duress, illegality, or mutual mistake.
2. Herzog also argued that the circuit court erred in confirming the sale and entering a deficiency judgment without an evidentiary hearing where the amount was patently inequitable.

Issue 1: Whether the Circuit Court Erred by Granting Summary Judgment

The appellate court, affirming the circuit court's granting of summary judgment, began its analysis by examining the validity of the release, since answering that question was necessary before being able to determine whether there was a valid, existing mortgage under which the mortgagee defaulted.

Accordingly, the court started out detailing the salient facts surrounding the release. Specifically, the release was executed by the prior mortgagee (Wells Fargo) on April 18, 2008, and recorded on May 6, 2008. The release identified Herzog as the mortgagor,

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it identified the subject mortgage at issue in the subject foreclosure action, it stated that Herzog was released from the subject mortgage, and it was signed by an agent of Wells Fargo. In 2015, seven years later, Wells Fargo, just prior to assigning the mortgage to Wilmington Savings, filed an "Affidavit of Rescission" with the Recorder of Deeds, which stated that the release was recorded in error. The mortgage was then "re-recorded" in 2016.

The court noted that a "release" like the one at issue, is a type of contract involving "the abandonment of a claim to the person against whom the claim exists." Thus, the release is governed by the rules of contract law and, in accordance with those rules, "where the release in question is valid on its face, the burden of proof is on the party seeking to rescind or invalidate the release."

Herzog asserted that, for Wilmington Savings to avoid enforcement of the release, it must provide *clear and convincing* evidence that the release was obtained through fraud, duress, illegality, or mutual mistake. As the court noted, Herzog's argument assumes that the release was, in fact, a valid contract, and Wilmington Savings took the position that the release was not a valid contract because a valid contract requires an offer, acceptance, and consideration, and no consideration for releasing Herzog from the mortgage was given in exchange.

The court agreed that consideration is required for every valid contract and thus, a contract lacking consideration cannot be a valid contract. However, Illinois law is clear that the party alleging lack of consideration must overcome the presumption of a valid consideration and cannot rely on the mere pleading of lack of consideration. Thus, in order to overcome the presumption of a valid consideration, the contesting party must provide evidence supporting its allegation, and such evidence "must be of a very clear and cogent nature." Here, since Wilmington Savings was the party alleging lack of consideration, it bore the initial burden of providing "clear and cogent evidence" demonstrating that the release was invalid for lack of consideration. However, upon providing such evidence, it will have proven it is entitled to summary judgment.

Herzog asserted two points in his attempt to defeat Wilmington Savings' argument that the release is not a valid contract based upon lack of consideration. First, Herzog cites to the legal principle that courts will typically not inquire into the sufficiency or adequacy of consideration. However, the court rejected that argument since the allegation at issue is a complete absence of consideration as opposed to an attack on the sufficiency of consideration. Second, Herzog made an assertion regarding the inadmissibility of "parol evidence" to validate the release. The court likewise found this second argument meritless, noting that "failure of consideration may be shown by parol evidence" where that issue is properly in dispute.

To support its claim that the release is invalid, Wilmington Savings points to three pieces of evidence: (1) Wells Fargo's 2015 Affidavit of Rescission; (2) Herzog's admission that he continued to make mortgage payments after the release was recorded; and (3) the amount of Herzog's outstanding indebtedness. Ultimately, the court ruled that neither the first nor the second evidentiary points were sufficient to establish a lack of consideration. However, the court was persuaded by the third point, that Herzog's mortgage has not been paid off, showing clear and cogent evidence that consideration was not paid in exchange for the release. Herzog failed to present any evidence to rebut that showing and, therefore, Wilmington Savings was entitled to summary judgment.

Issue 2: Whether the Circuit Court Erred in Confirming the Sale and Entering a Deficiency Judgment Without an Evidentiary Hearing

In his appeal, Herzog contended that the deficiency judgment amount was unfair, and he requested that the appellate court "reject the sale" or "require and evidentiary hearing to determine whether it should be approved." In response, Wilmington Savings argued that Herzog's objection is based upon conjecture regarding the fair market value of the property. Also, Wilmington contends, Herzog completely failed to make any showing as to any of the factors set forth in section 1508 of the Illinois Mortgage Foreclosure Act (section 1508).

The appellate court agreed with Wilmington Savings and affirmed the circuit court's decision to confirm the sale and enter a deficiency judgment without the need for an evidentiary hearing. The appellate court explained that confirmation of the foreclosure sale is governed by section 1508, which *requires* the court to confirm the sale unless the court finds one or more of the following four bases to exist: (1) a notice of sale required under section 1507(c) of the Foreclosure Act was not given; (2) the terms of the sale were unconscionable; (3) the sale was conducted fraudulently; or (4) justice was otherwise not done. The appellate court agreed that Herzog failed to provide sufficient evidence to establish that any of the four section 1508 bases applied. Specifically, with regard to the second basis, the court explained that the sale terms were not unconscionable just because the property sold at auction for below market value. Supporting Illinois case law cited by the court holds that property sold at auction often sells for less than fair market value, and mere inadequacy of price alone is not sufficient cause for setting aside a judicial sale. Finally, the court, affirmed the circuit court's decision to enter a deficiency judgment without conducting an evidentiary hearing. The appellate court's reasoning was simple: The circuit court was required to enter deficiency judgment in accordance with section 1508(e).■

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a strict liability-like standard on landlords for failure to follow the RLTO's security deposit requirements, they did not have to show that they were actually harmed by the landlord's failure to include the security deposit summary – only that it was required under the RLTO and not completed by the landlord.

The appellate court upheld the trial court's dismissal based on the plaintiffs' lack of standing. Because the tenants did not pay a security deposit, there was no risk of injury by not providing them with information about their rights with respect to security deposits, which were undoubtedly the rights that the City of Chicago was seeking to protect in instituting that requirement. The court distinguished this case from several others (not related to the RLTO) in which the harm suffered by the plaintiffs was immediate and indistinguishable from the violation itself. Rather, in this case, the court said that fining a landlord who did not take a security deposit for not including the security deposit disclosure would be a "useless act," likening such an interpretation as allowing a "regulation designed as a shield to be used as a sword."

The full opinion can be found here: https://ilcourtsaudio.blob.core.windows.net/antilles-resources/resources/6972d37f-3d70-4045-a47c-cbdf10e60af9/Hundley%20v.%20WPD%20Management,%202023%20IL%20App%20(1st)%20230075.pdf.

Security Deposits Under the RLTO

For those not familiar, RLTO includes a litany of specific requirements relating to leases and security deposits – which some attorneys liken to a minefield. Among many others, the RLTO dictates how much a landlord may require as a security deposit and over what period a tenant may pay it; requires landlords to provide receipts (listing a number of specific pieces of information) upon collection of the security deposit; dictates in which types of bank accounts landlords must hold the security deposit and requires that the lease must list the name and address of the financial institution where it is held; and the list goes on. Of course, given that security deposits belong to the tenant unless and until certain circumstances occur, there is a strong public interest in protecting tenants' rights with regard to this issue. The RLTO addresses this not only through the protections outlined in the ordinance itself and the penalties for mishandling those funds (discussed below), but by requiring landlords to furnish a city-published summary of the RLTO as well as a separate notice about tenants' rights with respect to security deposits and statutory interest required to be paid.

The practical result of these protections – at least in their current form – is that the security deposit section of the RLTO is so highly detailed and technical that it creates an impossibly high bar for landlords (particularly those without the benefit of professional property management and leasing services) to clear. The consequences for landlords who fail to follow the difficult footwork of the RLTO's security deposit provisions are severe: tenants are entitled to recover a penalty equal to two times the total of their security deposit (for up to a total of 3x the deposit, if the deposit is not kept for damages or back rent), *plus* the tenant's attorneys' fees in bringing the claim for non-compliance. Evidence of the violation itself is enough to confer standing for tenants to bring these claims, even if there was no actual damage as a result of the non-compliance. Not only do the complex security deposit requirements account for upwards of 16 percent of the total text of the RLTO, but they pack the biggest financial punch of all fees or penalties that landlords can incur (most of the others are more to the tune of $50-100 a pop).

Due to the difficulty of strict compliance with the security deposit regulations, many landlord-tenant attorneys in Chicago now counsel their landlord clients not to collect them at all. Given the complexity of the requirements for security deposits versus the potential to lose upwards of three months' rent in one fell swoop, landlords – like WPD Management, LLC in this case – are now looking to alternatives to limit their exposure to financial liability. With this trend likely to continue to grow, the *Hundley* ruling is likely to impact more landlords and tenants every year.

More Than Just Saving Paper

RLTO can hardly be described as "straightforward" or "intuitive," so especially when its purpose is to protect the rights of tenants, one has to wonder: there isn't a simpler way? Although many tenants can and do seek legal counsel for their landlord-tenant disputes, many provisions of the RLTO are targeted (in word, if not in deed) toward self-help litigants. Indeed, this is the proffered reason why each and every landlord is required to attach a "summary" of the RLTO to each and every lease – although it is hard to imagine anyone other than a lawyer calling this eight-page document a "summary." Its text, while perhaps slightly simplified from the original RLTO, is hardly readable for the every-tenant's perusal. And, although its contents are important, it is hard to argue that it is in anyone's best interest to provide tenants with even more pages of legalese, especially those – as in the *Hundley* case – that do not even pertain to their leases at all.

That being said, landlords should not take this as an open invitation to customize the RLTO summary as they see fit – the main summary must be included with all leases in full, as the court confirmed in *Kopnick v. JL Woode Mgmt. Co.* (2017 IL App (1st) 152054). The court points out that the *Hundley* plaintiffs' reliance on *Kopnick* in their case was misguided: *Kopnick* fined the landlord for leaving out key provisions of the RLTO summary, many of which were key to the tenants' rights in that case but did not address whether the security deposit summary must also be included (since the *Kopnick* plaintiffs did have a security deposit).

So, while *Hundley* has largely been heralded as a rare "win" for landlords' rights under the RLTO, perhaps it is really a "win" for everybody, after all. This holding removes an unnecessary hurdle for landlords to clear (while still leaving many more hurdles, to be sure), while making it easier for tenants to understand what their rights and responsibilities are under their leases.■

The Odyssey by Homer and the Rescission of Contract: An Analysis of *Zahdan v. Frontline Business Enterprise, Inc.*

BY DONALD HYUN KIOLBASSA & EMILY HOLMES

"Nostos" is an Ancient Greek word used to reference a "hero returning home" theme. One of the most famous Nostos stories is *The Odyssey* by Homer.

In the Odyssey, we follow our hero King Odysseus of Ithaca trying to return home from the Trojan War. Odysseus angered Poseidon, God of the Sea. Poseidon cursed Odysseus by not allowing him to return home after the Trojan War. After 10 years of extreme trials and tribulations (i.e. War, Cyclops, Sirens, and Hostile Suitors), Odysseus finally returned home and took back control of his family and kingdom.

Rescission of contract is all about returning home, and the parties of a breached contract. Rescission is an equitable remedy that allows one of the parties to cancel the contract, so as to "restore the parties to the status quo ante, the status before they entered into the contract." *Hassan v. Yusuf*, 408 Ill. App. 3d 327, 353, 944 N.E.2d 895, 348 Ill. Dec. 654 (2011).

In the Nostos of *Zahdan v. Frontline Bus. Enter.*, 2024 IL App (1st) 221351, the plaintiff and defendant entered into a real estate contract for a gas station located in Chicago.

The parties agreed that the real estate contract was subject to and conditioned upon the parties entering into a second contract they referenced as the Fuel Supply Management Agreement (hereinafter "Fuel Contract"). In the Fuel Contract, the defendant would purchase fuel from the plaintiff for a term of 25 years. After the parties closed on the real estate transaction, the defendant did not honor the Fuel Contract.

In response, the plaintiff sought to rescind the real estate contract and to return the gas station back to the original plaintiff seller. The circuit court granted summary judgment to the plaintiff in the breach of contract action and awarded the remedy of rescission of contract. The defendant appealed.

The defendant essentially made three arguments on appeal.

1. First, the defendant argued that the real estate contract and Fuel Contract were in fact two separate contracts. The defendant argued that breaching the Fuel Contract should not influence the real estate contract.

The court rejected this argument because the real estate contract clearly stated that the real estate contract was contingent on the Fuel Contract.

2. Second, the defendant argued that even if they did breach the Fuel Contract, rescission was the incorrect remedy. In the authors' opinion, this was the defendant's strongest argument.

In Illinois, a court will not rescind a contract if the status quo ante cannot be restored. *Newton v. Aitken,* 260 Ill. App. 3d 717, 633 N.E.2d 213, 216, 198 Ill. Dec. 751 (2d Dist. 1994) citing *Klucznik v. Nikitopoulos,* 152 Ill. App. 3d 323, 503 N.E.2d 1147, 1150, 105 Ill. Dec. 141 (2d Dist. 1987).

The defendant maintained that he upgraded the property and, therefore, the parties really could not be brought to the same condition prior to the contract. The court lost all pity and sympathy when they learned in depositions that the defendant knew about the Fuel Contract and never intended to honor it.

3. Third, the defendant argued that the plaintiff would be unjustly enriched if the court allowed rescission in light of the improvements the defendant made to the property. This was another valid point by the defendant. However, like the story of Odysseus at sea for 10 years, the defendant was on an eight-year journey of litigation with the plaintiff. The court felt that the defendant had plenty of notice of the conflict. Accordingly, the defendant should not have done such work knowing that this case lingered in the background.

The appellate court disagreed with the defendant and affirmed the circuit court's decision granting summary judgment.

There are many practical takeaways for the Illinois real estate practitioner. Legally, rescission of contract cancels the contract and is an equitable remedy available when the parties can be restored to pre-contract status in a breach of contract action. Practically, even if the party seeking rescission may be unjustly enriched through the rescission, the court may grant rescission, notwithstanding.

Do not anger Poseidon. It is better to avoid the 10-year journey home. You must exercise caution with your clients during representation. If your client is telling you that they do not intend to honor a contract that they are entering, that is a red flag. If a party enters into a contract where there is a second contract embedded, and where that party has no intent to perform the second contract, the first contract is rescindable.

Litigation can be a Nostos that teaches very valuable lessons. It took Odysseus 10 years to return home. In this case, it took the plaintiff eight years to return home. If you are not careful during your representations, you can find yourself on a long difficult journey trying to get home.■