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**Insufficient Funds Charges: A Consumer Triumph**

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INSUFFICIENT FUNDS CHARGES: A CONSUMER TRIUMPH

Perdue v. Crocker National Bank

Traditionally, the banking industry has been heavily regulated at both state and federal levels. These regulations have restricted activities ranging from the interest rates a bank can give on deposits to the rate of interest a bank may charge on loans, discounts, and purchases. However, since the passage of the Depository Institutions Deregulation and Monetary Control Act of 1980, there has been a new emphasis on free market competition. Although increased competition has aided the consumer in areas such as higher interest bearing depository accounts, the consumer has been harmed by a drastic increase in bank service charges.

Specifically, the consumer has been hard hit by the quickly rising charges on insufficient funds (NSF) checks. In response to these excessive charges,

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7. A survey conducted by Sheshunoff & Company, a consulting firm in Austin, Tex., shows that banks hiked fees for checking accounts, check cashing, and most other basic services by seven to eleven percent this past year. However, average consumer prices advanced by only four percent.

The following chart, also prepared by Sheshunoff & Company, demonstrates the rise in average nationwide banking fees.

<table>
<thead>
<tr>
<th>Service</th>
<th>1979</th>
<th>Latest</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bounced check</td>
<td>$5.07</td>
<td>$10.32</td>
</tr>
<tr>
<td>Overdraft</td>
<td>4.72</td>
<td>9.83</td>
</tr>
<tr>
<td>Cashing checks from noncustomers</td>
<td>.40</td>
<td>2.08</td>
</tr>
<tr>
<td>Safe-deposit box</td>
<td>6.96</td>
<td>12.16</td>
</tr>
<tr>
<td>Monthly checking fee</td>
<td>1.17</td>
<td>2.70</td>
</tr>
<tr>
<td>Balance inquiry</td>
<td>1.20</td>
<td>1.42</td>
</tr>
<tr>
<td>Annual credit-card fee</td>
<td>NA</td>
<td>15.88</td>
</tr>
</tbody>
</table>


8. Id.; see also Comment, Insufficient Fund Check Charges: The Need for Legislative Action, 45 Ohio St. L.J. 1003, 1008 n.50 (1984) (This excellent comment states that the cost of processing a NSF check is approximately $0.75.); Galante,
several depositors have filed suit against their banks. These suits have ignited both legislative and administrative reaction. For example, the New York legislature recently enacted a schedule of maximum NSF check charges, specifically implemented to deter the writing of bad checks.9 Also, the Office of the Comptroller of the Currency has released an interpretive ruling, stating that state laws which restrict or limit a national bank’s ability to establish any deposit account service charges “are preempted by the comprehensive federal statutory scheme governing the deposit-taking function of national banks.”10 Finally, the Chairman of the United States House of Representatives Banking Committee, Fernand St. Germain, has called for Congressional hearings on bank service charges stating, “[i]t is clear the American consumer cannot rely on the bank regulators for any protection from unconscionable service charges.”11

Until recently, the courts have unanimously ruled in favor of the banks.12 However, in the breakthrough decision of Perdue v. Crocker National Bank,13 the Supreme Court of California handed a momentary, yet stunning defeat to the banking industry. The court held that the Crocker National Bank could be sued for allegedly overcharging on NSF fees.14 Although the consumer has triumphed for the moment, it remains to be seen whether the NSF fee will be found excessive. However, regardless of the outcome in the courts, the need for legislative action is evident. Multiple class action suits are in-

Banks May Be Liable on Bounced-Check Charges, National Law J., August 5, 1985, at 9, col. 1 (Processing fees for NSF checks range from $5.00 to $30.00 and average $13.08. However, a national survey conducted in 1985 revealed that the average cost of processing a returned check is $0.57.).

9. N.Y. BANKING LAW § 108(8)(c) (McKinney Supp. 1986); see also Mo. REV. STAT. § 570-123 (Supp. 1985). The Missouri legislature recently enacted a statute providing civil penalties for bouncing a check. The statute provides that if a depositor lacks sufficient funds to cover a check or if he has closed his account with checks outstanding, the depositor must pay the amount owed within thirty days of notice and written demand for payment. If payment is not made, the depositor will be liable to the creditor for the face amount of the draft plus three times the face amount or one hundred dollars, whichever is greater. However, in no event may the damages exceed five hundred dollars.

This statute would appear to have a significant deterrent effect on bouncing checks or at least on nonpayment of the debt. Thus, this and similar statutes destroy the need, if any, for banks to charge high fees on NSF checks to provide a deterrent to writing bad checks.


12. See infra text accompanying notes 70-93.

13. 38 Cal. 3d 913, 702 P.2d 503, 216 Cal. Rptr. 345 (1985) (en banc), appeal dismissed, 106 S.Ct. 1170 (1986). The court held that the plaintiff could proceed against the defendant on an unconscionability theory. See infra notes 95-125 and accompanying text.

14. 38 Cal. 3d 913, 702 P.2d 503, 216 Cal. Rptr. 345.
efficient from both a legal and social viewpoint. Also, national banks are virtually unaffected by state banking law.\textsuperscript{15}

This casenote will discuss the major issues surrounding the NSF fee controversy and examine the various theories used to attack the NSF fee. This will be accomplished by the following three stage analysis: (1) application of contract principles to the NSF fee context; (2) a discussion of the case law addressing the NSF fee controversy; and (3) an in-depth look at \textit{Perdue v. Crocker National Bank}.\textsuperscript{16}

The issues which comprise the controversy surrounding NSF charges are all subject to fundamental principles of contract law.\textsuperscript{17} The debtor-creditor relationship between the bank and the depositor is established when the depositor signs a signature card and deposits money with the bank. The signature card normally contains a promissory statement whereby the depositor agrees that the account shall be “subject to all applicable laws, to the Bank’s present and future rules, regulations, practices and charges . . . .”\textsuperscript{18} Generally, the card makes no mention of the various charges imposed by the bank nor their amount.\textsuperscript{19} Furthermore, the depositor is rarely given a

\textsuperscript{15} See Jacobs v. Citibank, 61 N.Y.2d 869, 462 N.E.2d 1182, 474 N.Y.S.2d 464 (1984) (A federally chartered bank is not subject to the fee limitations imposed by the New York State Banking Board.).

\textsuperscript{16} 38 Cal. 3d 913, 702 P.2d 503, 216 Cal. Rptr. 345.

\textsuperscript{17} The Uniform Commercial Code (U.C.C.) provides that “[a]s against its customer, a bank may charge against his account any item which is otherwise properly payable from that account even though the charge creates an overdraft.” U.C.C. § 4-401(1) (1978). The Official Comment adds that “the draft itself authorizes the payment for the drawer’s account and carries an implied promise to reimburse the drawee.” Id. comment 1. Thus, although overdrafts were contemplated by the U.C.C. drafters, no provision specifically deals with the fees a bank may charge for NSF checks.

\textsuperscript{18} \textit{Perdue}, 38 Cal. 3d at 921, 702 P.2d at 508, 216 Cal. Rptr. at 350.

\textsuperscript{19} See Commerce Bank of Columbia, Missouri, signature card, form CB5357 (July, 1985), which provides in pertinent part:

In consideration of Bank’s creation and maintenance of this deposit account, the following terms will govern the operation of this account. This agreement incorporates clearing house rules and state and federal law, including the Uniform Commercial Code (as amended by this form), such regulations as may be posted in the main lobby of Bank, and general banking custom usage, as all the foregoing may be from time to time amended or modified without notice unless required by law.

FEES—The Bank may charge you, and you agree to pay, or if it desires, it may charge your account directly, for its maintenance and service charges in effect from time to time (including but not limited to transaction fees, overdraft fees, copy fees and returned item fees) and reasonable attorney’s fees incurred in the collection of any of the aforementioned charges.

It is important to note that the signature card does not state the amount of any of the fees, nor does it list all the fees for which a depositor may be liable. In fact, it seems that the bank may create new fees or raise the present fees without any justification whatsoever.
copy of the checking account agreement prior to the signing of the signature card. Thus, a depositor may well enter into this relationship without knowledge of possible liabilities, such as the NSF charge.

This factual setting raises the issue as to whether the depositor has assented to all the terms of the contract. Traditionally, the courts have not been receptive to parties who sought to be relieved of their agreements on the ground that the contract was standardized and that they were not fully aware of the contractual terms.\(^20\) Since the requirement of a bargain is met by simple adherence to a standardized form, the doctrine of consideration offers no relief.\(^21\) Also, the objective theory of contracts does not require that a party intend or even understand the legal consequences of his actions.\(^22\) Thus, a depositor is not entitled to relief merely because he neither read the standard signature card nor considered the legal consequences of it.

However, where the terms of a contract are incorporated by reference, such as the signature card incorporating the bank’s rules and regulations, the court may refuse to hold a depositor to all of the terms.\(^23\) This result is reached on the ground that, although the standardized form may plainly have been an offer, the term was not one that an uninitiated reader would have reasonably expected to be part of that offer.\(^24\)

Notwithstanding the lack of assent to all the contractual terms in the signature card contract, cases have uniformly agreed that the signature card is a valid contract authorizing the imposition of NSF fees.\(^25\) Although the courts have consistently ruled in favor of the banks on this issue, the banks could easily obviate this problem. The solution is full disclosure of both the contractual nature of the signature card and all the specific contractual terms embodied in it.

In modern society the typical agreement consists of a standardized form that has been prepared by one party and assented to by the other with little or no opportunity for negotiation. Although such standardized contracts can be of great benefit to both parties,\(^26\) the individual consumer is often disadvantaged in that he is usually completely or relatively unfamiliar with the

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21. Id. The bargain theory of consideration does not require that the parties actually bargain over the terms of the agreement. The basic requirement is that the consideration be sought by the promisor in exchange for his promise and be given by the promisee in exchange for his promise. Id. § 2.6.
22. Id. § 4.26.
25. See infra text accompanying notes 103-05.
26. Standard forms can be tailored to fit office routines and mechanical equipment. They simplify operations and reduce costs. Also, such forms help make risks calculable and thus provide stability and initiative.
terms of the contract. Often, the consumer is not expected to read the form; or if he does, its meaning is hidden in small print or convoluted by confusing clauses. Furthermore, there may be such disproportionate bargaining power that the contract is simply a take-it-or-leave-it proposition. Such a contract is often labelled a contract of adhesion.\textsuperscript{27}

A bank signature card is a classic example of an adhesion contract.\textsuperscript{28} However, to label a contract as adhesive does not indicate its legal effect.\textsuperscript{29} Instead, there are two judicially imposed restrictions on the enforcement of adhesion contracts. First, the contract or provision therein must fall within the reasonable expectations of the adhering party.\textsuperscript{30} Whether the imposition of NSF charges is within the reasonable expectations of the depositor hinges primarily upon the depositor's notice of such charges.\textsuperscript{31} Thus, the bank may ensure a favorable outcome on this issue by disclosing all charges prior to the signing of the signature card. Absent such express notice, the bank may successfully argue that the depositor has constructive notice of NSF charges since such charges are common knowledge in society. Due to the apparent inability of the depositor to prove lack of notice, it is unlikely that the depositor would prevail on this theory.\textsuperscript{32}

The second limitation provides that even if the contract is within the reasonable expectations of the adhering party, the contract will be denied enforcement if it is unconscionable.\textsuperscript{33} "Unconscionability has generally been recognized to include an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party."\textsuperscript{34} Typically, the analysis is broken down into the procedural and substantive aspects of unconscionability.\textsuperscript{35} Procedural unconscionability is generally involved with the contract formation process, focusing

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{28} \textit{Perdue}, 38 Cal. 3d at 925, 702 P.2d at 511, 216 Cal. Rptr. at 353.
\item \textsuperscript{29} \textit{Id.; see also} Graham v. Scissor-Tail, Inc., 28 Cal. 3d 807, 623 P.2d 165, 171 Cal. Rptr. 604 (1981).
\item \textsuperscript{30} \textit{Perdue}, 38 Cal. 3d at 925, 702 P.2d at 511, 216 Cal. Rptr. at 353; \textit{Graham}, 28 Cal. 3d at 820, 623 P.2d at 172, 171 Cal. Rptr. at 612.
\item \textsuperscript{31} \textit{Graham}, 28 Cal. 3d 807, 820 n.18, 623 P.2d 165, 173 n.18, 171 Cal. Rptr. 604, 612 n.18. Another factor which may have a significant effect on the reasonable expectations of the adhering party is the extent to which the contract affects the public interest. See Tunkl v. Regents of Univ. of Cal., 60 Cal. 2d 92, 383 P.2d 411, 32 Cal. Rptr. 33 (1963).
\item \textsuperscript{32} The cases addressing the NSF check issue have not analyzed the issue in terms of a depositor's reasonable expectations. Instead, the courts have focused on unconscionability. See \textit{infra} text accompanying notes 110-25.
\item \textsuperscript{33} \textit{Perdue}, 38 Cal. 3d at 925, 702 P.2d at 511, 216 Cal. Rptr. at 353; \textit{Graham}, 28 Cal. 2d at 820, 623 P.2d at 173, 171 Cal. Rptr. at 612.
\item \textsuperscript{34} E. Farnsworth, \textit{supra} note 20, § 4.28, at 314.
\item \textsuperscript{35} \textit{Id.; see Perdue}, 38 Cal. 3d at 925, 702 P.2d at 511, 216 Cal. Rptr. at 353.
\end{itemize}
\end{footnotesize}
on the use of fine print, the relative bargaining position of the parties, and misrepresentation. The procedural aspect includes "oppression?" arising from unequal bargaining power and "surprise" arising from the use of fine print or hidden, unexpected contract terms. The substantive aspect focuses on the contract terms themselves. This analysis involves consideration of whether the contract is totally one-sided, unreasonable, and lacked justification.38

Generally, there must exist both procedural and substantive unconscionability before a contract or clause can be voided by the unconscionability doctrine.39 In the application of these concepts, some courts have reasoned that if there exists gross procedural unconscionability then not much substantive unconscionability is needed.40 The same "sliding scale" analysis is applicable if there is great substantive unconscionability but little procedural unconscionability.41 Application of this doctrine to the NSF context leads one to the conclusion that NSF charges may indeed be unconscionable. Procedurally, there is gross inequality of bargaining power, the contractual language usually appears in small print, and there is usually an absence of full disclosure of all contractual rights and duties.42 Also, the bank presents the depositor with a document which serves in part as a handwriting example, but whose contractual character is not obvious.43 Furthermore, the bank may reserve the right to raise its fees at its own discretion, subject only to notice requirements of state law.44 Substantively, the transaction is totally one-sided. As far as the signature card is concerned, the bank has all the rights and the depositor has all the duties.45 The average charge for a NSF check may

40. Id.
41. Id.
42. See supra text accompanying note 19.
43. See Perdue, 38 Cal. 3d at 928, 702 P.2d at 513, 216 Cal. Rptr. at 355.
44. Id; see supra text accompanying note 19.
45. Perdue, 38 Cal. 3d at 928, 702 P.2d at 513, 216 Cal. Rptr. at 42. Although the bank must pay checks drawn on the depositor's account, the bank may raise or create new fees at its own discretion. Also, the bank may terminate the agreement if the bank determines that the account is not or will not be maintained in a reasonable manner. See supra text accompanying note 19.

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range from $10.3246 to $13.0847 while the estimated cost to the bank ranges from $0.5748 to $0.75.49 These figures result in the bank receiving a low of 1400% profit on NSF charges and a high of 2300% profit. Although the fee for one bounced check is relatively small, it is estimated that $200 million is collected per year on bad checks in California alone.50

Banks have sought to characterize the unconscionability issue in terms of the competitive structure of the banking industry.51 As pointed out by attorneys for the defendant bank in Perdue v. Crocker National Bank, "the price/cost theory advocated . . . is the breaking point between unconscionability analysis—an individual contract remedy—and pure judicial ratemaking affecting an entire industry. No court has ever held the market prices in an industry to be unconscionable."52 While it is unlikely that a court would find prices set by a freely competitive market unconscionable, it is arguable that banks do not operate in a freely competitive market. Although the current trend is toward deregulation of the banking industry, there still exists a comprehensive set of regulations governing the banking trade. However, regardless of how the banking industry is characterized, the competitive structure of the industry is but one factor to be considered in the analysis. The protection against unconscionable contracts has never been thought incompatible with a free and competitive market. The defendant bank is in essence asking for a market free of restraints against oppression and overreaching, applicable to all other commercial transactions. Thus, even if a bank's NSF charges are a product of a freely competitive market, this does not end the inquiry. Instead, the court must apply the procedural/substantive analysis to the particular facts of each case.

Stipulating in advance a sum payable as damages has several advantages over assessing a penalty. For both parties, liquidated damages may facilitate the calculation of risk and reduce the cost of litigation. For society as a whole, it may save the time of judges, juries, and witnesses. Thus, liquidated damages cut the expense of litigation in the aggregate as well as in the individual case. These advantages are especially significant when the amount in controversy is small, as is the case with NSF charges. A liquidated damages clause is valid only if the damages to be anticipated are uncertain in amount or difficult to prove; and the amount stipulated is reasonable, not greatly disproportionate to the actual loss.53 An amount greatly disproportionate to the loss is termed a penalty, which is ineffective and unenforceable.54

46. See supra text accompanying note 7.
47. See supra text accompanying note 8.
48. Id.
49. Id.
50. Galante, supra note 8, at 9, col. 1.
52. Id. (emphasis in original).
53. E. Farnsworth, supra note 20, § 12.18.
54. Id.
Several depositors have attacked the NSF charge on the ground that such charges constitute a penalty.\textsuperscript{55} However, an initial stumbling block to the application of this theory is the requirement of a breach of contract between the bank and depositor. Thus, the primary issue is whether a depositor breaches his contract with the bank by writing a NSF check. The courts have uniformly resolved this issue in favor of the banks, failing to find either an express or implied covenant not to write bad checks.\textsuperscript{56} The courts base this conclusion on the following factors. The Uniform Commercial Code (U.C.C.) section 4-401 specifically authorizes a bank to pay overdrafts and to charge customers' accounts to recover expenses.\textsuperscript{57} Furthermore, the signature card is silent on the characterization of a NSF check and the depositor in no way expressly agrees to refrain from writing bad checks.\textsuperscript{58} Thus, the courts conclude that the fee a bank may charge for processing a NSF check is limited by principles of reasonableness and unconscionability.\textsuperscript{59} However, the courts' reliance on section 4-401 as a basis for not finding a breach from a NSF check, may be attacked on three bases. First, although the U.C.C. does address the subject of overdrafts in section 4-401, it may be more accurate to say that the U.C.C. contemplates their occurrence rather than their use as an ordinary banking transaction. However, regardless of the terminology, it must also be recognized that the U.C.C. addresses forgery, fraud, and theft. Yet, these acts are in no way legitimized. Second, the fact that section 4-401 gives the bank the option of paying overdrafts by no means leads to the conclusion that a finding of breach is precluded. Section 4-401 merely gives a bank two basic options when a depositor writes a NSF check: pay the overdraft, charge against the customer's account the amount of the overdraft, and collect a fee for expenses incurred in processing the NSF check; or dishonor the check and collect a fee for expenses incurred in processing the NSF check. It is perfectly plausible to consider a NSF check a nonmaterial breach of the checking agreement for which liquidated damages may be assessed. A nonmaterial breach would allow the bank to charge a reasonable fee to recoup its processing expenses and make a small profit, while keeping intact the checking account agreement. Finally, just as the signature card is silent as to the characterization of a NSF check, so too is the U.C.C.

Although courts have failed to recognize an implied agreement not to write bad checks,\textsuperscript{60} one can easily argue that such an agreement does exist.

\textsuperscript{55} See infra text accompanying notes 77-82, 86-93, and 106-09.
\textsuperscript{56} Id.
\textsuperscript{57} See supra note 17.
\textsuperscript{58} Perdue, 38 Cal. 3d at 932, 702 P.2d at 516, 216 Cal. Rptr. at 358; see supra note 19.
\textsuperscript{59} Id. at 931, 702 P.2d at 516, 216 Cal. Rptr. at 358; see supra note 19.
\textsuperscript{60} Id. at 932, 702 P.2d at 516, 216 Cal. Rptr. at 358; see infra text accompanying notes 106-09.
\textsuperscript{61} See infra text accompanying notes 77-82, 86-93, and 106-09.
The mere fact that banks charge an extra fee for NSF checks implies that
the bank considers it an obligation of the depositor not to present bad checks.
Indeed, it is the practice of banks to discourage depositors from writing NSF
checks because proper financial management dictates that sufficient funds
be on deposit each time checks are written by a depositor. Thus, if one
establishes that it is the practice of a bank to discourage NSF checks and
that the signature card incorporates the practices of the bank, it is clear
that the bank and depositor have agreed that the depositor will refrain from
bouncing checks. Although presenting a NSF check may not be a material
breach of the agreement, it may constitute a nonmaterial breach to which
the penalty/liquidated damages analysis will apply.

If the courts recognize an implied covenant not to write bad checks, the
issue remains as to whether the NSF fee constitutes valid liquidated damages
or an unlawful penalty. Since the cost to ascertain damages would undoubt-
edly exceed the sum of the charge, the computation of actual damages for
each individual breach is both impractical and difficult to prove. Thus, the
bank could satisfy the first prong of the analysis. However, the bank arguably
fails the second prong. As previously stated, the average charge for a NSF
fee ranges from $10.32 to $13.08 while the cost incurred by the bank ranges from $0.57 to $0.75. By no stretch of the imagination can a 1400-
2300% differential between the fee charged and actual damages be deemed
reasonable or proportionate. Thus, if a depositor can establish an implied
agreement not to bounce checks, it would appear probable that he would
prevail on a penalty theory.

62. See supra note 19. (The signature card states that, "[t]his agreement incor-
porates . . . . general banking custom usage . . . ." This phrase arguably incor-
porates the bank's practice of discouraging NSF checks).
63. In response to the argument that the bank and depositor have impliedly
agreed that the depositor will refrain from bouncing checks, one could argue the
opposite. It is possible that the bank and depositor have impliedly agreed that pre-
sentment of a NSF check is not a breach of contract due to the common practice of
banks which allow the writing of NSF checks without termination of the checking
account agreement. Although this argument has an initial appeal, it does not dispel
the argument that a NSF check is a nonmaterial breach of the checking account
agreement. It is plausible that the bank and depositor have impliedly agreed that the
presentment of a NSF check will be a nonmaterial breach of the checking account
agreement. Indeed, when one combines the arguments that the depositor impliedly
agrees to refrain from bouncing checks and that the bank and depositor impliedly
agree that presentment of a bad-check does not constitute a material breach for which
the contract may be terminated, it is logical to consider a NSF check as a nonmaterial
breach.
65. See supra notes 7-8 and accompanying text.
66. Id.
67. Id.
68. Id.
69. Attorneys for Crocker National Bank claim that they can prove at trial
The limited case law concerning the legality of NSF charges is presented in several New York and California decisions. Two major claims have been advanced by the plaintiff depositors: first, that NSF fees constitute a penalty;\(^7\) and second, that unconscionably excessive charges are imposed pursuant to adhesion contracts.\(^7\)

In the first major New York case to address the issue of NSF fees, the Special Term Supreme Court in *Dietrich v. Chemical Bank*,\(^7\) ruled in favor of the defendant bank. The plaintiff had commenced a class action alleging that NSF fees were excessive and that their imposition constituted a breach of contract.\(^7\) In response to plaintiff's claim that the NSF charge was excessive, the court noted that New York Banking Law\(^7\) "specifically authorizes . . . a fee that will act as a deterrent to customers who create overdrafts or present items subsequently dishonored."\(^7\) In regard to plaintiff's breach of contract claim, the court found that Ms. Dietrich had assented to the charges as a term and condition of opening her account.\(^7\)

In a similar action, the Appellate Division Supreme Court in *Jacobs v. Citibank*\(^7\) ruled against plaintiff as a matter of law. The plaintiff based his

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70. See infra text accompanying notes 77-82, 86-93, and 106-109.
71. See infra text accompanying notes 110-25.
73. Id. at 714, 454 N.Y.S.2d at 491.
75. *Dietrich*, 115 Misc. 2d at 714, 454 N.Y.S.2d at 491. Although the banks stress that a relatively high fee is needed to act as a deterrent to writing NSF checks, the deterrent effect of such fees is questionable. According to one author, there is absolutely no deterrent effect provided by a $15.00 NSF fee. Comment, *supra* note 8, at 1015.
cause of action on the theory that the charges imposed for NSF checks were "grossly excessive" and hence constituted an unlawful penalty.\textsuperscript{78} The court found against the plaintiff on two bases. First, the court found no breach of contract, thus precluding a suit based on a penalty theory. Second, although the New York Banking Board had set a maximum schedule of fees to be imposed for bad checks, the defendant was a federally chartered bank, not subject to the strictures of state banking law.\textsuperscript{79}

Recently, the result in Jacobs was affirmed in a memorandum decision by the New York Court of Appeals.\textsuperscript{80} The court addressed three main issues. First, the court reasoned that since the plaintiff had agreed to pay the charges specified in his account agreement, the bank did not breach that agreement by charging more than the actual cost of processing the NSF checks.\textsuperscript{81} Next, plaintiff's argument that the NSF fee constituted a penalty was rejected on the ground that no breach had occurred. The court stated that there is no statutory or common law duty imposed upon a depositor to refrain from bouncing checks—"indeed the use of overdrafts is expressly contemplated by and provided for in subdivision (1) of section 4-401 of the Uniform Commercial Code . . . ."\textsuperscript{82} Finally, since plaintiff had failed to show that he was deprived of any meaningful choice and that the transaction was totally one-sided, the court found no merit in plaintiff's claim of unconscionability.\textsuperscript{83}

Chief Justice Cooke dissented, focusing on the provision in the account agreement providing for fees "necessary to compensate [the bank] for services rendered."\textsuperscript{84} He argued that the bank, "which has exclusive control of the information that might establish plaintiff's cause of action, does not itself know what is the cost per transaction for processing returned checks. Defendant should not be permitted to exploit this exclusivity and self-created ignorance to defeat plaintiff's action."\textsuperscript{85}

The California courts have resolved the NSF charge issues much the same as the New York courts. In Hoffman v. Security Pacific National Bank\textsuperscript{86}

\textsuperscript{78} Id. at 787, 459 N.Y.S.2d at 782.
\textsuperscript{79} Id. The General Regulations of the New York State Banking board, section 321, in accordance with New York Banking Law section 108(8)(a)-(c) (1983) provided for a maximum service charge of $4.00 when a depositor wrote a NSF check. The defendant bank imposed a fee of $7.00 for bounced checks, $3.00 in excess of the maximum charge fixed by state statute. However, since the defendant bank was federally chartered, the court found that the statute imposed no limitations upon the bank. Instead, the court reasoned that the bank was governed by 12 C.F.R. § 7.8000 (1984), which required only that service charges be fixed on a competitive basis.
\textsuperscript{81} Id. at 871, 462 N.E.2d at 1183, 474 N.Y.S.2d at 465.
\textsuperscript{82} Id. at 872, 462 N.E.2d at 1184, 474 N.Y.S.2d at 466; see supra note 17.
\textsuperscript{83} Jacobs, 61 N.Y.2d at 872, 462 N.E.2d at 1184, 474 N.Y.S.2d at 466.
\textsuperscript{84} Id. at 873, 462 N.E.2d at 1184, 474 N.Y.S.2d at 466.
\textsuperscript{85} Id.
the Second District Court of Appeals affirmed a Superior Court’s grant of dismissal in favor of the defendant. Plaintiff brought suit on the sole theory that the NSF fee was a penalty.87 However, as in Jacobs,88 the plaintiff failed to establish any implied or express agreement on the depositor’s part not to write overdrafts. Instead, the court characterized the overdraft as an application for an advance of credit.89 The court went on to state that even if there had been an implied covenant not to write NSF checks, “it appears all but certain that defendant Bank could, upon a proper showing, have established that its practice of setting in advance an agreed-upon service charge to be paid as compensation for breach of contract was necessary and therefore permissible . . . .”90

The same issue was presented and the same result reached in Shapiro v. United California Bank.91 In an attempt to establish an implied covenant not to write overdrafts, plaintiff introduced the testimony of a banking expert. The expert testified that the signature card incorporated the practices of the bank as part of the contract and that the defendant bank considered it an obligation of the plaintiff not to write overdrafts.92 While the court conceded that plaintiff’s expert testimony was enough to establish such an obligation, it was not sufficient to establish the depositor’s implied promise not to write NSF checks.93 Thus, the court affirmed the trial court’s grant of dismissal.

The latest and by far most important case addressing the NSF check controversy is Perdue v. Crocker National Bank.94 On July 3, 1978, the plaintiff filed a class action on behalf of all persons with checking accounts at the defendant bank. The complaint first alleged the existence of a contract through which the bank furnishes a checking service in return for a monthly maintenance charge. Next, plaintiff alleged that defendant collected a fee for NSF checks and that defendant had unilaterally and unjustifiably increased the amount of such fee without reference to any criteria. At the time of filing, the fee for a NSF check was $6.00 whether honored or returned and the alleged cost of processing a NSF check was approximately $0.30.95 Plain-

87. Id. at 967, 176 Cal. Rptr. at 15.
89. Hoffman, 121 Cal. App. 3d at 969, 176 Cal. Rptr. at 16.
90. Id. at 970, 176 Cal. Rptr. at 17. Although the court was correct in stating that it was necessary to have an agreed-upon NSF charge, necessity does not in and of itself validate a liquidated damages clause. The court must also consider the reasonableness of the charge. See supra text accompanying notes 64-69.
91. 133 Cal. App. 3d 256, 184 Cal. Rptr. 34 (1982).
92. Id. at 262, 184 Cal. Rptr. at 38.
93. Id. The court’s reasoning on this issue is vague and suspect. If the bank incorporates its practices into the contract and it is the practice of the bank to discourage the writing of NSF checks, it would seem to follow that the depositor agrees to refrain from writing NSF checks when he signs the signature card.
95. Id. at 922, 702 P.2d at 508, 216 Cal. Rptr. at 350.
tiff further alleged that defendant required each depositor to sign a signature card to serve as a handwriting example and that the promissory portion of the signature card was in extremely small (6 point) type. Also, plaintiff alleged that the signature card did not identify the amount of the charge nor did the bank furnish the depositor with a copy of the applicable bank rules and regulations.  

On the basis of these allegations, plaintiff asserted five causes of action: that the bank’s signature card was not a contract authorizing NSF charges; that such charges were unconscionable; that the bank had been unjustly enriched from the collection of NSF charges; that the bank utilized unfair and deceptive trade practices in failing to inform customers of the contractual nature of the signature card and its practice of waiving NSF fees for preferred customers; and that the NSF charge constituted a penalty.

The defendant filed general and special demurrers to each of the asserted causes of action. The Superior Court, as well as the First District Court of Appeals, sustained the general demurrers and accordingly dismissed plaintiff’s case. On appeal, the Supreme Court held that plaintiff’s unconscionability and unjust enrichment causes of action stated grounds for relief without further amendment. Plaintiff was given leave to amend his claims that the bank’s signature card was not a contract authorizing NSF charges and that the bank had employed unfair and deceptive trade practices. Also, plaintiff’s penalty cause of action was dismissed without leave to amend.

Addressing plaintiff’s first cause of action, the court began its analysis by ruling that the signature card was a valid contract for the handling of the

96. Id.
97. Plaintiff’s third cause of action was derivative; the charge of unjust enrichment depended upon finding that the NSF charge was excessive. Thus, since no issues for decision were presented, the court did not address the issue of unjust enrichment.
98. Plaintiff alleged two unfair acts of competition. First, plaintiff asserted that the signature card was used in a deceptive manner, in that depositors are led to believe the signature card is for identification purposes only. Second, plaintiff asserted that defendants arbitrarily waived the NSF charge for preferred customers.

The court sustained the demurrer with leave to amend as to plaintiff’s first assertion. The court stated that the allegation was neither clear nor precise. The court was unsure whether the card or the manner in which it was presented was deceptive.

The court stated that even if true, plaintiff’s second assertion would not suffice to prove unfair competition. Furthermore, plaintiff advanced no theory through which waiver constituted unfair competition. Thus, it was left within the trial court’s discretion whether to grant leave to amend. Id. at 929-30, 702 P.2d at 514-15, 216 Cal. Rptr. at 356-57.

99. Id. at 930, 702 P.2d at 515, 216 Cal. Rptr. at 357.
101. See supra note 98.
102. Perdue, 38 Cal. 3d at 932, 702 P.2d at 516, 216 Cal. Rptr. at 358.
account. 103 Plaintiff then argued that the contract was unenforceable because it permitted the bank to lower or raise the service charges at its own discretion. The court responded by stating that "a contracting party's discretionary power to vary the price or other performance does not render the agreement illusory if the party's actual exercise of that power is reasonable." 104 Thus, the court held, as a matter of law, that the signature card validly authorized the imposition of NSF charges subject only to the bank's duty of good faith in setting or varying such charges. 105

Next, the court addressed plaintiff's claim that the NSF charge was a penalty. The court reached the same result as that in Hoffman 106 and Shapiro 107 but differed slightly in its reasoning. Unlike the two Court of Appeals decisions, the Supreme Court did not characterize a NSF fee as an application for advance credit. The court noted that the signature card was silent on the characterization of a NSF check and that the depositor often bounces a check entirely by mistake without any intent to apply for credit. 108 But, the court did agree that the depositor in no way agreed to refrain from writing NSF checks. Thus, since no breach occurred, there could be no penalty. The court stated that the fee a bank could charge for a NSF check is limited only by principles of good faith, reasonableness, and unconscionability. 109

Finally, the court addressed plaintiff's claim of unconscionability. The court began its analysis by noting that the signature card was a classic example of an adhesion contract. However, the court explained that to label a contract as adhesive in character, "is not to indicate its legal effect . . . ." 110 Instead, the court stated that there are two judicially imposed limitations on the enforcement of adhesion contracts. First, the contract or provision therein


104. Perdue, 38 Cal. 3d at 923, 702 P.2d at 510, 216 Cal. Rptr. at 352 (emphasis in original).

105. Id. at 924, 702 P.2d at 510, 216 Cal. Rptr. at 352.


108. Perdue, 38 Cal. 3d at 932, 702 P.2d at 516, 216 Cal. Rptr. at 358. Reasoning that a NSF check is not an advance application for credit would appear to be the better approach for two reasons. First, unless the depositor has a personal relationship with his banker and is assured his NSF check will be honored, the depositor has no reason to believe his NSF check will be honored. Second, it is difficult to believe that a depositor would intentionally bounce a check with the knowledge that his check will almost certainly be dishonored and a substantial fee will be assessed against his account. Only a very large check amount or a desperate depositor could justify such actions. Comment, supra note 8, at 1013.

109. Perdue, 38 Cal. 3d at 932, 702 P.2d at 516, 216 Cal. Rptr. at 358.

110. Id. at 925, 702 P.2d at 511, 216 Cal. Rptr. at 353.
must fall within the reasonable expectations of the adhering party.\textsuperscript{111} Second, the contract will be denied enforcement if it is unconscionable.\textsuperscript{112} The court utilized a substantive/procedural framework to analyze the unconscionability issue.\textsuperscript{113} In regard to the substantive aspect, the court focused on the justification for the price of the NSF charge.\textsuperscript{114} The factors considered by the court in the price justification analysis included: the price being paid by similarly situated depositors in similar transactions;\textsuperscript{115} whether the charge was set by a freely competitive market; the cost of the service to the seller;\textsuperscript{116} the inconvenience imposed on the seller;\textsuperscript{117} and the true value of the service.\textsuperscript{118} Procedurally, the court considered: the absence of a meaningful choice;\textsuperscript{119} the lack of sophistication of the buyer;\textsuperscript{120} and the presence of deceptive seller practices.\textsuperscript{121}

Applying this analysis to the facts, the court reasoned that the alleged 2000% profit earned on the NSF charges definitely required further inquiry.\textsuperscript{122} Also, the court noted that the contractual character of the signature card was not obvious, the contractual language appeared in very small print, and that the bank did not provide the depositor with a copy of the bank’s rules and regulations which were incorporated into the signature card.\textsuperscript{123} In sum, the court stated, “[t]he absence of equality of bargaining power, open negotiation, full disclosure, and a contract which fairly sets out the rights and duties of each party demonstrates that the transaction lacks those checks

\textsuperscript{111} Id. The court did not discuss whether the NSF charge was within the reasonable expectations of the depositor.

\textsuperscript{112} Id.

\textsuperscript{113} Id. at 926, 702 P.2d at 512, 216 Cal. Rptr. at 354; see supra notes 33-41 and accompanying text.

\textsuperscript{114} Perdue, 38 Cal. 3d at 926, 702 P.2d at 512, 216 Cal. Rptr. at 354. The court noted that the price term, like any other term, may be unconscionable. Id. However, allegations that price exceeds value or cost, standing alone, do not state a cause of action. Morris v. Capitol Furniture Co., 280 A.2d 775 (App. D.C. 1971) (100 % markup over cost). Instead, the court must focus on the justification for the price.


\textsuperscript{118} Perdue, 38 Cal. 3d at 927, 702 P.2d at 512, 216 Cal. Rptr. at 354; see American Home Improvements v. Maclver, 105 N.H. 435, 201 A.2d 886 (1964).


\textsuperscript{120} Compare Geldermann & Co. v. Lane Processing, 527 F.2d 571 (8th Cir. 1975) (relief denied to sophisticated investor) with Frostifresh, 52 Misc. 2d 26, 274 N.Y.S.2d 757 (Dist. Ct. 1966) (relief granted to unsophisticated buyers).

\textsuperscript{121} Perdue, 38 Cal. 3d at 927, 702 P.2d at 513, 216 Cal. Rptr. at 355; see Vom Lehn v. Astor Art Galleries, Ltd., 86 Misc. 2d 1, 380 N.Y.S.2d 532 (Sup. Ct. 1976).

\textsuperscript{122} Perdue, 38 Cal. 3d at 928, 702 P.2d at 513, 216 Cal. Rptr. at 355.

\textsuperscript{123} Id.
and balances which would inhibit the charging of unconscionable fees."\textsuperscript{124} Thus, the court ruled that plaintiff was entitled to present evidence as to the commercial setting, purpose, and effect of the signature card and the NSF fee in order to determine whether the fee was indeed unconscionable.\textsuperscript{125}

Although the depositor in \textit{Perdue} has won the battle, the war is far from over. It remains to be determined whether the NSF charges will be found unconscionable. Even if such charges are declared unconscionable, as well they should be, the inquiry must not end. The proper role of NSF charges must be determined: Are they needed to serve as a deterrent to bouncing checks or do they serve merely as a profit-making device for the banking industry? If the former, which is doubtful, are excessive fees the most desirable method to achieve the goal of deterrence. If the latter, who should determine the amount that a bank can charge for NSF checks—the banks, the judiciary, or the legislature?

Delegating such trust and responsibility to the banking industry would be no better than the fox guarding the henhouse. The banks have already proven too well that they cannot be trusted to impose reasonable charges. Likewise, judicial ratemaking has its pitfalls. Does the judiciary have the expertise to handle such matters, and if so, is the judiciary an efficient vehicle through which to solve the problem? The obvious answer is no. The cost of litigation would be staggering from both a social and legal viewpoint. Also, incongruity of decisions and the inherent time delays would be unacceptable to both the public and the banking industry. The proper solution is federal legislative regulation. Congress has regulated the banking industry for decades, thus possessing the knowledge and machinery to achieve a just and efficient solution. Presently, the wealthy or influential depositor is often not affected by excessively high NSF fees because such fees are often waived by

\textsuperscript{124} \textit{Id.} at 928, 702 P.2d at 514, 216 Cal. Rptr. at 356.

\textsuperscript{125} \textit{Id.} at 928-29, 702 P.2d at 514, 216 Cal. Rptr. at 356. Plaintiff based his cause of action on a California statute which codified the common law doctrine of unconscionability. Defendant contended that the statute on which plaintiff based his cause was preempted by federal law. Specifically, defendant cited to the National Bank Act of 1864, the Garn-St. Germain Depository Institutions Act of 1982, and 12 Code of Federal Regulations section 7.8000 (1984), as a basis for preemption. The court ruled that the state law was not preempted by either a federal statutory scheme occupying the field of banking law, nor did the state law create a conflict with federal law, in the sense that it was impossible to comply with both state and federal law. The court also found that application of the state law was not contrary to the purposes sought to be achieved in the Garn-St. Germain Depository Institutions Act of 1982.

The court recognized that defendant’s argument assumed that if state law were preempted, a federally chartered bank would be free to enforce unconscionable contracts. Since the court ruled against defendant on this issue, the court did not address this assumption. However, the court did note that a federal court may very well choose to follow the lead of state courts and limit the power of banks to enforce oppressive contracts.
the bank due to the depositor’s financial importance. Conversely, the average depositor has no protection from unconscionable fees. The average depositor’s account is not large enough to receive preferential treatment, nor does the single depositor comprise enough clout to effect a change in the bank’s policies. Thus, the stage is set for congressional action. Although deregulation is needed to provide a competitive atmosphere from which consumers will certainly benefit, limited regulation is needed to insure that the benefits of deregulation accrue equally to all.

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