

This case presents for review the decision of the Court of Appeals affirming the trial court's award of summary judgment for the defendants. The trial court found that the record shows, as a matter of law, that the defendant banks did not breach the duty of good faith in imposing fees for returned checks drawn on accounts with insufficient funds. This Court concurs in the decision made by the trial court and the Court of Appeals.

The Case

Forty named plaintiffs filed suit against nine banks doing business in Shelby County asserting six separate causes of action, all based on the allegation that the banks charged "excessive" fees for checks drawn on accounts with insufficient funds ("NSF checks") and for third party checks deposited and returned unpaid ("DIR checks"). The plaintiffs seek compensatory damages, punitive damages, and treble damages. The trial court sustained the defendants' motions to dismiss the suit for failure to state a claim on which relief can be granted. The Court of Appeals, on the first appeal, affirmed the dismissal of all claims except the allegation that the banks breached a common law duty of good faith in the performance of their contractual obligations to their customers. On remand, the defendants' motions for summary judgment, based on the pleadings, affidavits, and stipulations, were granted by the trial court and the Court of Appeals affirmed.

Analysis

This is an action for breach of written contract.¹ The Court of Appeals noted that the plaintiffs failed to comply with Rule 10.03, Tennessee Rules of Civil Procedure, regarding a claim founded upon a written instrument² but found that the references in the complaint to the substance of the deposit agreements upon which the plaintiffs base their suit meet the minimum requirements for stating a cause of action. In order to consider the merits of the case, this Court will defer to the Court of Appeals' decision.

The plaintiffs do not contend that there are disputed issues of material fact. They contend instead that the court erred in holding as a matter of law that the defendants did not breach the duty of good faith in the performance of their obligations pursuant to the contracts between the banks and their customers.

The essential facts shown by the record are: each plaintiff had a checking account with at least one of the defendant banks; each account was opened upon the execution of a deposit agreement prepared by the bank and signed by the

¹The Court of Appeals has held that in Tennessee there is no cause of action in tort for breach of the duty of good faith in the performance of a contract. Solomon v. First American Nat'l Bank, 774 S.W.2d 935, 945 (Tenn. App. 1989). See also 17 Am. Jur. 2d Contracts § 732 (1991).

²"Whenever a claim or defense is founded upon a written instrument other than a policy of insurance, a copy of such instrument or the pertinent parts thereof shall be attached to the pleading as an exhibit" Tenn. R. Civ. P. 10.03.

customer; the agreements provide that the customer agrees to the terms stated in the agreement, including service charges for NSF and DIR checks; each customer was informed, upon the execution of the deposit agreement, of the amount of the NSF and DIR fees; each customer also was informed that the fees were subject to change upon notice to the banks' customers; each customer was given notice prior to the effective date of the increase in fees; and each plaintiff was charged at least one service charge for an NSF or DIR check.

The first issue for consideration is the nature of the duty of good faith. In Tennessee, the common law³ imposes a duty of good faith in the performance of contracts. This rule has been considered in several recent decisions of the Court of Appeals. The law regarding the good faith performance of contracts was well stated by the Court of Appeals in TSC Industries, Inc. v. Tomlin, 743 S.W.2d 169, 173 (Tenn. App. 1987):

It is true that there is implied in every contract a duty of good faith and fair dealing in its performance and enforcement, and a person is presumed to know the law. See Restatement (2d) Contracts, § 205 (1979). What this duty consists of, however, depends upon the individual contract in each case. In construing contracts, courts look to the language of the instrument and to the intention of the parties, and impose a construction which is fair and

³Tenn. Code Ann. § 47-1-203 (1992) is not applicable to the contracts between the parties in this case, because, by its terms, that statute applies only to contracts within Chapters 1 through 9 of the Uniform Commercial Code.

reasonable.

In Covington v. Robinson, 723 S.W.2d 643, 645-46 (Tenn. App. 1986), which was relied upon by the Court of Appeals in TSC Industries, Inc. v. Tomlin, the Court of Appeals held that in determining whether the parties acted in good faith in the performance of a contract, the court must judge the performance against the intent of the parties as determined by a reasonable and fair construction of the language of the instrument. In a later decision, the Court of Appeals held that good faith in performance is measured by the terms of the contract. "They [the parties] may by agreement, however, determine the standards by which the performance of obligations are to be measured." Bank of Crockett v. Cullipher, 752 S.W.2d 84, 91 (Tenn. App. 1988).

The present case is similar to a case in which the Oregon Supreme Court held that, as a matter of law, the bank acted in good faith. That court described the case as follows:

This class action involves the obligation of good faith in the performance of contracts. The primary issue is the nature of the good faith obligation owed by defendant First National Bank of Oregon (Bank) to its non-business checking account customers (depositors) in setting and revising, from time to time, the fees it charged to depositors who wrote checks when there were not sufficient funds in their accounts (NSF fees).

Tolbert v. First Nat'l Bank, 823 P.2d 965, 966 (Or. 1991).

Upon finding facts very similar to the facts in the case before the Court, the Oregon court held:

The uncontroverted evidence before the trial court on summary judgment in this case was that: (1) the depositors initially agreed that Bank could change the amount of the NSF fees in its unilateral discretion; (2) Bank's practice was to inform depositors of future changes to the NSF fees before such changes became effective; and (3) plaintiffs continued to maintain their accounts with Bank and, in some cases, even continued to write NSF checks after Bank informed them of the changes. No inference available to plaintiffs (other than flat disbelief, which is not an inference that plaintiffs may invoke on summary judgment) creates an issue of fact as to these pivotal circumstances. Based on this record, any reasonable expectations held by the depositors were met by Bank's procedures. As a matter of law, Bank acted in good faith in its treatment of the NSF fees; there was no issue regarding any material fact, and Bank was entitled to a judgment as a matter of law.

Id. at 971 (emphasis in original). That court's rationale regarding the duty to perform in good faith was stated as follows:

We emphasize that it is only the objectively reasonable expectations of parties that will be examined in determining whether the obligation of good faith has been met. In the context of this case - when (1) the parties agree to (and their contract provides for) a unilateral exercise of discretion

regarding changes in one of the contract terms, and (2) the discretion is exercised after prior notice - we hold as a matter of law that the parties' reasonable expectations have been met.

Id. at 970.

In this case, as in the Tolbert case, the contract authorized the banks to charge overdraft fees, the customers were advised regarding the amounts of those fees upon the execution of the deposit agreements, and they were advised of the increases in the fees before the increases became effective. The language of the agreements clearly states the terms and reflects the intent of the parties. Reason requires the conclusion that the plaintiffs could expect that the stated fees would be imposed on their NSF and DIR checks. Performance of a contract according to its terms cannot be characterized as bad faith.

The plaintiffs would avoid this conclusion by asserting that, even though the banks' acts in charging fees were consistent with the terms of the deposit agreements, those agreements were adhesive in nature and, therefore, provided the banks no authority to charge fees characterized by the plaintiffs as "too high," "excessive," and "in excess of the banks' own cost in handling the transaction."

Before addressing the plaintiffs' allegation that the deposit agreements are adhesive and, therefore, not

enforceable, it should be noted that the common law duty of good faith in the performance of a contract does not apply to the formation of a contract. See Restatement (Second) of Contracts, § 205 cmt. c (1979). Consequently, the common law duty of good faith does not extend beyond the agreed upon terms of the contract and the reasonable contractual expectations of the parties. See Sheets v. Knight, 779 P.2d 1000 (Ore. 1989).

The plaintiffs' allegations raise two further questions - whether the deposit agreements are contracts of adhesion and, if they are contracts of adhesion, are the terms enforceable. This Court recently approved the following statement defining and setting forth the essential characteristics of an adhesion contract:

An adhesion contract has been defined as "a standardized contract form offered to consumers of goods and services on essentially a 'take it or leave it' basis, without affording the consumer a realistic opportunity to bargain and under such conditions that the consumer cannot obtain the desired product or service except by acquiescing to the form of the contract." Professor Henderson has observed that "the essence of an adhesion contract is that bargaining positions and leverage enable one party 'to select and control risks assumed under the contract.'" Courts generally agree that "[t]he distinctive feature of a contract of adhesion is that the weaker party has no realistic choice as to its terms."

Buraczynski v. Eyring, 919 S.W.2d 314, 320 (Tenn. 1996)

(citations omitted).

The record in this case does not support the plaintiffs' claim that the agreements between the banks and their customers are adhesion contracts. Some of the characteristics of an adhesion contract are present, the deposit agreements are standardized forms, and, undoubtedly, the opportunity to open an account with a particular bank was presented on a take-it-or-leave-it basis. However, these factors standing alone are not sufficient. The record shows that the banks provided checking accounts which were exempt from overdraft charges. The record does not include a schedule of the charges, and, perhaps most significantly, there is no showing in the record that the customers had no realistic choice but to acquiesce in the imposition of the banks' charges. There is no showing that the fees were the same at all the defendant banks or that banking services could not be obtained from other institutions. It is common knowledge that the banking industry is very competitive. For example, different banks may charge lower fees for some services and higher fees for other services, and they also may charge lower interest rates on loans but higher fees for services, thus providing choices which may appeal to various prospective customers. In the absence of a showing that there was no effective competition in the providing of services among the banks in the area served by the defendants, there is no basis for concluding that the appellants had no realistic choice regarding the terms for

obtaining banking services.

And, further, not all adhesion contracts are unenforceable. Even if a contract is found to be adhesive, it is enforceable unless it is unduly oppressive or unconscionable. The Court discussed this issue in Buraczynski v. Ewing:

Our conclusion that the contracts were contracts of adhesion is not . . . determinative of the contract's enforceability. Enforceability generally depends upon whether the terms of the contract are beyond the reasonable expectations of an ordinary person, or oppressive or unconscionable. Courts will not enforce adhesion contracts which are oppressive to the weaker party or which serve to limit the obligations and liability of the stronger party.

Buraczynski, 919 S.W.2d at 320 (citations omitted). The California Supreme Court discussed this rule in Graham v. Scissor-Tail, Inc., 623 P.2d 165 (Ca. 1981):

Generally speaking, there are two judicially imposed limitations on the enforcement of adhesion contracts or provisions thereof. The first is that such a contract or provision which does not fall within the reasonable expectations of the weaker or "adhering" party will not be enforced against him. The second--a principle of equity applicable to all contracts generally--is that a contract or provision, even if consistent with the reasonable expectations of the parties, will be denied enforcement if, considered in its context, it is unduly oppressive or

"unconscionable."

Id. at 172-173 (citations omitted).

As previously discussed, the reasonable expectations of the appellants were that fees would be imposed pursuant to the terms of the agreements. Further, based on the record before the Court, the provisions in the agreements regarding NSF and DIR fees were not oppressive or unconscionable.

The determination that, on the facts shown by the record, the defendants, as a matter of law, have not breached the common law duty of good faith in the performance of the contracts with their checking account customers resolves the issue presented in this case. The defendants' assertion that unconscionable and oppressive provisions of a contract cannot constitute the basis for a cause of action, but only can be pleaded in defense to an action for breach of contract, need not be considered.

The judgment of the Court of Appeals sustaining summary judgment for the defendants and dismissing the suit is affirmed.

Costs will be taxed to the plaintiffs.

Reid, J.

Concur:

Birch, C.J., Drowota, Anderson,
and White, JJ.