

IN THE SUPREME COURT OF THE STATE OF NEVADA

REZA MASHHOUR AND FARIDEH  
MASHHOUR,  
Appellants,  
vs.  
U.S. BANCORP HOME LOANS, AN  
OREGON CORPORATION,  
Respondent.

No. 39471

**FILED**

JUN 08 2004

JANETTE L. BLOOM  
CLERK OF SUPREME COURT  
BY *J. Richards*  
CHIEF DEPUTY CLERK

ORDER OF REVERSAL AND REMAND

Reza and Farideh Mashhour appeal from a summary judgment<sup>1</sup> entered below on their claims against U.S. Bancorp Home Loans for negligent disbursement of home construction funds to their general contractor.<sup>2</sup> The assignments of error stem from the district court's ruling that no material issues of fact remained undecided and that Bancorp, as a matter of law, owed no duty in tort to inspect the progress of construction prior to making interim payments to the contractor. We reverse and remand this matter for trial.

FACTUAL HISTORY

The Mashhours contracted with Kever Construction to build a custom home in southwest Reno and obtained \$413,000.00 in construction financing from Bancorp. According to the Mashhours, their decision to finance the project through Bancorp followed discussions with a Bancorp representative, Lisa Rogers, in which Ms. Rogers informed

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<sup>1</sup>See NRAP 3A.

<sup>2</sup>The contractor defaulted prior to completion of the home construction project.

them that Bancorp was an experienced home construction lender, that it would conduct periodic inspections of construction progress, and that Bancorp would only disburse loan proceeds to Kever based upon inspections and only for work consistent with the construction plans.

The loan agreement provided that Kever and the Mashhours would use the construction loan proceeds to build the home in accordance with the plans and specifications approved by Bancorp, and that Kever would follow Bancorp's construction progress schedule, or proceed at a rate deemed satisfactory by Bancorp. The loan agreement provided Bancorp with a right, not the obligation, to inspect, and that Bancorp would issue progress payments jointly to the Mashhours and Kever. If Bancorp found any of the work to be unsatisfactory, in its discretion, it could order replacement. Finally, the Mashhours agreed to indemnify Bancorp for any structural defects or inadequacies in the home.

"Construction Draw Procedures" signed contemporaneously with the contract provided that Bancorp's "inspector will complete inspections generally on the last day of the month and the 1st, 2nd and 3rd day of the next month." Kever began construction in July 1995 and continued through December 1995, during which Bancorp's inspector, Susan Mataruga, visited the construction site several times.

Kever submitted eleven draw requests to Bancorp for work performed between July 7, 1995 and January 23, 1996, all of which the Mashhours countersigned. The Mashhours did not inspect Kever's construction progress themselves, but on several occasions observed Bancorp's inspector at the construction site. Bancorp disbursed funds on the various draw requests through a series of checks made jointly payable

to Keever and the Mashhours. The Mashhours endorsed ten of the drafts, voiding the eleventh.

In January 1996, the Mashhours realized that Keever Construction was receiving payment for uncompleted work. The Mashhours confronted Keever and advised him that the remaining construction loan funds were insufficient to complete the home. Keever refused to complete construction without additional funds and abandoned the project. The Mashhours estimated the cost of completion at \$250,000.

### PROCEDURAL HISTORY

On January 12, 1998, the Mashhours filed a complaint in district court against Keever Construction and its principals for breach of contract, fraud, negligence, conversion and conspiracy; and against Bancorp in tort for negligent supervision of the construction, alleging failures to verify that work had been properly performed before the disbursements of progress payments. The complaint against Bancorp also alleged breach of its agreement to disburse funds to Keever only upon construction of improvements in accordance with plans and specifications. In short, the Mashhours alleged that Bancorp improperly disbursed money to Keever for incomplete work and, to a degree, for defective work.

Following a period of discovery, Bancorp moved for summary judgment, contending that it was under no duty to the Mashhours to inspect the property to insure that construction was proceeding in accordance with plans and specifications. Bancorp also asserted that the Mashhours breached their contractual duty to assure proper construction by countersigning the improper draw requests and endorsing the progress payment checks. Additionally, Bancorp asserted that the Mashhours

failed to establish the elements for construction lender liability under Davis v. Nevada National Bank.<sup>3</sup>

In response, although recognizing that “construction lenders generally owe no duty to their borrowers to identify unworkmanlike or defective construction;”<sup>4</sup> the Mashhours asserted that Bancorp assumed a duty in tort to inspect and independently determine that the work billed for by the contractor had in fact been completed in accordance with the plans and specifications. In pressing this argument, the Mashhours abandoned their more discrete breach of contract claim, and their claims concerning construction defects. Thus, the district court was presented with the singular issue of whether Bancorp assumed a duty in tort to inspect for the benefit of the Mashhours.

Reza Mashhour’s affidavit in opposition to summary judgment asserted his lack of experience in residential construction, and that he

was particularly pleased that [Bancorp] represented . . . that it would hire an inspector to conduct periodic inspections and that loan proceeds would only be distributed to the contractor after inspections and for work performed consistent with the plans. . . . That [he] was specifically told by Ms. Rogers that [Bancorp] had a particular inspector in mind and that [he] would be advised upon his/her employment; that [he] was further told that the bank would process disbursement requests on a bi-monthly basis after submission of inspection reports.

The affidavit concerning Ms. Rogers was considerably expanded from previously given answers to Bancorp’s interrogatories, in

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<sup>3</sup>103 Nev. 220, 737 P.2d 503 (1987).

<sup>4</sup>See NRS 41.590.

which Bancorp requested that the Mashhours identify all communications with all agents or representatives of Bancorp, and to specifically state the substance of the communications. In response, the Mashhours identified three persons, including Ms. Rogers, indicating that, among other issues that came up during construction, "Ms. Rogers had communication with the Mashhours regarding their loan, loan disbursements, and personally inspected the property . . . ." Neither the affidavit nor the interrogatory answers indicate that Ms. Rogers ever represented that the inspections would be conducted for the Mashhours' benefit.

In summary, Mr. Mashhour asserted that, based upon Ms. Rogers' representations, the loan documents and Bancorp's actual retention of an inspector, he rightfully believed he was under no responsibility to inspect, and that he rightfully relied on Bancorp to ensure that funds were properly disbursed.

The district court found that the written loan agreement fully incorporated all of the rights and obligations of the parties concerning inspection of the course of construction. More particularly, that the contract gave Bancorp a right, not an obligation, to inspect, and obligated the Mashhours to verify construction progress. Accordingly, the court found no issues of fact regarding the respective duties of the parties and, finding that the terms of the contract contained none of the duties alleged by the Mashhours, granted summary judgment in favor of Bancorp. In aid of its ruling, the district court observed that a lender should not "consider

itself at risk if it volitionally elects to inspect and does so negligently or inefficiently.” The Mashhours filed their timely notice of appeal.<sup>5</sup>

### DISCUSSION

The Mashhours contend that issues of fact remained as to whether Bancorp voluntarily and independently assumed an obligation to inspect construction for the Mashhours’ benefit. We agree and remand this matter for trial.

This court reviews orders granting summary judgment de novo.<sup>6</sup> “Summary judgment is appropriate when the pleadings, depositions, answers to interrogatories, admissions, and affidavits on file show that there exists no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law.”<sup>7</sup> “A genuine issue of material fact is one where the evidence is such that a reasonable jury could return a verdict for the non-moving party.”<sup>8</sup>

When a party files a motion for summary judgment and the motion is “supported as required by NRCP 56, the non-moving party may not rest upon general allegations and conclusions, but must, by affidavit or otherwise, set forth specific facts demonstrating the existence of a genuine

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<sup>5</sup>As the claims against Keever remain unresolved, the district court properly certified the summary judgment as final under NRCP 54(b).

<sup>6</sup>Pegasus v. Reno Newspapers, Inc., 118 Nev. \_\_\_, \_\_\_, 57 P.3d 82, 87 (2002), cert. denied, \_\_\_ U.S. \_\_\_, 124 S. Ct. 82 (2003).

<sup>7</sup>Id.

<sup>8</sup>Id. (quoting Posadas v. City of Reno, 109 Nev. 448, 452, 851 P.2d 438, 441-42 (1993)).

factual issue.”<sup>9</sup> The district court must accept all of the non-movant’s statements as true and must draw all reasonable inferences from the evidence.<sup>10</sup> “[N]either the trial court nor this court may decide issues of credibility based upon the evidence submitted in the motion or the opposition.”<sup>11</sup>

The Mashhours concede that the loan documents imposed no duty to inspect on behalf of the Mashhours, and that no duty to inspect may be implied from an ordinary lender-borrower relationship, even where the lender elects or enjoys a right to inspect. The sole claim of liability is that Bancorp, through Ms. Rogers, affirmatively promoted the benefits of its expert inspection activities to induce the Mashhours into doing business with the bank. The Mashhours reason that, contrary to the ordinary construction loan scenario, Bancorp undertook its inspections in this case, at least in part, for their benefit. Accordingly, the Mashhours claim entitlement to inferences that Ms. Rogers’ statements were calculated to alleviate Mr. Mashhour’s concerns about his inability to monitor construction, and to obtain him as a banking client.

In Davis, this court, in the context of claims of defective construction, held that a construction lender was not entirely free to disregard the interest of its borrower in the narrow instance where the borrower identified defects in the construction, requested that the bank withhold payments, and where the bank refused the request, “apparently

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<sup>9</sup>Id. at \_\_\_, 57 P.3d at 87.

<sup>10</sup>Id.

<sup>11</sup>Id.

without any investigation of the truth of [the borrower's] assertions.”<sup>12</sup> Accordingly, it held that under the narrow circumstances presented, “the Bank had a duty to conduct a reasonable investigation and reach a bona fide conclusion as to the validity of the [borrower's] request, at the risk of incurring liability for wrongful disbursement of funds.”<sup>13</sup> The court also noted that

under usual construction loan terms and conditions, no lender should consider itself at risk if it elects not to generally inspect the progress of the construction of a project financed by the lender. Nor is a lender to consider itself at risk if it volitionally elects to inspect and does so negligently or ineffectively.<sup>14</sup>

Thus, in the context of a construction defect claim, where the owner was not a joint payee on the progress payment drafts, we restricted extra-contractual liability of a construction lender to situations where: (1) the lender assumes the responsibility to disburse loan funds to a party other than the borrower; (2) the borrower informs the lender of substantial construction defects; (3) the borrower requests that the lender withhold further disbursements pending resolution of the construction deficiencies; (4) the lender continues to distribute funds and does not attempt to make a bona fide attempt to ascertain the truth of the borrower's complaint; and (5) the borrower is damaged because its complaint was accurate and the borrower is unable to recover damages against the deficient builder.<sup>15</sup>

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<sup>12</sup>Davis, 103 Nev. at 222, 737 P.2d at 505.

<sup>13</sup>Id. at 223, 737 P.2d at 505-06.

<sup>14</sup>Id. at 223-24, 737 P.2d at 506.

<sup>15</sup>Id. at 224, 737 P.2d at 506.



We note that the Davis criteria in construction defect scenarios seemingly apply with equal force to failures to complete construction in accordance with plans and specifications approved by the bank. This notwithstanding, the Mashhours fail to meet all of the conjunctive elements for liability under Davis. Bancorp clearly made progress payments jointly to the contractor and the Mashhours, made no payments over the protests of the Mashhours, and lodged no contentions that Kever is judgment-proof.

This, however, does not necessarily end the analysis. For liability to obtain, the construction lender must engage in some activity outside the scope of the normal lender relationship before the lender can be held to have assumed an obligation to protect the interest of the borrower.<sup>16</sup>

The Legislature has expressly limited construction lender liability in NRS 41.590.<sup>17</sup> However, as in Davis, the Mashhours' claims of

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<sup>16</sup>Id. at 222, 737 P.2d at 505.

<sup>17</sup>NRS 41.590 states:

A lender who makes a loan of money, the proceeds of which are used or may be used by the borrower to finance the design, manufacture, construction, repair, modification or improvement of real or personal property, shall not be held liable to the borrower or to third persons for any loss or damage occasioned by any defect in the real or personal property so designed, manufactured, constructed, repaired, modified or improved or for any loss or damage resulting from the failure of the borrower to use due care in the design, manufacture, construction, repair, modification or improvement of such real or personal property,

*continued on next page . . .*

liability do not fall within this protection. The Mashhours' claims are based upon alleged activities beyond "the loan transaction"<sup>18</sup> itself. Thus, Bancorp may potentially be liable for a breach of an extra-contractual duty to act on behalf of the Mashhours.

As the Georgia Court of Appeals in Russell v. Barnett Banks<sup>19</sup> observed:

[O]rdinarily, an action for damages for faulty construction and incidents thereto, by a homeowner or purchaser against a lending or financing authority, will not lie because the lender's customary participation, the inspection, is normally not made for the benefit of the homeowner, but is made instead for the protection and benefit of the lender. An exception has been recognized when the lender's financing activity extends beyond that of a conventional construction lender. If any exception to this rule is made, it will have to be based on some clear promise of the lender to perform certain protective functions, and upon a clear and distinct participation in the activity which resulted in the damage. It is certainly not enough to make general allegations that the lender inspected the work, since such inspections are presumed to be for its own financial purposes and are not intended to ensure a quality of work. The lender is not an insurer of

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*... continued*

unless the loss or damage is the result of some other action or activity of the lender than the loan transaction.

<sup>18</sup>Davis, 103 Nev. at 222, 737 P.2d at 505.

<sup>19</sup>527 S.E.2d 25 (Ga. Ct. App. 1999).

the work of the contractor, unless clear promises appear to the contrary.<sup>20</sup>

Further, the Restatement (Second) of Torts, section 323, is consistent with the aforementioned proposition, as well as Nevada law, and therefore provides guidance in this matter. That section states:

One who undertakes, gratuitously or for consideration, to render services to another which he should recognize as necessary for the protection of the other's person or things, is subject to liability to the other for physical harm resulting from his failure to exercise reasonable care to perform his undertaking, if

(a) his failure to exercise such care increases the risk of such harm, or

(b) the harm is suffered because of the other's reliance upon the undertaking.<sup>21</sup>

Clear indications that a construction lender has assumed an additional duty toward the borrower include the lender's control over the disbursement of funds, a mortgagee's representations of expertise, and/or a mortgagee's statements that the expertise in the inspection process will be of benefit to the borrower and serve to induce the borrower into the loan arrangement. Although Bancorp made no payments other than on the joint requests of Keever and the Mashhours, the other indicators of an assumed duty are present.

Reza Mashhour's affidavit, when reviewed in the light most favorable to him, established the existence of triable issues of fact, to wit:

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<sup>20</sup>Id. at 27 (quoting Decoudreaux v. Mut. Fed. Sav. & Loan, 455 S.E.2d 88, 90 (1995)) (emphasis added).

<sup>21</sup>Restatement (Second) of Torts § 323 (1965).

whether Ms. Rogers' representations induced the Mashhours to enter into the loan arrangement, whether Ms. Rogers actually made statements of expertise, and whether Bancorp represented that it would inspect the progress of construction and disburse funds only upon completion of construction in accordance with plans and specifications. In this, the affidavit described Bancorp's advice that it would hire a particular inspector, Bancorp's inspector visited the property on several occasions, Bancorp retained the construction loan proceeds, and stated it would only disburse loan proceeds after its inspector submitted reports. Mr. Mashhour's affidavit compels the conclusion that a trier of fact should determine whether the parties' course of conduct,<sup>22</sup> documents,<sup>23</sup> and representations<sup>24</sup> give rise to a duty in tort to inspect for their benefit.

We have also considered Bancorp's argument that Mr. Mashhour's affidavit cannot support a material issue of fact because it conflicts with the Mashhours' prior interrogatory response.<sup>25</sup> We conclude that the affidavit and interrogatory response do not conflict. Although the interrogatory requested the substance of the Mashhours' communications

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<sup>22</sup>E.g., Bancorp's inspection of Keever's progress and requiring the Mashhours to pay a fee to hire an inspector.

<sup>23</sup>E.g., the construction draw procedures document that stated Bancorp's inspector would visit the construction site on a regular basis.

<sup>24</sup>E.g., Bancorp's statements to Mr. Mashhour that it would hire a particular inspector, that Bancorp would process disbursements upon receiving inspection reports from its inspector and that Bancorp would only make disbursements for work completed consistent with the construction plans.

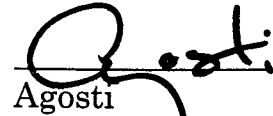
<sup>25</sup>See Aldabe v. Adams, 81 Nev. 280, 402 P.2d 34 (1965).


with Bancorp, the Mashhours responded that they spoke generally with Ms. Rogers about their loan and loan disbursements. Mr. Mashhour's later affidavit merely elaborated on that conversation. Therefore, the affidavit may properly create an issue of material fact.


In light of the above, we accordingly


ORDER the judgment of the district court REVERSED AND REMAND this matter to the district court for proceedings consistent with this order.<sup>26</sup>

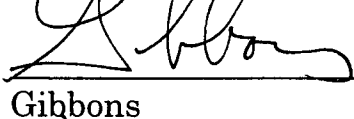
 \_\_\_\_\_, C.J.  
Shearing


 \_\_\_\_\_, J.  
Agosti

 \_\_\_\_\_, J.  
Rose

 \_\_\_\_\_, J.  
Becker

 \_\_\_\_\_, J.  
Maupin

 \_\_\_\_\_, J.  
Gibbons

 \_\_\_\_\_, D.J.  
Dobrescu

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<sup>26</sup>The Honorable Steve L. Dobrescu, Judge of the Seventh Judicial District Court, was designated by the Governor to sit in place of the Honorable Myron L. Leavitt, Justice. Nev. Const. art. 6, § 4.

cc: Hon. James W. Hardesty, District Judge  
Marshall Hill Cassas & de Lipkau  
Van Cott, Bagley, Cornwall & McCarthy  
Washoe District Court Clerk