IN THE SUPREME COURT OF THE STATE OF NEVADA

MEEKS BUILDING CENTER,
Appellant,
vs.
DUFFY WRIGHT AND DIANA E. WRIGHT, HUSBAND AND WIFE,
Respondents.

No. 41702

FILED

SEP 07 2005

JANETTE M. BLOOM
CLERK OF SUPREME COURT
BY [signature]
CHIEF DEPUTY CLERK

ORDER OF AFFIRMANCE

This is an appeal from a district court judgment in a mechanic's lien case. Second Judicial District Court, Washoe County; Brent T. Adams, Judge.

Meeks Building Center appeals from a district court judgment denying enforcement of its mechanic's lien against respondents Duffy and Diana Wright and awarding the Wrights attorney fees and costs. The Wrights entered into a contract with contractor Brown Rice Development, Inc. to build their residence in Reno, Nevada. Brown Rice, which had other accounts with Meeks, opened an account with Meeks for the Wright project. Brown Rice received disbursements directly from the Wrights' lender and then paid Meeks. Meeks asserts that it was unaware that Brown Rice was directing payments from Wrights' lender to other Brown Rice accounts with Meeks. A year after opening the account, when Brown Rice failed to pay, Meeks recorded a mechanic's lien against the Wrights' property, claiming it was owed about $41,000. The district court, pursuant to this court's decision in Sherman Gardens Co. v. Longley,[1] entered judgment in favor of the Wrights and against Meeks and awarded

[1]87 Nev. 558, 491 P.2d 48 (1971).

05-17704

attorney fees and costs. Meeks appeals. Meeks argues that we should reverse or modify Sherman Gardens. Meeks contends that Sherman Gardens imposes an impossible burden on a supplier to contact an owner every time the contractor makes a payment on a building account.

We conclude that the district court properly applied the Sherman Gardens holding, and therefore, we affirm the district court's judgment.

This court conducts de novo review of conclusions of law, and we will not disturb the district court's factual findings that are supported by substantial evidence.[2] In Sherman Gardens, this court held that an owner could not be compelled to pay twice when the supplier applied funds, paid by the owner through the contractor, to other accounts of the contractor.[3] Relying on the 1916 Iowa Supreme Court decision in Sioux City Foundry and Manufacturing Co. v. Merten,[4] we reasoned that even if the subcontractor did not knowingly misappropriate the funds, the subcontractor used the owner's funds to pay another debt.[5] Therefore, equity demands that the subcontractor cannot recover from the owner, because the owner has already paid.[6] We noted the general rule that, absent direction from the debtor, a creditor has the right to apply a

---

[2]Keife v. Logan, 119 Nev. 372, 374, 75 P.3d 357, 359 (2003).

[3]Sherman Gardens, 87 Nev. at 566, 491 P.2d at 53.

[4]156 N.W. 367 (Iowa 1916).

[5]Sherman Gardens, 87 Nev. at 566, 491 P.2d at 53.

[6]Id.

payment from the debtor to any account of the debtor.[7] However, that rule applies between a creditor and debtor, and is inapplicable when a payment comes from a third party.[8] We agreed with Williams v. Willingham-Tift Lumber Co.,[9] and concluded that in a three-party situation, the subcontractor must ascertain the correct source of payment before he can place a mechanic's lien on the owner's property.[10]

We note that in Goss v. Strelitz,[11] cited in Sherman Gardens, the California Supreme Court stated that when an owner pays a contractor for supplies and the contractor directly pays the supplier, the supplier cannot legally apply those payments to other debts of the contractor. Otherwise, the owner would be subjected to paying the contractor's other debts, outside of the owner's building contract.[12] In Goss, the supplier applied the contractor's payment on behalf of one owner to the contractor's general account.

In the present case, the district court found that law and equity demanded that the Wrights not be made to pay again for materials supplied by Meeks. The court noted that the owners had never built a house before and that they relied on the advice of their lender and Brown Rice as to the easiest, most efficient manner to handle loan disbursements.

---

[7]Id. at 566-67, 491 P.2d at 54.

[8]Id.

[9]63 S.E. 584, 585 (Ga. Ct. App. 1909).

[10]Sherman Gardens, 87 Nev. at 566, 491 P.2d at 54.

[11]54 Cal. 640, 645 (1880).

[12]Id.

The court found that Meeks knew that particular payments from Brown Rice should be applied to the correct project account. The court found that, with the exception of one payment, Meeks did not inquire as to the source of payments and instead applied Brown Rice payments to whichever Brown Rice account had the oldest invoices due. The court reasoned that Meeks was in the best position to protect itself by taking steps such as refusing to extend any more credit to Brown Rice. The court also emphasized that Meeks could have contacted the Wrights when Brown Rice first began to fall behind in its payments and could have notified the Wrights before acquiescing to the contractor's demand to reverse a particular $15,000 credit to the Wright account. We determine that the district court correctly applied the legal and equitable principles of Sherman Gardens in finding that Meeks could not pursue its mechanic's lien against the Wright's property.

Meeks also argues that, if Sherman Gardens controls, substantial evidence does not support the district court's conclusion that Meeks failed to fulfill its duties because Meeks served notice of its preliminary lien on both the Wrights and the lender, Meeks attempted to contact the lender and was told no financial information would be released, and Brown Rice misinformed Meeks regarding the source of payments. Meeks also notes that the Wrights did not require lien releases or joint checks when disbursing funds to Brown Rice, the Wrights already had experienced problems with Brown Rice and had filed a complaint with the state contractors board and the Wrights informed Meeks that the construction loan provided sufficient funds to pay Meeks.

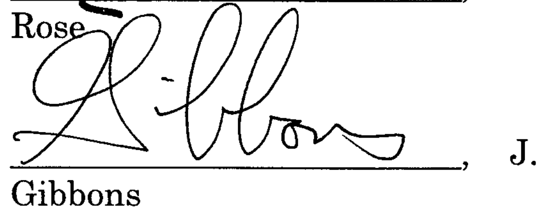
The district court is charged with evaluating the evidence and the witnesses' credibility,[13] and substantial evidence supports the court's determination that Meeks applied payments as directed by Brown Rice without further inquiry, continued to sell to Brown Rice and did not contact the Wrights until Brown Rice had incurred large debts on the Wright account. Therefore, the district court did not err as a matter of law in applying Sherman Gardens, and substantial evidence supports the district court's judgment.

We have considered appellant's remaining assignments of error and have determined that they lack merit. Accordingly, we

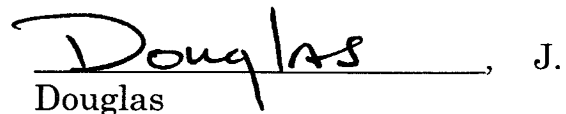
ORDER the judgment of the district court AFFIRMED.

_______________, C.J.
Becker

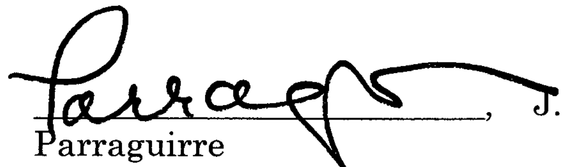
_______________, J.
Rose



_______________, J.
Gibbons



_______________, J.
Douglas



_______________, J.
Parraguirre

---

[13]Olivero v. Lowe, 116 Nev. 395, 403, 995 P.2d 1023, 1028 (2000).

cc: Hon. Brent T. Adams, District Judge
Jeffrey K. Rahbeck
Hale Lane Peek Dennison & Howard/Reno
Lemons Grundy & Eisenberg
Washoe District Court Clerk

HARDESTY, J., with whom, MAUPIN, J., agrees, dissenting:

I would overrule Sherman Gardens v. Longley.[1] Sherman Gardens conflicts with the present mechanics lien statutes and imposes an onerous burden on a supplier to contact an owner every time the contractor makes a payment on a building account.

The district court found that Meeks complied with the mechanics lien statutes by providing notice to the Wrights and their lender of Meeks' intention to supply materials to the Wrights' land. Neither the Wrights nor their lender required lien releases or joint checks with suppliers. Instead, the lender paid Brown Rice directly, which allowed the contractor to misuse the Wrights' money. The record does not support the majority's conclusion that the district court found that Meeks knew of the misapplication of payments from the Wrights' lender by Brown Rice. The district court made no such finding and concluded that both Meeks and the Wrights were innocent in this transaction. Nevertheless, the district court invalidated Meeks' mechanics lien by applying Sherman Gardens because Meeks did not satisfy a duty to investigate the source of Brown Rice's payments and because Meeks was in a better position than the Wrights to monitor the source of payments.

The district court's conclusion demonstrates the policy reasons why Sherman Gardens should be overruled. First, it is unreasonable to invalidate statutorily created mechanics liens when the duty to investigate is so ill defined and the supplier has complied with the mechanics lien statutes. In this case, after some accumulation of charges on the Wrights' job, Meeks attempted to contact the Wrights' lender, but

---

[1]87 Nev. 558, 491 P.2d 48 (1971).

the lender refused to discuss the matter with Meeks. Meeks' investigation of Brown Rice would have been futile because, as the district court found, "Brown Rice's accounting records were inappropriate, confusing, likely inaccurate, and could not have been relied upon by either party to this action." Therefore, applying Sherman Gardens, we must conclude that Meeks breached its duty to investigate solely because it did not contact the Wrights directly. However, requiring suppliers to contact every customer of a contractor directly in order to determine the source of the contractor's cash flow if there is suspicion about the application of a payment is commercially unreasonable and legally unsound.

Second, the owner and lender are in a better position than the supplier to control the source of payments that the owner makes to the contractor. Here, notwithstanding their receipt of pre-lien notices from Meeks, the Wrights and their lender failed to assure that the supplier was paid. Without any statutory authority, Sherman Gardens improperly shifts the burden from the owner (and the lender) to the supplier to determine how the contractor is using the owner's money. Consistent with the intent and purpose of the mechanics lien statutes, when an owner and the lender receive a pre-lien notice, the burden of tracing the contractor's spending rests with the owner or the lender, not the supplier.

I would reverse the judgment of the district court, remand for an accounting of the payments that can be traced and permit enforcement of the mechanics lien for the unpaid balance.

_____________________, J.
Hardesty

I concur:

_____________________, J.
Maupin

SUPREME COURT
OF
NEVADA

(O) 1947A