Pass-Through Claims in Texas: the aftermath of *Interstate Contracting Corp. vs. City of Dallas*

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Nearly two years ago, the Texas Supreme Court decided *Interstate Contracting Corp. v. City of Dallas*, 135 S.W. 3d 605 (Tex. 2004), which formally recognized the validity of pass-through claims in Texas. *Interstate Contracting* held that Texas would join the majority of other states, and over 100 years of federal jurisprudence, permitting contractors to pursue the claims of their subcontractors. This decision has not only paved the way for contractors to prosecute claims on behalf of subcontractors, but may have opened the door for other previously untenable claims, including a general contractor's claim against the architect, an owner's claim against the architect's consultant, and claims against the geotechnical engineer, thus blurring the lines of contractual privity and traditional claims prosecution.

Factual Background of Interstate Contracting

In *Interstate Contracting*, the City of Dallas entered into a lump sum contract with Interstate Contracting Corp. to build two storm water detention lakes and three levees around the Southside Waste Water Treatment Plant in Dallas, Texas. ICC entered into two separate subcontract agreements with Mine Services, Inc. ("MSI") to perform the bulk of the site work.

The instructions to bidders said:

> All material required to complete Phase I construction shall be excavated first from the Northeast Borrow Area. When this resource has been excavated to finish grades the remainder of the required material shall be excavated from the Interior Borrow Lake Area . . . . All material required to complete Phase 1A construction shall be excavated from the Interior Borrow Lake and the channel work adjacent to the levee.[1]

[1] Interstate Contracting Corp. v. City of Dallas, 407 F.3d 708, 714 (5th Cir. 2005).

However, the drawings provided to bidders contained the following disclaimer:

> Subsurface information shown on these drawings was obtained solely for use in establishing design controls for the project. The accuracy of this information is not guaranteed and it is not to be construed as part of the plans governing construction of the project. It is the bidder's responsibility to inquire of the City of Dallas if additional information is available, to make arrangements to review same prior to bidding, and to make his own determinations as to all subsurface conditions. Refer to Section 00220—Soils Investigation Data for additional information.[2]

Specification Section 00220 listed several reports containing the results of soil, subsurface, and geotechnical investigations, and encouraged bidders to examine this data and make their own investigations. The soil borings were made available to bidders at the construction engineer's office, and after executing the subcontracts, MSI contacted the City's engineer—LAN—to obtain the subsurface soil information.[3]

During construction, MSI discovered that the soils at the site were not suitable for use in building the levees—as represented in the documents prepared by LAN. Specifically, MSI discovered that the designated "borrow" site had been previously designated and used as a *spoil dump* for previous City projects and did not have the required PI. Instead of using the soils from the lake excavation, as originally intended, MSI was forced to manufacture suitable fill materials by mixing sand with the limited quantities of clay available at the site. Obviously, the process of manufacturing the fill material slowed construction, and substantially increased MSI's costs.

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[2] *Interstate Contracting Corp*., 407 F.3d at 714.

[3] Interstate Contracting Corp. v. City of Dallas, 2000 WL 1281198 (N.D. Tex.) (memorandum opinion).

ICC filed suit against the City, for itself and on behalf of MSI, alleging breach of contract, quantum meruit, breach of implied warranty, and fraudulent inducement. The City, in turn, filed a third-party petition against LAN for breach of contract and breach of implied warranty.[4] The trial court ultimately dismissed the City's claims against LAN.[5]

Despite the City's objections, the trial court allowed ICC to pursue the claims largely on behalf of MSI. After an 11-day jury trial, the jury found that the City had breached its contract with ICC and had breached the implied warranty to provide accurate and suitable plans and specifications. The City appealed.

The Fifth Circuit was unable to discern whether Texas recognized pass-through claims, and therefore, certified the question to the Texas Supreme Court. The Supreme Court, after reviewing the law in other jurisdictions, ultimately held that Texas would permit a contractor to pursue claims on behalf of its subcontractor, provided the contractor remains liable to the subcontractor.

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[4] *Interstate Contracting Corp.*, 2000 WL 1281198 (N.D. Tex.). LAN argued that the City's breach of contract claim was simply an indemnity claim masked as breach of contract. After a hearing, the district court dismissed the City's indemnity claim against LAN finding no enforceable contractual indemnity and no common law right to indemnity under these circumstances.

[5] 2000 WL 1281198 (N.D. Tex.). The court ruled that the City did not have a valid indemnity claim, and could not seek contribution from LAN.

> The City's right to claim contribution is derivative of Interstate's right to recover from LAN. Because LAN was never a party to the contract between Interstate and the City, Interstate has no right to seek contribution from LAN under the contract between Interstate and the City. Accordingly, the City has no right to seek contribution from LAN under a breach of contract cause of action.

Because ICC's claims against the City "sounded in contract alone" (the alleged injury was purely economic loss to the subject of the contract itself), ICC's claims against the City were purely contractual. Thus, the City had no right of contribution from LAN.

The case went back to the Fifth Circuit to determine whether the City was liable to ICC and MSI for the allegedly defective contract documents regarding the subsurface soil conditions. ICC argued that the plans and specifications provided by the City were defective because they represented that ICC could obtain sufficient levee-fill material from the on-site locations. Alternatively, ICC argued that the City breached the contract by failing to provide the soil information referenced in the specifications.

The City, on the other hand, argued that the contract placed the risk of subsurface conditions on ICC, and therefore, it had not duty to provide any soil information to ICC. After a lengthy opinion examining *Lonergan v. San Antonio Loan & Trust Co.*, 104 S.W. 1061 (Tex. 1907) and its progeny, the Fifth Circuit held that the contract placed the risk of defective plans and specifications on ICC, and that ICC waived any right to claim that the City breached the contract by not providing the soil reports by bidding on the project without the soil reports.

The City prevailed because of the language in the instructions to bidders, which became part of the contract documents. The relevant portions relied upon by the court included the following:

- [t]he CONTRACTOR represents that he has satisfied himself as to the subsurface conditions at the site of the work . . . . [the contract documents] including subsurface conditions, are for information purposes only and are not warranted or represented in any manner to accurately show the conditions at the site of the work . . . All risks of differing subsurface conditions shall be borne solely by the CONTRACTOR;

- [CONTRACTOR] shall bear all losses, if any, resulting on account of the amount and character of the work, or because the conditions under which the

work must be done are different from what were estimated or anticipated by him . . .;

- BIDDERS are required, prior to submitting any proposal, to review the plans and specifications, proposals, contract and bond forms carefully; to visit the site of the work; to examine carefully local conditions; to inform themselves by their independent research, tests and investigations of the difficulties to be encountered and judge for themselves the accessibility of the work and all attending circumstances affecting the cost of doing the work . . . BIDDERS shall rely exclusively upon their own estimates, investigations, tests and other data which are necessary for full and complete information . . . .

Based on this language, the Fifth Circuit had no trouble finding that the contract unambiguously placed the risk of defective plans and specifications on ICC. Since ICC bore the risk of defective plans, the City did not breach the contract with ICC when it provided the defective plans. Moreover, the court held that ICC waived any right to claim the City breached the contract by not providing the soil reports when ICC chose to bid on the project without the reports. "ICC was not forced to bid on this project, but chose to do so, knowing it did not have all of the information it wanted. In doing so, it assumed the risk that the site's conditions might differ from its expectations."[6]

Pass-Through Claims

The Supreme Court provided a very simple definition for pass-through claims: It is a claim (1) by a party who has suffered damages . . ; (2) against a responsible party with whom it has no contract . . ; and (3) presented through an intervening party . . . who has a contractual relationship with both.[7] The only requirement for a valid

[6] *Interstate Contracting Corp.*, 407 F.3d at 724.

[7] Interstate Contracting Corp. v. City of Dallas, 135 S.W.3d 605, 610 (Tex. 2004).

pass-through claim is that the general contractor must be liable to the subcontractor, even if that liability is contingent upon an eventual recovery from the owner.

The requirement that the contractor remain liable to the subcontractor is a well-established requirement of pass-through claims in federal courts, as noted by the court in *Severin v. United States*, 99 Ct. Cl. 435 (1943). In *Severin*, the contractor agreed to build a post office in accordance with the drawings and specifications. The architect hired by the Government was required to furnish models to the contractor for use in building the marble caps and ornamental work. The contractor and his subcontractor, who was hired to cut the marble, were delayed because the architect failed to deliver the models on time. The models were not delivered on time because "the contract for the models had not been awarded because of faulty designs" furnished to the architect. The Government approved a change order extending the contract time, but refused to give the contractor, or his subcontractor, a change order for the additional costs associated with the delays.[8]

Severin held that the contractor was permitted to recover from the Government for its own damages, but was not permitted to recover on behalf of its subcontractor.

> We have, then, a case in which plaintiffs are suing for damages sustained by themselves as a result of the Government's breach of contract and also for damages sustained by another person, a subcontractor. Plaintiffs may, of course, recover for their own loss . . . . [However for the claims of the subcontractor] we think plaintiffs may not recover. The subcontractor could not sue the Government since it has not consented to be sued, so far as relevant to this case . . . .[9]

[8] *Severin*, 99 Ct. Cl. 435, *5. The general contractor requested $73.71 for additional overhead, and the subcontractor requested $702 for additional labor and rental costs, and $35.10 for overhead. The total claim was for $810.81.

More importantly, however, the court held that the contractor was not permitted to recover on behalf of its subcontract because the contractor did not remain liable to its subcontractor. The subcontract stated:

> The Contractor or Subcontractor shall ***not*** in any event be held responsible for any loss, [damages], detention or delay caused by the Owner or any other Subcontractor upon the building . . . or by any other cause beyond the control of Contractor or Subcontractor . . . .[10]

Because the contractor was not liable to the subcontractor, the subcontractor's claim was independent of the contractor's, and court held that the subcontractor could not, independently, sue the government. This is essentially the holding in *Interstate Contracting*, however, *Interstate Contracting* is factually distinguishable from *Severin* because ICC remained liable to MSI, even though that liability was contingent on a recovery from the City. The agreement between ICC and MSI contained the following provision:

> In the event SUBCONTRACTOR has a claim for which the Owner may be responsible, the CONTRACTOR, in its sole discretion, may initiate with the Owner, at the SUBCONTRACTOR'S expense and which shall include attorney's fees, any dispute or claim procedures provided for in the Contract Documents for the use and benefit of SUBCONTRACTOR: otherwise SUBCONTRACTOR shall have full responsibility for the preparation of its claims and shall bear all expenses thereof, including attorney's fees.
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> **CONTRACTOR shall be liable to SUBCONTRACTOR only to the extent of the amount, if any, actually awarded as a result of the disputes [sic] process:** SUBCONTRACTOR shall be entitled only to the amount, if any, actually awarded as a result of the disputes process:

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[9] *Id*.

[10] *Id*. at *6 (emphasis added).

> and such amount when received by CONTRACTOR from the Owner shall satisfy and discharge CONTRACTOR from any and all liability to SUBCONTRACTOR for or on account of the acts or omissions of the Owner or its Architect or Engineer.[11]

Here, ICC was liable to its subcontractor, but only for any amounts actually recovered from the City, which satisfied the Supreme Court's requirements for pass-through claims.

> Conditional liability as expressed in a subcontract, liquidating agreement, or some other type of claims-presentment arrangement is sufficient to prove liability, even when the agreement provides that the contractor has no obligation to pay the subcontractor unless and until it recovers from the owner.[12]

An owner can defeat a subcontractor's pass-through claim if it proves that the contractor would "not be liable to the subcontractor if it refused to present the pass-through claim or to remit the recovery to the subcontractor."[13]

Advantages of Pass-Through Claims

Pass-through claims avoid issues of contractual privity, because the subcontractor avoids having to pursue its claims against the contractor first, and therefore reduces the amount of litigation. Reducing the amount of litigation promotes judicial economy and thus reduces the number of cases on the judge's docket. However, getting around contractual privity is no small task.

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[11] *Interstate Contracting Corp.*, 135 S.W.3d at 608 (emphasis added).

[12] *Interstate Contracting Corp.*, 135 S.W.3d at 619.

[13] *Id*. at 620. The court also noted that in Texas, a contractor is statutorily required to promptly pay its subcontractors proportionately from any amount paid by an owner attributable to work performed under a subcontract. Since the Prompt Pay Act cannot be waived, the contractor "will be conditionally liable to the subcontractor for any amount recovered from the owner that is attributable to the subcontractor's work."

It goes without saying that before the advent of pass-through claims, an owner was not liable to a subcontractor for breach of the owner/general contractor agreement.[14]

> In order for a subcontractor to recover on his contract against a property owner, he must establish that he was in privity of contract with the property owner. As a general rule, in the absence of an express contract making the owner liable, the compensation of persons who perform labor for or furnish material to a prime contractor is to be paid by the prime contractor and not by the owner, although the work is done under the direction of and in accordance with the plans furnished by the owner. The subcontractor or materialman must look to the prime contractor for payment, because, in the absence of an express contract, there is no privity between the subcontractor, employed by the prime contractor, and the owner. The liability of the owner is only to the prime contractor, who is liable to the subcontractor.[15]

To avoid issues of contractual privity, subcontractors often claim to be third-party beneficiaries to the owner/general contractor agreement. However, subcontractors usually cannot satisfy the stringent third-party beneficiary requirements in Texas.

> Contracts between property owners, general contractors, and subcontractors are governed by general contract principles; absent clear evidence to the contrary, a property owner is not considered a third-party beneficiary of a contract between a general contractor and a subcontractor. Mere knowledge that the property owner will benefit from the contract is insufficient to establish a third-party beneficiary arrangement.[16]

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[14] George v. Hall, 371 S.W.2d 874, 876 (Tex. 1963).

[15] City of Corpus Christi v. Acme Mechanical Contractors, Inc., 736 S.W.2d 894, 898 (Tex. App.—Corpus Christi 1987, writ denied).

[16] *Acme*, 736 S.W.2d at 898.

The privity requirement cuts both ways, however, and owners have also been unable to pursue direct actions against subcontractors. In *Rahme v. Raymond*, the court held that the owner could not sue the subcontractor directly for breach of contract, absent contractual privity.

> [Owner] did not have a contractual relationship with [subcontractor]. [General contractor] contracted with [subcontractor] and [owner] in turn contracted with [general contractor]. [Owner] was not a party to and there is no evidence to support a finding that he was a third-party beneficiary of [subcontractor's] contract with [general contractor] . . . [Owner] could have sued [general contractor] for breach of contract but did not do so. [General contractor] in turn could have sued [subcontractor] for breach of contract. Lacking any privity of contract with [subcontractor], [owner] cannot recover from [subcontractor] for breach of contract."[17]

Much to their chagrin, general contractors have been unable to maintain direct claims against the architect or the engineer.[18] General contractors are not third-party beneficiaries to the architect/owner contract. "The fact that a contractor will benefit and profit from plans that are carefully and professionally drawn, and from specifications that are clear and precise, is an *incidental* benefit that accrues to the contractor."[19]

With the advent of pass-through claims, subcontractors are now able to avoid legal barriers to claims directly against the owner. Likewise, owners should be able to maintain claims directly against the subcontractors. Pass-through claims, therefore,

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[17] Raymond v. Rahme, 78 S.W.3d 552, 561-62 (Tex. App.—Austin, 2002 no pet.).

[18] Bernard Johnson, Inc. v. Continental Constructors, Inc., 630 S.W.2d 365 (Tex. App.—Austin 1982, writ ref'd n.r.e.).

[19] *Id*. at 371 (emphasis added).

allow the parties to avoid privity obstacles and difficult third-party beneficiary arguments. While pass-through claims may resolve some issues inherent in contract-based causes of action, they do not afford any greater benefit to claimants for tort-based claims.

In prosecuting a pass-through claim, a subcontractor must overcome the economic loss rule to succeed on a negligence or other tort-based claim. The economic loss rule precludes recovery of economic losses in negligence claims when the loss is the subject matter of a contract between the parties.[20]

Barring personal injury or *other* property damage, any claim arising from the construction project undoubtedly will be damages to the subject matter of the contract. Therefore, the economic loss rule will almost always bar a negligence claim arising from a construction project, even in the context of a pass-through claim.

The Future of Pass-Through Claims after Interstate Contracting

The Supreme Court limited its holding to "construction contracts involving owners, contractors, and subcontractors." Conspicuously absent is any reference to the architect, engineer, or any of the other parties on the construction team. It is only a matter of time before a party argues that *Interstate Contracting* applies with equal force to disputes between: (1) the general contractor and the architect; (2) the owner and the architect's consultant; or (3) the general contractor or the architect and the geotechnical engineer.

[20] Coastal Conduit & Ditching, Inc. v. Noram Energy Corp., 29 S.W.3d 282, 285 (Tex. App.—Houston [14th Dist.] 2000, no pet.) (citing *Southwestern Bell Tele. Co. v. DeLanney*, 809 S.W.2d 493, 494 (Tex. 1991); *Jim Walter Homes, Inc. v. Reed*, 711 S.W.2d 617, 618 (Tex. 1986)).

If a subcontractor is permitted to pass its claim through the general contractor against the owner, why shouldn't the general contractor be permitted to liquidate its claim vis-à-vis the owner, and pursue the claim directly against the architect? Although it may be true that such pass-through claims would reduce the amount of litigation, there are compelling reasons such pass-through claims should not be permitted.

The first and most obvious reason is that the Supreme Court expressly limited its holding to pass-through claims between the subcontract and the owner. The court wisely declined to apply its analysis to all construction dispute because the potential ramifications was (and remains) unknown.

Second, the duties owed by the owner to the contractor are essentially the same as the duties owed by the contractor to its subcontractor. The general contractor has promised to construct a project for the owner in exchange for a sum of money. The subcontractor, in turn, has agreed to construct a portion of the project for the general contractor. If the general contractor would be entitled to additional compensation from the owner, the subcontractor is, therefore, also entitled to additional compensation.

This rationale does not apply when considering a general contractor's pass-through claim against an architect because the owner and general contractor do not share the same responsibilities with respect to the architect as the subcontractor and general contractor share with respect to the owner.

However, in one case the court did allow a general contractor to prosecute a pass-through claim against the owner's consulting engineer. In *Rice Lake Contracting Corp. v. Rust*, 616 N.W.2d 288 (Minn Ct. App. 2000), the general contractor agreed to improve two sewage treatment plants for the City. The general contractor sued the City claiming it was owed an additional $2 million for unanticipated rock excavation. The parties executed a liquidating agreement allowing the general contractor to prosecute the claim against the City's engineer.

The City and the general contractor entered into a settlement agreement where the City agreed to pay the general contractor $200,000 immediately, and almost $1.6 million through a *conditional* promissory note. The conditional payment was to be funded by the recovery, if any, from the claims against the engineer. The general contractor agreed that it would finance the suit against the engineer and would exercise full control over the prosecution of the case.

At trial, the jury found the engineer caused the City to incur $1.9 million in damages as a result of its negligent preparation of the contract documents and negligent supervision of the work. In accordance with the previously executed settlement agreement and conditional promissory note, the judge entered judgment against the engineer for $1,785,402 (the amount of the conditional promissory note, plus the $200,000).

The engineer appealed, claiming that the City never incurred any damages since the promissory note was conditional. The court disagreed, holding that the City's obligation to pay the general contractor "ceased to be conditional once the jury

determined" that the contractor was owed $2 million by the City, and the engineer was liable for $1.9 million to the City.[21]

Other Considerations

The Texas Supreme Court held that pass-through claims were not assignments, and that pass-through claims did not violate *State Farm Fire & Cas. Co. v. Gandy*, 925 S.W.2d 697 (Tex. 1996).[22] However, the subcontractor prosecuting the claim in the name of the general contractor is bound by the terms in the contract between the owner and the general contractor. As such, an arbitration clause will require the parties to prosecute the claim in arbitration.

A standard AIA A201-1997 contract, however, contains an anti-consolidation clause preventing the architect from being joined in the arbitration between the owner and the general contractor.[23] If a general contractor is allowed to pass its claims

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[21] Rice Lake Contracting Corp. v. Rust, 616 N.W.2d 288 (Minn Ct. App. 2000).

[22] In *State Farm v. Gandy*, the court held that the assignment in that case was void as being against public policy because it (1) tended to spur additional and caustic litigation rather than putting the matter to rest; and (2) distorted the litigation by causing parties to take positions contrary to their natural interests. Justice Jefferson noted that a pass-through claim did not present the same issues as in *Gandy*, because pass-through claims tend to facilitate efficient litigation.

[23] The General Conditions of the Contract for Construction, AIA Document A201-1997®:

> § 4.6.4 Limitation on Consolidation or Joinder. No arbitration arising out of or relating to the Contract shall include, by consolidation or joinder or in any other manner, the Architect, the Architect's employees or consultants, except by written consent containing specific reference to the Agreement and signed by the Architect, Owner, Contractor and any other person or entity sought to be joined. No arbitration shall include, by consolidation or joinder or in any other manner, parties other than the Owner, Contractor, a separate contractor as described in Article 6 and other persons substantially involved in a common question of fact or law whose presence is required if complete relief is to be accorded in arbitration. No person or entity other than the Owner, Contractor or a separate contractor as described in Article 6 shall be included as an original third party or additional third party to an arbitration whose interest or responsibility is insubstantial. Consent to arbitration involving an additional person or entity shall not constitute consent to arbitration of a Claim not described therein or with a person or entity not named or described therein. The foregoing agreement to arbitrate and other

through the owner against the architect, the general contractor is thus allowed to circumvent the anti-consolidation clause, but it will bound by the arbitration clause nonetheless.

Pass-through claims can also benefit subcontractors by avoiding sovereign immunity. In *Interstate Contracting*, there was some concern over whether the pass-through claim could overcome sovereign immunity. At the time of oral arguments, several cases were pending at the Texas Supreme Court on sovereign immunity, and MSI was concerned that the Supreme Court would jump to the conclusion that it was not a party to the contract between ICC and the City of Dallas, and summarily dismiss the claim based on sovereign immunity. In fact, the City's Brief to the Supreme Court devoted a considerable amount of time arguing issues of sovereign immunity. Since the case was eventually decided under a *Lonergan*-theory, sovereign immunity never became an issue.

However, the Federal District Court for the Northern District of Texas recently addressed the issue of sovereign immunity in the context of a subcontractor's pass-through claims against a governmental entity. The court held that a subcontractor's ***pass-through*** claims were not barred by sovereign immunity. In *Hensel Phelps Construction Co. v. Dallas/Fort Worth Int'l Airport Bd.*, 2005 WL 1489932, the court said:

> agreements to arbitrate with an additional person or entity duly consented to by parties to the Agreement shall be specifically enforceable under applicable law in any court having jurisdiction thereof.

> Under Texas law, a contractor who is liable to a subcontractor for damages the subcontractor sustained can, pursuant to a pass-through agreement, bring an action against the owner for the subcontractor's damages. Although in *Interstate Contracting* the Texas Supreme Court declined to address whether sovereign immunity must be waived before a pass-through claim against a governmental entity could be recognized, this court holds that this conclusion follows from Texas law.
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> The Texas Supreme Court has repeatedly held that, "[w]hen a governmental entity contracts with a private party, . . . it is liable on its contracts as if it were a private party." Under *Interstate Contracting*, a contractor who is in privity of contract with an owner has standing to assert against the owner the claims of its subcontractor for which the contractor remains liable to the subcontractor. It therefore follows that, when a governmental entity-owner waives immunity from liability by entering into a contract with a contractor, it also waives immunity from liability with respect to all pass-through claims that the contractor may lawfully assert under the contract.[24]

The court held, however, that the subcontractor's ***direct claims*** against D/FW were barred by sovereign immunity because D/FW had not agreed to waive immunity from liability since there was no contract between D/FW and the subcontractor.[25]

Ethical Considerations

It may be tempting, especially at the beginning of a dispute, to execute a joint prosecution agreement to represent both the subcontractor and general contractor in claims against the owner, or both the general contractor and owner in claims against the architect. Given the complexity of pass-through claim litigation, the potential for conflicts of interest can be a trap for the unwary.

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[24] Hensel Phelps Construction Co. v. Dallas/Fort Worth Int'l Airport Bd., 2005 WL 1489932 (N.D. Tex.) (citations omitted).

[25] *Hensel Phelps*, 2005 WL 1489932 *4.

It is critically important to specifically identify the client so that all future decisions regarding confidentiality, conflicts, and privilege are understood. Remember, a lawyer does not have to be paid or have an engagement letter to form an attorney-client relationship. To establish an attorney-client relationship, the parties must explicitly, or by their conduct, manifest an intention to create it. In other words, an attorney-client relationship may be established either expressly or impliedly from the conduct of the parties.[26]

It is also important to make certain that the scope of the representation is clear, and that the agreement addresses the costs of prosecuting the claim, including any allocation of fees or recovery.

A potential conflict will almost always arise in joint representation agreements, and particularly in pass-through claim prosecution cases. The comments in the Texas Rules of Professional Conduct state:

> An impermissible conflict may exist or develop by reason of substantial discrepancy in the parties' testimony, incompatibility in positions in relation to an opposing party or the fact that there are substantially different possibilities of settlement of claims or liabilities in question. Such conflicts can arise in criminal cases as well as civil. The potential for conflict of interest in representing multiple defendants in a criminal case is so grave that ordinarily a lawyer should decline to represent more than one co-defendant. On the other hand, common representation of persons having similar interests is proper if the risk of adverse effect is minimal and the requirements of paragraph (b) are met.[27]

[26] Vinson & Elkins v. Moran, 946 S.W.2d 381 (Tex. App.—Houston[14th Dist.] 1997, writ dism'd by agr.).

[27] TEXAS RULES OF PROFESSIONAL CONDUCT, 1.06 (cmt. 3).

In pass-through claim prosecution, there likely will be some conflict of interest. There will be different settlement pressures for the named claimant and the real party in interest. Under a joint representation agreement, you as the lawyer will have a duty of confidentiality to both clients. Neither one of these clients will want their secrets shared with the other. If the conflicts become too severe, the lawyer will obviously have to withdraw from representation. A conflict may not be a concern at the beginning, and will likely be waiveable by the parties. However, as the litigation progresses, the conflict may become too great, requiring the lawyer to withdraw.

Conclusion

The recent development of pass-through claims in Texas may have far-reaching implications for construction litigation. Previously untenable claims by a general contractor against the architect are now at least possible. But with the new-found possibilities come new ethical issues. Attorneys representing pass-through claimants are advised to thoroughly document the agreement so that all parties know who is responsible for the costs of the litigation, how any recovery will be allocated, and for whom the attorney is working. Issues undoubtedly will come up during the course of the litigation that may require the lawyer to make certain disclosures, which can be awkward.

As Texas lawyers struggle to understand the complexities of pass-through claim litigation, the decisions of other states, and most importantly those of federal courts, certainly will provide the needed guidance. For better or for worse, pass-through

claim litigation almost certainly will impact the landscape of construction disputes in the years to come.