Termination for Convenience Clauses - Limitless or Limited Authority to Terminate?

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Is termination for convenience truly at your convenience, as the name of the clause suggests, or are there limits on using such clauses to terminate a contract or subcontract? Before you terminate for convenience, you had better be sure of the answer, because the authority to terminate for convenience without liability for breach of contract will vary depending on whether your contract is subject to federal contract law or state law.

Termination for convenience terms first appeared in federal government contracts about the time of the Civil War to allow the federal government to terminate military procurements that were no longer needed due to technological developments or the end of hostilities. Since then, the clauses have become common in both public and private contracts.

While terms may vary, typical termination for convenience clauses grant broad authority to terminate a contract in exchange for a limited payment to the terminated party, typically for the costs of goods and services furnished, demobilization costs, and a reasonable profit on the work performed. Because a termination for convenience is a mutually agreed right under the contract, such a termination does not constitute a breach of contract that would allow the terminated party to recover its anticipated or lost profits, or other damages allowed for breach of contract.

Federal Law and Federal Contracts

Federal courts interpreting the termination for convenience clause in federal government contracts have said the clause does not give the government unfettered authority to terminate at will. If a terminated contractor can prove the federal government acted in bad faith or abused its discretion when terminating the contract

for convenience, then the termination is a breach of contract entitling the terminated party to breach of contract damages.

To prove bad faith or abuse of discretion, however, the terminated party must generally prove by clear and convincing evidence that the federal government acted with the intent to injure the contractor. This is a high standard of proof, most times not met.

The federal courts have also held a termination for convenience of a federal contract to be a breach of contract when the government entered into the contract knowing it would not honor the contract and thereafter terminated the contract for convenience. Proof of the government?s knowledge is a prerequisite to such a claim.

Most recently, in the April 2013 decision in *Tigerswan, Inc. v. United States*, No. 1:12cv62 (Fed. Cl. 2013), Judge Firestone of the Court of Federal Claims addressed whether the government?s breach of its implied duty of good faith and fair dealing, without a showing of intent to harm the contractor, would be sufficient to state a cause of action for breach of contract for improper termination for convenience. Judge Firestone wrote that breach of the government?s implied duty of good faith and fair dealing can be shown by proof of lack of diligence, negligence or failure to cooperate; proof of bad faith or of intent to harm the contractor is not required. Judge Firestone went on to rule that if the government?s termination for convenience arose from the government?s violation of its implied duty of good faith and fair dealing, then the government can be liable for breach of contract damages and not the limited damages of the termination for convenience clause.

State Law and Public/Private Contracts

Most state courts applying state and common law principles to termination for convenience disputes have imposed a good faith limitation on the authority to terminate for convenience.

For example, in an often cited case, *RAM Engineering & Construction, Inc. v. University of Louisville*, 127 S.W.3d 579 (Ky. 2003), the Kentucky Supreme Court ruled that the exercise of the termination for convenience clause must be in good faith. The court wrote that, in determining whether there was good faith, it would look for a substantial change in circumstances underlying the termination for convenience. In this case, the court did not find that the circumstances changed the bargain or the parties? expectations significantly enough to justify termination.

In *Capital Safety, Inc. v. State Division of Building and Construction*, 848 A.2d 863 (N.J. 2004), the New Jersey court considered whether a state agency?s inability to relocate agency employees during asbestos removal was sufficient grounds to terminate the asbestos contractor for convenience. The court found that the

terminated contractor did not prove the agency acted in bad faith, and, therefore, the termination for convenience was upheld.

In a Maryland case, *Questar Builders, Inc. v. CB Flooring, LLC*, 978 A.2d 651 (Md. 2009), the Maryland Court of Appeals held that termination for convenience clauses in private contracts are allowable and will be enforced subject to the terminating party exercising the clause in accordance with the implied duty of good faith and fair dealing. The court specifically noted, however, that its ruling should not be construed as a commentary on how the court would interpret a termination for convenience clause in a state public works contract.
Compare the Florida court?s decision in *Vila & Son Landscaping Corporation v. Posen Construction, Inc.*, 90 So.3d 563 (Fla. App. 2012), in which the Florida state court rejected a subcontractor?s contention that the general contractor?s termination for convenience to obtain a better price from another subcontractor was in bad faith. The Florida state court further wrote that the termination for convenience was not a breach of the general contractor?s implied duty of good faith and fair dealing. Citing the plain language of the clause, the court held that the general contractor?s exercise of its right to terminate for convenience was not contrary to the reasonable expectations of the contracting parties.

What Does It Mean for You?

Contrary to the implication of the term ?convenience,? a termination for convenience clause is not a carte blanche to terminate without exposure. If you are the terminating party relying on the termination for convenience clause, be sure your grounds for invoking the clause are valid under the law governing your contract. If you are the terminated party, remember that not all terminations qualify for convenience.

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