

TERMINATION FOR DEFAULT

IS IT JUSTIFIED, AND WHAT ARE MY OPTIONS?

INTRODUCTION

The Federal Government inserts certain clauses into its construction contracts in order to protect itself. One such clause is the Termination for Default clause. The Termination for Default clause provides protection by allowing the government to **terminate a contract when the contractor does not perform satisfactorily**, with the contractor becoming liable to the government for any resulting damages.

Because Terminations for Default are challengeable, contractors should be aware of the requisite justifications, procedures, and costs associated with such a drastic measure.

TERMINATION FOR DEFAULT CLAUSE

The Termination for Default clause allows the government to terminate a contract if the contractor fails to perform on time, fails to perform with the diligence to ensure timely completion, or fails to perform work in accordance with the requirements of the contract. Termination for Default is a **“drastic sanction, which should be imposed (or sustained) only for good grounds and on solid evidence.”** See *C-Shore International, Inc. v Department of Agriculture*, CBCA 1697, 10-1 BCA ¶ 34,380.

Simply falling behind schedule does not necessarily warrant a Termination for Default. The government, as the terminating party, has the burden to prove that timely completion would not be possible under the circumstances, or that the contractor’s performance did not meet contractual requirements.

JUSTIFYING TERMINATION FOR DEFAULT

In order to justify a Termination for Default, the FAR requires the Contracting Officer to consider **a number of factors**, including the terms of the contract and applicable regulations, the specific failure and/or excuses of the contractor, and other “pertinent facts and circumstances.” FAR 49.402-3(f).

However, this clause also provides for time extensions if the contractor is delayed by “unforeseeable causes” beyond its control, and where no contractor negligence or fault is found. These situations may be thought of as exceptions to the rule, and include:

- Acts of God or of the public enemy
- Acts of the government in either its sovereign or contractual capacity
- Acts of another contractor in the performance of a contract with the government
- Fires, floods, or epidemics
- Quarantine restrictions
- Strikes
- Freight embargos
- Unusually severe weather, or
- Delays of subcontractors or suppliers at any tier arising from unforeseeable causes beyond the control and without the fault or negligence of both the contractor and the subcontractor or suppliers. FAR 52.249-10(b)(1)(i-ix).

Where such exceptions apply, or where the evidence establishes that the contractor could have indeed completed its performance by the scheduled date (even if extended), then a **Termination for Default is not proper** and will be **converted** into a **Termination for Convenience**. See FAR 52.249-10(c); see also *Preston-Brady Co.*, VABCA No. 1849, 86-2 BCA 18,860 (holding that a Termination for Default was not proper where evidence established that the contractor could have indeed completed performance by the extended date); and *D.W. Sandau Dredging*, ENG BCA No. 5812, 96-1 BCA 28,064 (where the Board determined that the completion date used to determine whether there was a reasonable likelihood of the contractor completing performance in a timely manner was the original completion date plus the appropriate extension of time).

TERMINATION PROCEDURE

Before terminating a contract for Default, the Contracting Officer will usually issue a **“Cure Notice.”** The Cure Notice allows the contractor at least 10 days to cure any defects in the timing or quality of its performance. If the contractor does not cure within 10 days, the Contracting Officer may issue a notice of Termination for Default.

If there is not sufficient time for a cure, the Contracting Officer will typically issue a **“Show-Cause” notice**. That notice directs the contractor to show why its contract should not be terminated for Default. It ensures that the contractor understands the problem and provides an opportunity to respond and provide reasons, exceptions, or other mitigating factors in an effort to persuade the government to not issue the Termination for Default notice. The Show-Cause notice typically requires a response within 10 days of receipt.

COSTS OF TERMINATION

If a contractor is terminated for Default, it is entitled to payment **only for items or work that are accepted** by the government. Additionally, the government has the right to re-procure the work in order to complete the project, and any excess **re-procurement costs are passed on to the defaulted contractor**. Negative indications of a contractor’s performance are often attached to the Defaulted contractor, including negative **CPARS** rating or other performance reviews that can damage the contractor’s good reputation. Obviously, this would be a harsh result for any contractor.

Conversely, if the contractor can persuade the government to convert the Termination for Default into a Termination for Convenience (or prove that the T for D is not warranted, resulting in an automatic conversion to T for C), then the contractor is entitled to recover:

- Costs incurred for work completed and accepted at the time of the Termination
- Costs that are considered allowable, allocable, and reasonable
- Profit on the above costs incurred, and
- Close-out, demobilization, and settlement proposal costs associated with preparing a final cost proposal for submission to the government

This result is much more advantageous to the contractor, and should be planned for and pursued as early as a Default Termination is suspected.

CONCLUSION

Contractors should educate themselves on what constitutes grounds for a Termination for Default. Knowing what the government will need to prove-up when justifying a Termination for Default – along with a contractor’s viable

excuses and other options – will provide the best opportunity to successfully challenge the Termination, converting it into a Termination for Convenience or having the Default Termination rescinded and continuing with the work.

Because the consequences of a Termination for Default are so severe, contractors should consider consulting with an expert who has deep experience in these matters. After all, your reputation and bottom-line may be on the line.

In the end, you will be glad you made the call; by the way, it's a FREE CALL.

EXCELL CONSULTING: “HERE TODAY FOR YOUR TOMORROW.”

Author's note: The information contained in this article is for general informational purposes only. This information does not constitute legal advice, is not intended to constitute legal advice, nor should it be relied upon as legal advice for your specific factual pattern or situation. – John G. Balch, CEO CPCM