

What To Know When a Government Contract Is Terminated

Fact checked on May 24, 2012.

Almost every federal contract contains a clause allowing termination for convenience or default. Termination for convenience allows the federal government to terminate all or part of a contract for its convenience, while termination for default means the government doesn't think you're performing adequately.

The government can terminate a contract for their convenience, or in the case of most contracts in excess of \$25,000, for default when the government believes that a contractor failed to perform in accordance with the provisions of the contract.

Termination for Convenience

A termination for convenience (T for C) allows the federal government to terminate all or part of a contract for its convenience. This type of termination protects the government's interests by allowing cancellation of contracts for products that become obsolete or unneeded. The termination does not arise from any fault on the part of the contractor.

If the federal government terminates your contract for its convenience, it must notify you in writing. The notice of termination must contain the effective date of the termination, the extent of the termination, and any special instructions.

The contract termination notice and clause generally require a contractor to stop work immediately on the terminated portion, to terminate all affected subcontracts, to perform any specified unterminated portions of the contract, and to proceed promptly to settle termination claims, both its own and those of its subcontractors.

If you receive a termination notice and fail to follow these directions, you do so at your own risk and expense. You should also receive detailed instructions as to the protection and preservation of all property that is, or may become, government-owned.

After termination, the government is required to make a fair and prompt settlement with you. Generally speaking, settlement takes the form of a negotiated agreement between the parties. The idea is to agree on an amount that will compensate you fully and fairly for the work you have done and for any preparation you have made for the terminated portion of the contract. A reasonable allowance for profit is also included. Settlement of cost-reimbursement contracts is somewhat simpler than that of fixed-price contracts, since you will have been reimbursed on a cost basis from the beginning of the contract.

You are entitled to recover all allowable costs incurred in settling a termination for convenience. Those costs may include the following:

- Preparation and presentation of claims
- Termination and settlement of subcontracts
- Storage, transportation, protection and disposition of property acquired or produced for the contract
- Other termination activities

The federal government retains the right to approve or ratify any settlements made with subcontractors. When you and the government agree to all or part of your claim for compensation as a result of the termination, a written amendment (known as a settlement agreement) is made to the contract.

Generally, termination halts regular payments to you under the contract. However, since you may have money tied up in finished and unfinished products, materials and labor, most termination clauses provide you with interim financing through partial payments.

Termination for Default

A termination for default (T for D) means that the government may terminate all or part of a contract for anything that was done that was not in the interest of the government, including:

- Attempted fraud
- Failure to meet quality requirements
- Failure to deliver the supplies or perform the services within the time specified in the contract
- Failure to make progress and that failure endangers performance of the contract
- Failure to perform any other provisions of the contract.

Before terminating a contract for default because of your failure to make progress or to perform, the contracting officer will usually give you a written notice, called a "cure notice." That notice allows you at least 10 days to cure any defects. Unless the failure to perform is cured within the 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 usually send a show-cause notice. That notice directs you to show why your contract should not be terminated for default. It ensures that you understand your predicament, and your answer can be used in evaluating whether circumstances justify default action.

Upon termination for default, you are entitled to payment on the contract only for items accepted by the government. Under a default clause, the government has the right to repurchase the item elsewhere and charge any excess re-procurement costs to the contractor.

If you can show that your failure to perform the contract is excusable, your contract cannot be terminated for default. To be excusable, the failure must be beyond your control and not caused by your fault or negligence.

Examples of excusable failure include:

- Acts of God
- Acts of a public enemy
- Acts of government
- Fires
- Floods
- Epidemics
- Quarantine restrictions
- Strikes
- Freight embargoes
- Unusually severe weather

Here's a happy thought! If, after termination, you are found not to be in default or the default is found to be excusable, the termination will be treated as one for the convenience of the government. This means that not only will you have removed the tarnished image that a T for D gives a contractor, but you will also get some of your money back as well!