

Termination for Convenience Clause

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The general rule is that neither party to a contract may avoid performance of its duties to the other unless the other party first materially breaches the contract. For example, a contractor may not refuse to perform its work under a contract unless the owner does something that would constitute a material breach, such as failing to make payments in accordance with the agreed-upon payment terms. Similarly, absent a material breach by a contractor, a project owner cannot simply call it quits and pay the contractor only for the work performed up to the date of cancellation. Indeed, a party wrongfully terminating a contract or otherwise refusing to perform entitles the other party to be placed in the same position it would have been absent the first party's breach. In the case of the contractor, it would be entitled to recover all costs incurred plus the profit it can show it would have realized had it been allowed to perform the entire contract.

The Termination for Convenience contract clause is a provision that entitles usually one party to a contract to terminate it at any time without any liability for damages the other party might suffer as a result of the termination. A typical Termination for Convenience clause reads as follows:

The Owner may terminate this Agreement for its convenience at any time upon providing five (5) days written notice to the Contractor. In such case, the Contractor shall be entitled to receive as full compensation for all services performed hereunder payment for all Work performed prior to the date of termination, together with all retainage withheld in accordance with Article 4. Payment of such compensation is the sole and exclusive remedy of the Contractor for termination of this Agreement by Owner hereunder and the Contractor shall not be entitled to, and hereby waives, claims for lost profits and all other damages and expenses.

A Termination for Convenience clause usually is without limitation and an owner is free to terminate for any reason – even no reason at all. Consequently, the clause is regarded as a potential for abuse. For example, nothing would prevent an owner of a project from terminating for convenience a contractor during initial mobilization because the owner received a lower project price from another contractor.

Obviously, in the public contracts arena, Contractors have no ability to negotiate contract terms and, therefore, must accept a public entity's Termination for Convenience clause. However, the good news is public entities rarely abuse their termination for convenience rights. On the other hand, contractors performing private construction work are generally able to negotiate their contract terms. In such cases, consider the following:

- If possible, eliminate the Termination for Convenience clause altogether from the contract;
- If the owner insists on the clause, try to narrow down those circumstances under which the owner would desire to terminate the contract, such as, for example, the loss of project financing or governmental approval of the project, and draft language into the clause limiting termination rights to those enumerated circumstances;
- Alternatively, attempt to negotiate more favorable compensation in the event of termination for convenience and include such payment parameters into the clause; and
- Lastly, if the contractor must agree to include a Termination for Convenience clause in a prime contract, it must insure that all subcontracts and purchase orders similarly include Termination for Convenience clauses that contain identical payment terms as those contained in the prime contract. Failure to do so will subject the contractor to liability for damages incurred by subcontractors and suppliers with no ability to recover same from the owner.

The same strategy applicable to contractors applies equally to subcontractors except that subcontractors should first determine whether the prime contract contains a Termination for Convenience clause. If it does, the subcontractor must realize that the prime contractor is very unlikely to delete the clause from the subcontract because it requires protection in the event of owner termination. However, the subcontractor should insist that the prime contractor's right to terminate the subcontractor for convenience is limited to only if the owner terminates the prime contractor. If, on the other hand, the prime contract does not contain a Termination for Convenience clause, the subcontractor should revert to the same strategy described above for negotiations with an owner.