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Terminations For Convenience And Creedence Clearwater Revival: "Bad Moon Rising"

By Bruce Shirk

> ***The U.S. won't be able to avoid a crippling debt crisis as long as Congress refuses to include defense spending . . . in the mix of program cuts to reduce federal spending, the co-chairman of the presidential debt commission said Tuesday.***
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> *Army Times*, March 8, 2011, available here
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> ***Terminations for the Government's convenience developed as a tool to avoid enormous procurements upon completion of a war effort. Because public policy counseled against proceeding with wartime contracts after an end to [Civil War] hostilities the government, under certain circumstances, began to terminate contracts and settle with the contractor for partial performance.***
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> *Krygoski Constr. Co. v. United States,* 94 F.3d 1537 (Fed. Cir. 1996)

It now is generally accepted that the federal budget must be reduced drastically, although just how drastically and where is still a matter for debate. But public policy already has "counseled against proceeding" with certain procurements, and the process of terminating increasing numbers of contracts for the convenience of the government already may have begun in earnest, as indicated by the following developments:

- On January 13, 2011, the Commandant of the Marine Corps recommended cancellation of the Marine Corps Expeditionary Fighting Vehicle ("EFV") because its costs had become "too onerous." He did so in the face of the outspoken opposition of many senior Marine generals who believed that without the EFV the Marines would "have to begin abandoning the [amphibious] mission that has long been at the core of their identity."

- On February 4, 2011, the White House web site boasted that it has reduced contract spending from an annual 12% increase between 2000 and 2008, to a FY 2010 reduction to "$535 billion versus $550 billion in the prior year." To accomplish this feat, agencies have, among other things, "*ended unnecessary or unaffordable contracts,* including contracts for weapons systems, information technology, financial management, operations and maintenance, transportation and fuel." (emphasis in original). But the White House cautions that "[t]here is still much to be done to make sure every contracting dollar is well spent."

This posting offers a brief review of the history and principles of the government's right to terminate for convenience, including two recent decisions that illustrate just how minimal courts and Boards of Contract Appeals view the limits that exist on the Government's authority to exercise that right.

The Government's termination right is unilateral; it is not "balanced by a comparable right or advantage to the contractor."

As the Federal Circuit explained in *Krygoski*, the concept of termination for convenience first appeared at the end of the Civil War. *Krygoski Constr. Co. v. United States,* 94 F.3d 1537, 1541 (Fed. Cir. 1996) (citations omitted). It since has evolved into a powerful and mandatory contractual provision that gives the government the right to terminate a contract "in whole or . . . in part . . . [without cause] if . . . termination is in the Government's interest." FAR 52.249-2 Termination for Convenience of the Government (Fixed Price) (May 2004). The clause limits contractor recovery to reasonable costs of preparing the termination settlement proposal, costs actually incurred in performance of the contract work, plus a reasonable profit on those costs, thereby relieving the government of the obligation of paying anticipatory profits (*i.e.*, breach damages) on the work that, but for the termination, the contractor would have performed. *See Dairy Sales Corp. v. United States,* 219 Ct. Cl. 431, 593 F.2d 1002 (1979). Moreover, if the government can show that the contractor would have incurred a loss on a fixed price contract had it been completed, then (i) profit will not be allowed even on the work performed and (ii) the costs of performance recovered will be reduced in an amount proportionate to the projected loss. FAR 49.203(a); *Systems & Computer Info., Inc.*, ASBCA No. 18458, 78-1 BCA ¶ 12,946. These provisions give the government a broad and indeed unique right not "balanced by a comparable right or advantage to the contractor." *District of Columbia v. OFREGO,* 700 A.2d 185, 199 (D.C. 1997), *citing* John Cibinic, Jr., & Ralph C. Nash, Jr., *Administration Of Government Contracts*, 1073-1075 (3d ed. 1995).

The Government's right to terminate for convenience is extremely difficult to overturn.

The government's right to terminate a contract for convenience generally has been viewed as virtually bullet-proof. For many years the contractor was required to present "well nigh irrefragable proof" of bad faith or abuse of discretion on the part of the

contracting officer to justify a finding of breach. *Kalvar Corp. v. United States*, 211 Ct. Cl. 192, 543 F.2d 1298 (1976), *cert. denied*, 434 U.S. 830 (1977). Then, for a brief period, it was believed that the government must show some change in circumstances between contract award and termination to justify exercise of its right or risk a determination that its termination was undertaken in bad faith. *Torncello v. United States,* 231 Ct. Cl. 20, 681 F.2d 756 (1982). But the Federal Circuit severely limited *Torncello* in 1996 by ruling in *Krygoski* that *Torncello's* changed circumstances doctrine could no longer apply in light of the Competition in Contracting Act, which "permits a lenient convenience termination standard." For example, a contracting officer may discover that the specifications "inadequately describe the contract work" and "may therefore need to terminate [the] contract for the Government's convenience to further full and open competition." The court did note that "the Government's authority to invoke a termination for convenience has . . . retained limits," *i.e.,* the government can not act in bad faith by, for example, entering into a contract with no intention of performing it or terminating a contract "simply to acquire a better bargain from another source." *Krygoski,* 94 F.3d at 1541,1543. More recent cases have established that bad faith must be proved by "clear and convincing" evidence, including a showing that the contracting officer was motivated by malice towards the contractor, which can be demonstrated by showing, among other things, "a specific intent to injure" or a "conspiracy . . . to get rid of" the contractor. *Am-Pro Protective Agency, Inc. v. United States,* 281 F.3d 1234, 1241 (Fed. Cir. 2002) (citations omitted). The bar to overturning a T for C, plainly, is extraordinarily high.

The Government can terminate for convenience even if it has prior knowledge of facts indicating that it might want to terminate the contract for convenience in the future.

In *McHugh v. DLT Solutions, Inc.,* 618 F.3d 1375 (Fed. Cir. 2010), the CAFC reviewed and reversed a decision of the Armed Services Board of Contract Appeals ("ASBCA") holding that (i) the government had breached a "non-substitution clause" stating that the government agreed not to replace the software it was purchasing "for a period of one . . . year" after the contract expires or is terminated" so that (ii) the government's termination of the contract for convenience was a breach of contract which together made the government liable for "expectation damages." After the contractor delivered the software, the procuring agency realized that its platform was inadequate to support the software and the agency with approval responsibility refused to approve its use. The procuring agency continued to use its existing software, with upgrades, and terminated the contract for convenience of the government. In reversing the Board's holding, the Federal Circuit noted that the Board had "specifically found that [the agency] terminated the contract because its platform was inadequate and it could not obtain approval of the oversight agency, and held that "in light of . . . changed circumstances . . . the government was justified in utilizing the termination for convenience clause in terminating the contract . . . ." But the Court took special care to emphasize that use of the clause was justified "even if the agency had prior knowledge that it might not be successful in deploying the contracted for software," *citing Caldwell v. Santmyer, Inc. v. Glickman,* 55 F.3d. 1578, 1583 (Fed. Cir. 1995) (Court refused to

overturn a termination for convenience where the government has awarded the contract in good faith but, "at the same time, has knowledge of facts supposedly putting it on notice that, at some future date, it may be appropriate to terminate the contract for convenience"); *McHugh,* 618 F.3d at 1378.

However, the Government may not terminate simply to get a better price for performing needed work.

In *Sigal Constr. Corp. v. Gen. Servs. Admin.,* CBCA, No. 508*,* 10-1 BCA ¶ 34,442 (May 13, 2010), the solicitation required a lump sum bid price for base contract work and fixed unit prices for certain restoration work items, the latter accompanied by estimated quantities "for the purpose of estimating offers." The contractor's post-award survey of the quantities for the restoration work revealed that actual quantities for certain of the bid units were substantially in excess of the estimated quantities for those units. Several months after learning how much the actual quantities exceeded the estimated quantities in the solicitation, the GSA requested and received a lower unit price quote from another contractor to perform the work on a number of the affected bid units and suspended the contractor's work on those units. The contractor submitted a certified claim for breach damages, including lost profits for itself and its subcontractors. *Id*. at 169,969. The Contracting Officer denied the claim, arguing that the work in question was not part of the contract specifications in the first place and, in any event, GSA had authority to reduce the scope of work either under the Changes or Termination for Convenience clause. The Board rejected GSA's interpretation of the specifications and found the agency had committed a breach of contract, stating in part:

> One of the few limitations on the Government's right to terminate for convenience is that the Government may not terminate simply to get a better price for performing needed work.

Id. at 169,971.

The Government's actual understanding of its requirements at time of award and termination are key facts in determining the propriety of a termination for convenience.

Sigal Construction and *McHugh* illustrate the narrow contours of the fact patterns that will support a successful challenge to a T for C:

1. A termination likely will not be overturned merely because the contractor shows the government should have known it might later terminate the contract for convenience.

2. But – a termination for convenience can be overturned if the contractor can show the government acted in bad faith because it awarded the contract with no

intention of performing it.

3. And – a termination for convenience can be overturned on the ground of bad faith if the contractor can show that, at the time of termination, the government understood the work was still required, but terminated solely to obtain a better price from another contractor.

Conclusion

Against the foregoing background, contractors may wish to take the following steps to protect themselves from unwarranted terminations for convenience:

- When responding to solicitations, make reasonable efforts to assure that the specifications accurately describe the government's requirements.

- When the government reduces the scope of work of your contract, take all practicable steps to confirm that the government's reasons for doing so reflect its present understanding of its actual requirements, and that the reduction does not reflect an effort to obtain a lower price from another source.

While these steps will not ensure protection, they certainly will reduce the risks.

Authored By:

W. Bruce Shirk
(202) 741-8426
bshirk@sheppardmullin.com