Terminating a contract for 'convenience'

By Michael J. Baker, Esq.

Q: We have a problem contractor who is struggling to complete a project. Our client, the owner, has come to us for advice as to whether the owner should terminate the contractor. We took a look at the contract and determined we could either terminate for fault or terminate for convenience. We understand that if we terminate for fault, we would have to prove that there was some contractual fault on the part of the contractor. Is there any advantage to terminating for convenience, and what specifically is a termination for convenience?

A: Basically, termination for "convenience" provisions in contracts are standard clauses seen in public and private work settings generally allowing one party to terminate a contract, even in the absence of the other party's fault, without suffering any of the usual financial consequences associated with a breach of contract. Absent some restrictive language in the contract provision, the party favored by the clause can terminate the contract at its own will. Courts throughout the United States do not impose a good faith requirement in order to terminate a contractor if let go pursuant to a termination for convenience clause. Please note, when the owner exercises termination for convenience and fires the contractor, the owner must still pay the contractor certain damages, which typically are outlined in the contract or required by applicable law.

Q: We are a consulting engineering firm to an architect on a public works project where the contractor was unable to finish. There was a performance bond in favor of the owner. It is expected that the surety will take over. Generally, what are the surety's obligations in such a situation?

A: If a surety has issued a performance bond for a construction contract, it may become liable under the bond when the principal (in this case, contractor) fails to fully and correctly perform the underlying contract between the principal and the obligee/owner. Typically, the surety's obligations under the performance bond are triggered by the default of the contractor. The surety generally is allowed a reasonable period of time to investigate the circumstances surrounding the default and an opportunity to choose a course of action in performing bond obligations. Keep in mind that a performance bond is a three-part agreement whereby the surety assures that the contractor's performance of the underlying construction contract between the contractor and the owner is performed. The surety can choose to either complete performance or finance the completion of the project. Some of the most common ways the surety completes the project are executing a series of contracts, assignments, and ratification agreements that allow the surety to formally take over the project, or simply contract for its completion. It also may allow the owner to complete the contract, in which case the surety is responsible for costs in excess of the contract price. Additionally, a surety may satisfy its obligation by providing funds to an insolvent contractor to complete the performance.

Q: We were hired as a consultant to provide structural engineering services to an architect. While we were trying to complete the construction documents, we were told by the architect who hired us to stop working and that the owner had cancelled the project. The architect agreed to settle for its fees at 50 percent of the amount due with the owner. However, by the time we were informed of the architect's settlement with the owner, we had almost finished all of the construction documents. The architect has agreed to pay us for only 50 percent of our work and refuses to pay for the 95-percent-completed construction documents. Do we have a claim against the architect for the balance of the fees?

A: Absent a written contract stating otherwise, or an agreement to the contrary, you would be entitled to the reasonable value of services that were performed. If there was a written contract, you need to read the contract carefully because most architect/consultant agreements do contain contract clauses that address the situation where the owner cancels or terminates the project and the consequences for compensation due for work performed. It is always a good idea to include in your consulting agreements a provision in the contract that entitles you to recover for work performed up to the point of formal notice that a project is being terminated or suspended, and to recover for reasonable costs associated with stopping the work. The contract should require formal written notice of an event that triggers such a clause so there are no disputes as to when you were informed.

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