

Recommendation 3: Align and clarify FAR commercial termination language.

Problem

FAR 52.212-4, Contract Terms and Conditions – Commercial Items, contains a set of standard terms and conditions for the procurement of commercial items. These terms are intended to satisfy the requirement of FASA section 8002 that contracting officers use terms that “are determined to be consistent with standard commercial practice.”¹ Included in 52.212-4 are terms and conditions regarding the government’s ability to terminate commercial contracts under various circumstances.

The termination language has been unchanged for the past 24 years. One commenter brought to the Section 809 Panel’s attention several areas where the termination-related language of Part 12 and 52.212-4 has been the subject of litigation, and recommended the language be addressed. Additionally, the policy guidance for terminations in FAR Part 49 does not properly align with the policy guidance for the termination of commercial contracts in FAR Part 12.

Background

FASA required that the FAR contain a list of contract clauses for commercial item contracts that are, to the maximum extent possible, “consistent with standard commercial practices.”² FAR 52.212-4, Contract Terms and Conditions – Commercial Items, was established for that purpose. The language of FAR 52.212-4 is not as comprehensive and prescriptive as typical FAR clauses because it is intended to be more commercial-like. These simpler, more commercial-like terms also benefit contractors that may be unfamiliar with all the details and nuances of government contracting and associated business processes. These terms are intended to provide a framework that better reflects commercial practices without each contracting officer having to develop unique terms and conditions for each procurement.

It is impossible to establish a single set of terms and conditions that would be appropriate for every commercial product or service the federal government might procure. FAR 12.302, Tailoring of Provisions and Clauses for the Acquisition of Commercial Items, addresses this problem by stating that FAR 52.212-4 represent clauses “intended to address, to the maximum extent possible, commercial practices for a wide range of potential Government acquisitions of commercial items.”³ Recognizing that no one set of terms and conditions could be appropriate across all commercial item procurements, FAR 12.302 gives contracting officers the flexibility to tailor the majority of the terms and conditions in 52.212-4. This authority allows contracting officers to tailor the procurement to the actual product or service being procured, including the standard commercial practices for procuring that item in the commercial marketplace. Of the 21 terms and conditions in 52.212-4 (paragraphs (a) thru (u)), all but seven terms may be tailored. Among the terms the contracting officer is given the flexibility to tailor are paragraphs 52.212-4(l), Termination for the Government’s Convenience, and 52.212-4(m), Termination for Cause.

¹ FASA, section 8002.

² Ibid.

³ Tailoring of Provisions and Clauses for the Acquisition of Commercial Items, FAR 12.302.

Findings

Applicability of Part 49, Terminations, to Contracts for Commercial Products and Services

The FAR recognizes that government contracts for commercial products and services need a vehicle for terminations; however, it also recognizes that those clauses need to reflect, to the maximum extent possible, standard commercial practice for commercial products and services that were procured in the commercial marketplace on the basis of price and without the government-unique cost data or contractor cost accounting systems. For this reason, the standard FAR Part 49 termination clauses were not used. Much of the administrative process of termination may apply to the extent it does not conflict with the more commercial approach in FAR 52.212-4.

In reviewing the professional literature regarding the relationship between the standard FAR Part 49 clauses and processes and those in FAR 12.403 and FAR 52.212-4 intended for procurements of commercial items, it appears there has been some confusion between that language of FAR 12.403, Terminations, and the language in FAR 49.002, Applicability.⁴ Specifically, the language in 12.403 states that FAR Part 49 does not apply, but 49.002 states it is to be used as guidance.

Termination for the Government's Convenience

52.212-4(l) reserves for the government the right to terminate a contract for a commercial item at its sole convenience. This is not necessarily a standard commercial practice; however, it does represent a long-standing practice in government procurement. It gives the government the unique, but necessary, flexibility to respond to changes in its mission or to a threat without the complex, time-consuming, and costly process of establishing mutual agreement to terminate a contract prior to completion. For this reason, FAR 52.212-4 includes a clause that gives the government the right to terminate at its convenience, but with more commercial-like terms than those in FAR Part 49 and associated standard FAR termination clauses.

In reviewing the professional literature related to the termination for the government's convenience clause at FAR 52.212-4(l), it appears confusion exists and some litigation has taken place regarding compensation for a terminations for convenience.⁵ Central to the standard FAR policies for convenience terminations is the concept of the contractor being *compensated fairly* for the termination prior to final delivery under the contract. The existing clause is somewhat unclear about the elements of a *fair compensation*.⁶

Termination for Cause

More typical in both commercial and government contracts is a clause providing the buyer with the right to terminate the contract for cause, including late delivery and failure to provide adequate

⁴ Nash & Cibinic Report, 29 N&CR ¶ 21. The Nash & Cibinic Report is a long-standing legal periodical that addresses federal government contract case law and practice

⁵ Ibid.

⁶ Fair Compensation is a term discussed in FAR 49.201, but not defined. The FAR states "Fair compensation is a matter of judgment and cannot be measured exactly." The issue here was that terminations under commercial terms were not required to follow Part 49, so it left open the question of whether "fair compensation" was necessary as discussed in part 49.

assurances of future performance. FAR 52.212-4(m) provides the government with the authority to terminate for cause.

FAR 12.403 (c) states “the contracting officer shall send a cure notice prior to terminating a contract for a reason other than late delivery.”⁷ The professional literature points out that the clause at 52.212-4(m) does not contain a similar requirement.⁸ This disconnect needs to be corrected.

Conclusions

FAR 12.403 is the policy regarding terminations of commercial items, but the policies in Part 49 are intended to be used as guidance in such terminations. The lack of alignment between FAR Parts 12 and 49 should be reconciled by the elimination of the *guidance* language in Subpart 12.403.

FAR 52.212-4(l) and (m) are intended to represent standard or customary commercial practice, but both may be tailored or replaced by the contracting officer to better reflect the commercial practice for the product or service being procured. Because these two clauses are frequently used as is, it is important they reflect best practices, given their scope and intent. As a result, the language of FAR 52.212-4(l) and (m) requires further clarification to elucidate the *fair compensation* principle in paragraph (l) and the use of a *cure* notice for a termination for cause in paragraph (m).

Implementation

Legislative Branch

- No statutory changes are required.

Executive Branch

The Section 809 Panel recommends the FAR Council do the following:

- Revise FAR Subpart 12.403, Terminations, paragraph (a) to remove the reference to Part 49 as guidance.
- Revise FAR 52.212-4(l), Terminations for the Government’s Convenience, to clarify the elements of *fair compensation* when a contract for commercial product or service is terminated for the government’s convenience.
- Revise FAR 52.212-4(m), Termination for Cause, to include language regarding cure notices and to align this clause with the language at 12.403(c)(1).

Implications for Other Agencies

- The recommended changes will benefit all federal agencies that use the FAR.

⁷ Termination, FAR 49.607. Delinquency Notices, FAR 12.403.

⁸ *Packer v. Social Security Administration*, CBCA 5038, 16-1 BCA ¶136,260.

Termination Clauses

FAR Subpart 12.403

(a) *General.* The clause at [52.212-4](#) permits the Government to terminate a contract for commercial items either for the convenience of the Government or for cause. However, the paragraphs in [52.212-4](#) entitled “Termination for the Government’s Convenience” and “Termination for Cause” contain concepts which differ from those contained in the termination clauses prescribed in Part 49. Consequently, contracting officers shall follow the requirements and procedures in this section and the termination paragraphs in [52.212-4](#).

(b) *Policy.* The contracting officer should exercise the Government’s right to terminate a contract for commercial items either for convenience or for cause only when such a termination would be in the best interests of the Government. The contracting officer should consult with counsel prior to terminating for cause.

(c) *Termination for cause.*

(1) The paragraph in [52.212-4](#) entitled “Excusable Delay” requires contractors notify the contracting officer as soon as possible after commencement of any excusable delay. In most situations, this requirement should eliminate the need for a show cause notice prior to terminating a contract. The contracting officer shall send a cure notice prior to terminating a contract for a reason other than late delivery.

(2) The Government’s rights after a termination for cause shall include all the remedies available to any buyer in the marketplace. The Government’s preferred remedy will be to acquire similar items from another contractor and to charge the defaulted contractor with any excess procurement costs together with any incidental or consequential damages incurred because of the termination.

(3) When a termination for cause is appropriate, the contracting officer shall send the contractor a written notification regarding the termination. At a minimum, this notification shall --

(i) Indicate the contract is terminated for cause;

(ii) Specify the reasons for the termination;

(iii) Indicate which remedies the Government intends to seek or provide a date by which the Government will inform the contractor of the remedy; and

(iv) State that the notice constitutes a final decision of the contracting officer and that the contractor has the right to appeal under the Disputes clause (see [33.211](#)).

(4) The contracting officer, in accordance with agency procedures, shall ensure that information related to termination for cause notices and any amendments are reported. In the event the termination for cause is subsequently converted to a termination for convenience, or is otherwise withdrawn, the

contracting officer shall ensure that a notice of the conversion or withdrawal is reported. All reporting shall be in accordance with [42.1503\(h\)](#).

(d) *Termination for the Government's convenience.*

(1) When the contracting officer terminates a contract for commercial items for the Government's convenience, the contractor shall be paid --

(i) (A) The percentage of the contract price reflecting the percentage of the work performed prior to the notice of the termination for fixed-price or fixed-price with economic price adjustment contracts, or

(B) An amount for direct labor hours (as defined in the Schedule of the contract) determined by multiplying the number of direct labor hours expended before the effective date of termination by the hourly rates(s) in the Schedule; and

(ii) Any charges the contractor can demonstrate directly resulted from the termination. The contractor may demonstrate such charges using its standard record keeping system and is not required to comply with the cost accounting standards or the contract cost principles in Part 31. The Government does not have any right to audit the contractor's records solely because of the termination for convenience.

(2) Generally, the parties should mutually agree upon the requirements of the termination proposal. The parties must balance the Government's need to obtain sufficient documentation to support payment to the contractor against the goal of having a simple and expeditious settlement.

FAR 52.212-4(l) and (m)

(l) *Termination for the Government's convenience.* The Government reserves the right to terminate this contract, or any part hereof, for its sole convenience. In the event of such termination, the Contractor shall immediately stop all work hereunder and shall immediately cause any and all of its suppliers and subcontractors to cease work. Subject to the terms of this contract, the Contractor shall be paid a percentage of the contract price reflecting the percentage of the work performed prior to the notice of termination, plus reasonable charges the Contractor can demonstrate to the satisfaction of the Government using its standard record keeping system, have resulted from the termination to fairly compensate the contractor. Reasonable charges include costs and reasonable profit on such costs incurred in anticipation of performing the entire contract, not adequately reflected as a percentage of the work performed. The Contractor shall not be required to comply with the cost accounting standards or contract cost principles for this purpose. This paragraph does not give the Government any right to audit the Contractor's records. The Contractor shall not be paid for any work performed or costs incurred which reasonably could have been avoided.

(m) *Termination for cause.* The Government may terminate this contract, or any part hereof, for cause in the event of any default by the Contractor, or if the Contractor fails to comply with any contract terms and conditions, or fails to provide the Government, upon request, with adequate assurances of future performance. The Government's right to terminate this contract for a reason other than late delivery may be exercised if the contractor does not cure such failure within 10 days (or more if authorized in writing by the Contracting Officer) after receipt of the notice from the Contracting Officer specifying the failure. In the event of termination for cause, the Government shall not be liable to the Contractor for any amount for supplies or services not accepted, and the Contractor shall be liable to the Government for any and all rights and remedies provided by law. If it is determined that the Government improperly terminated this contract for default, such termination shall be deemed a termination for convenience.