



Terminating a Construction Contract

BY JP VOGEL AND JULIA EDWARDS

What happens when an owner fails to pay or a contractor continually fails to properly perform its work? Termination provisions exist to prevent uncertainty when unexpected and undesired events occur and should be carefully drafted in every construction contract.

Generally, there are two types of termination provisions in a construction contract: 1) termination for cause and 2) termination for convenience.

TERMINATION FOR CAUSE

A termination for cause provision provides rights and remedies in the face of a breach by the other party. Owners, general contractors and subcontractors should consider their risks under a construction contract and allocate those risks through a termination provision. A well-written termination for cause provision will protect contracting parties by providing a clear mechanism to terminate, as well as, the resulting remedies. Each party to a construction contract will have different goals for a termination for cause provision. For example, a general contractor may want to consider a provision allowing it to terminate if:

- The work has stopped for a period of days due to no fault of the contractor;
- The Owner has not issued a Certificate of Payment or the Owner has not made payment in a timely manner; or
- The Owner files bankruptcy

If one of these events are triggered, a termination provision needs to provide the contractor's post termination remedies, such as recovering payment for the work executed, reasonable overhead and profit, and costs incurred as a result of termination.

An owner may want to consider a provision if the general contractor, for example:

- Fails to pay its subcontractors; Repeatedly fails to supply enough workers or materials; or
- Delays completion of a project.

Examples of Owner's post termination remedies might include getting an assignment of the general contractor's subcontracts, limiting payment to the general contractor for work actually performed, or excluding the general contractor from the site.

While termination for cause provisions provide clarity, they can also limit a party's ability to terminate the contract. To avoid this, a catch-all provision that allows termination for a party's "material breach of any provision of the contract" is suggested. The party on the other side of a termination for cause provision should attempt to add a notice period and opportunity to cure to the provision to prevent an automatic termination in the event it defaults.

DETERMINING FOR CAUSE

In case of disagreement between parties, a termination



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for cause provision should include a "conversion clause", which authorizes a third party, such as an architect, mediator, arbitrator or judge to determine whether the termination for cause was appropriate and convert it to "for convenience," if not.

TERMINATION FOR CONVENIENCE

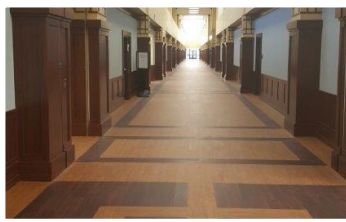
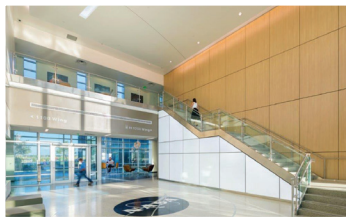
A termination for convenience clause typically allows one party to terminate the contract with or without cause and bars a subsequent claim against the terminating party for wrongful termination. These clauses can be mutual, or one-sided. Depending on the party doing the drafting, these clauses typically provide more remedies for the party who is being terminated without cause. For example, a contractor may want to put in the termination for convenience provision that they are entitled to lost profits on the entire project and direct cancellation costs if terminated for convenience. When these termination clauses exist, it is vital that a general contractor, or

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sub-contractor, include similar such provisions in their downstream contracts.

THE IMPACT OF TERMINATION

While a contract termination clearly affects the parties to the contract, it will also impact down-stream subcontractors. Beware of lien and bond deadlines that may arise after the termination.

In summary, consult with a construction attorney to get the most favorable termination provision in your contracts. ♦

ABOUT THE AUTHORS



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An active member of ABC Houston, Julia Edwards joined Gray Reed's litigation section in 2018 after participating in the firm's summer associate program. She is often called upon by the firm's litigators who are going to trial to offer her expertise on voir dire and jury selection. While attending The University of Texas School of Law, Julia received the Dean's Achievement Award for

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Clients throughout Texas, the U.S. and abroad rely on JP to guide them through every phase of sophisticated, time-sensitive commercial construction projects and resolve disputes when they don't go as planned. JP focuses on brainstorming new ways for clients to seize opportunities and overcome challenges - whether he's helping an international company

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