

# Gov't Contracts Rulings Hold Termination Challenge Tips

By **Kara Daniels and Amanda Sherwood** (February 21, 2023)

Any default termination can be devastating for a contractor, especially an unwarranted one.

Challenging a default termination can seem like a daunting, David versus Goliath endeavor, but recent cases out of both the U.S. Court of Federal Claims and the U.S. Civilian Board of Contract Appeals highlight several ways such challenges can be successful.

We discuss two such cases and the lessons contractors facing performance difficulties can learn from them.

## Schneider Electric

First, in *Schneider Electric Buildings Americas Inc. v. U.S.*,<sup>[1]</sup> the COFC **considered** the propriety of the government's "drastic decision of terminating Schneider for default after receiving 91.45% of the value of the contract" for implementation of certain energy conservation measures at a government facility.

The contract followed the structure of the National Energy Conservation Policy Act, whereby contractors incur the upfront costs of acquiring and installing energy savings measures, and in exchange receive a share of any resulting energy savings.<sup>[2]</sup>

The contract in question anticipated 23 years of performance, over which time the contractor would earn over \$24 million in annual installments. One category of energy conservation measures the contractor installed were boilers; the government claimed the boilers never worked properly and, after several alleged boiler failures, refused to pay the contractor's invoice for its fifth year, later only remitting a partial payment.

The contractor claimed the government failed to adequately service the boilers — the contract tasked the government with routine maintenance — and noted that it nevertheless submitted a repair plan in response to the agency's request, but the government revoked its access to the facility.

For the sixth year, the government again belatedly — eight months late — paid only a portion of the invoice. Thereafter, the government sent a cure notice and show cause letter, which the contractor did not immediately respond to because the only recipient of the notice was out on maternity leave.

The government then noticed its intent to terminate the contract for default. The contractor again attempted to explain its nonresponse to the cure notice and show cause letter and to address the government's concerns, but the government finalized the termination on the basis that the boilers were hindering the U.S. Department of Agriculture's research efforts.

The COFC found the default termination improper; the government premised its termination decision on what it expected from the contractor, not what the contract actually required of the contractor. Nowhere did the contract state that interference with the USDA's research



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was a critical failure in performance and cause for termination.

The COFC said that instead, the contract was clear that its goals were energy reduction, and "[t]he United States has not argued, let alone establish[ed], that Schneider did not deliver the energy reduction guarantees or failed in the delivery of upgraded equipment."

While the government urged the COFC to look beyond the contract's language to its intent, the court opined that tribunals "are ill-suited to divine other, unexpressed intentions of contracting parties" and cited U.S. Court of Appeals for the Federal Circuit precedent requiring terminations be both contract-related and maintain a close nexus to a clear violation of contract terms.[3]

According to the COFC, because "[t]he United States has not shown that the Contract expressly allowed the United States to use any secondary impact on the USDA's research as a quality control measure for Schneider's performance, even when Schneider has met its energy-savings goals," the government thus lacked a valid justification for the default termination.

The court furthermore found a prior government breach based on the agency unilaterally withholding significant portions of the contractor's annual payments, reasoning that this breach provides a separate ground for converting the default termination to a termination for convenience.[4]

The court eloquently concluded:

Contract law keeps an attentive eye on the exercise of default termination power, having recognized that the power causes "a drastic adjustment of the contractual relationship." [5] And so, the Court strongly adheres to the principle, also reflected in FAR, that the termination decision must be governed by the provisions of the contract. The United States' approach in unilaterally withholding payments bypassed the Measurement and Verification procedure of the Contract. The United States' default termination analysis also contorted the Contract's stated goals and performance metrics. Feeling aggrieved by aspects of Schneider's performance — rightly or wrongly — the United States' freewheeling stroll down the road to default termination involved turning away from the paths specifically laid out by the Contract's terms. The party that hastily diverts from the path provided by the contract's terms is bound to meet its destiny on the road it took to avoid it.

Under the Federal Acquisition Regulation, the court determined the proper remedy was the conversion of the default termination to a termination for convenience.

### **Alan E. Fricke Memorials**

Second, in *Alan E. Fricke Memorials Inc. v. U.S. Department of Veterans Affairs*, [6] the CBCA granted a contractor relief from a default termination because the contractor was not in breach at the time the contract was terminated and because the VA failed to issue a proper cure notice.

The contract was for inscription of gravestones, and the contractor experienced a series of performance problems resulting in backlogs of overdue inscribed markers.

The VA engaged with the contractor and learned the reasons for its delays, even determining that some of the causes were industrywide, but repeatedly expressed

frustration with the performance failures and even diverted orders to other contractors. Despite these issues, however, the VA exercised an option under the contract, requesting another year of performance from the contractor.

About a month after the option exercise, in October 2021, the contracting officer issued a cure notice, listing complaints with the contractor's performance, although at the time, the contractor was only delinquent on two markers, which were delivered shortly thereafter in November 2021.

The VA issued a second cure notice complaining of nine undelivered markers, which were likewise delivered in November 2021. Then, in December 2021, the VA terminated the contractor for default citing the contractor's failure to provide inscription services within ten days as required by the contract, its failure to provide timely inscription services for certain types of markers, and its failure to respond to the cure notice.

The CBCA found that none of these three reasons were an adequate basis for contract termination. While the contractor had been delinquent — to the tune of hundreds of untimely delivered markers — earlier in the contract, at the time of the termination, the contractor was not late on any orders.

Regarding the second supposed basis, the contractor had no outstanding orders for the particular type of marker at the time of the termination. The CBCA also observed that by exercising the option after the contractor's record of delinquencies, the contracting officer had seemingly found the contractor's performance acceptable.

The CBCA stated:

The contracting officer cannot exercise the option on the contracts, seemingly accepting these performance difficulties, and then decide to terminate the contract three months later, finding that these performance difficulties are no longer acceptable.

Finally, the CBCA found that the cure notices did not adequately put the contractor on notice that the VA sought any response other than timely delivery of outstanding orders, i.e.,

While the cure notice expressed frustration that VA experienced during Fricke's performance, VA did not explicitly request a plan to handle all of the line items on the contract, as the contracting officer testified she expected.

The CBCA concluded:

It appears that the contracting officer terminated the contract because she had no confidence in Fricke's ability to meet the requirements of the contract. But this lack of confidence does not provide a basis for termination, absent a proper request for future assurances.

## **Lessons Learned**

These cases give contractors important tips for how to handle performance issues and how to respond should the government initiate the default termination process.

- The relationship with one's customer is key; avoid surprises by communicating performance difficulties and suggested solutions, or the contractual obligations, if they differ from the customer expectations, and attempt mutual resolution.
  
- Document any circumstances that could constitute the government's prior material breach.
  
- Consider whether the government unilaterally withheld payment before exercising the termination, and if so, if there was a contractual basis for that withholding.
  
- Consider whether the government could be said to have waived certain performance standards or accepted the contractor's performance.
  
- Respond promptly to any cure notices and, if possible, establish processes to ensure redundancy should a sole recipient be unavailable.
  - Consider whether the cure notice adequately informs the contractor of the problem and how the termination could be avoided.
  
  - In a prompt written response, describe how the contractor has met the contractual obligation or has been unable to perform based on any government prior breach or other excusable delay, or the path for curing any performance issue.
  
- Read the termination notice and determine if it states a reasonable basis for termination that clearly ties to the contract.
  - Evaluate whether the contractor was actually in default of an express contractual provision at the time of the termination.

- Remember that a termination for default is a government claim that must be appealed to the appropriate Board of Contract Appeals within 90 days, or to the COFC within one year.

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[1] [Schneider Electric Buildings Americas Inc. v. United States](https://ecf.cofc.uscourts.gov/cgi-bin/show_public_doc?2021cv0788-86-0), [https://ecf.cofc.uscourts.gov/cgi-bin/show\\_public\\_doc?2021cv0788-86-0](https://ecf.cofc.uscourts.gov/cgi-bin/show_public_doc?2021cv0788-86-0).

[2] See 42 U.S.C. § 8287(a)(1).

[3] Keeter Trading Co. v. United States, 79 Fed. Cl. 243, 253 (2007) (itself citing McDonnell Douglas Corp. v. United States, 182 F.3d 1319, 1328 (Fed. Cir. 1999)).

[4] The court also concluded that the contract placed the duty of routine maintenance on the government (the contractor was only responsible for "quarterly" or "annual" boiler maintenance tasks) and the government breached that obligation, but made no finding regarding the materiality of that breach. The court found the contractor failed to adequately demonstrate that the government's denial of access to its facilities constituted a breach for purposes of summary judgment.

[5] Clay Bernard Sys. Int'l Ltd. v. United States, 22 Cl. Ct. 804, 810 (1991).

[6] Alan E. Fricke Memorials v. Department of Veterans Affairs, [https://cbca.gov/files/decisions/2023/SULLIVAN\\_01-12-23\\_7352\\_\\_ALAN\\_E\\_FRICKE\\_MEMORIALS\\_INC%20\(DECISION\).pdf](https://cbca.gov/files/decisions/2023/SULLIVAN_01-12-23_7352__ALAN_E_FRICKE_MEMORIALS_INC%20(DECISION).pdf).