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Tools of the Trade: Reacting to Government Contract Terminations and Pauses

CURRENT CLIMATE

On February 26, 2025, Executive Order 14222, Implementing the President's "Department of Government Efficiency" Cost Efficiency Initiative, was released. This Executive Order ("EO 14222") states that its purpose is to "commence[] a transformation in Federal spending on contracts, grants, and loans to ensure Government spending is transparent and Government employees are accountable to the American public."

EO 14222 requires agency heads to establish a system to record payments, include payment justifications, and provide the Agency Head the ability to pause and review any payment that does not include the required justification. EO 14222 requires Agency Heads to post such payment justifications publicly, to the maximum extent allowed by law and deemed practicable by the Agency Head. Importantly, each Agency Head will (1) review existing covered contracts and grants and (2) where appropriate and consistent with applicable law, terminate or modify those agreements to reduce or reallocate federal spending to promote efficiency and advance the policies of the Administration.[i]

The Department of Government Efficiency ("DOGE"), working with federal department and agency leaders, is taking actions seeking to save billions of taxpayer dollars through a combination of actions including contract, lease, and grant terminations.[ii] DOGE's terminations number around 2,300 according to DOGE's "Wall of Receipts." Accordingly, government contractors and award recipients are experiencing unexpected and unprecedented cancellations or pauses in their contracts with the federal government. We've outlined some information and options that federal contractors may consider below.

TERMINATIONS, CANCELLATIONS, OR PAUSES OF FEDERAL SPENDING

Federal government agencies and instrumentalities issue a variety of agreements that contain funding, including (i) contracts subject to the Federal Acquisition Regulation ("FAR") and the applicable agency supplements; (ii) grants and cooperative agreements; (iii) contracts that do not obligate appropriated funds (known as Non-Appropriated Funding Instruments, or "NAFI," contracts); and (iv) Other Transaction Authority agreements. The focus of this article is on FAR contracts.

FAR contracts can be terminated or performance paused in various ways, including when the federal agency:

- Issues a temporary stop-work order;
- Stops funding a contract;
- Decides not to exercise an option;
- Terminates for the government's convenience; and
- Terminates for default (a breach of the contractual or related statutory or regulatory obligations).

1. Stop Work Order

A stop work order is a written order under FAR 52.242-15 that directs the contractor to stop all or part of your work under your federal government contract for a period of up to 90 days. Contractors should review the order closely to determine what specific portions of the contract (and underlying work) are paused. Contractors should clarify with their contracting officer ("CO") if the scope of the stop work order is unclear and promptly inform all subcontractors affected by the order. Contractors should take steps to minimize the incurrence of costs allocable to the work covered by the order and instruct subcontractors to do the same.

Within the 90-day period, the government may take any of the following actions: (1) request an extension of the period; (2) cancel the stop-work order; or (3) terminate the work remaining under the contract prior to, or on, the 90th day. Importantly, if a stop-work order is cancelled or expires (and there is no extension of the period subject to the pause executed), then the contractor is expected to resume work promptly. Pursuant to the applicable FAR Changes clause,[iii] if the contractor incurs additional expenses or costs, the contractor may submit a request for an equitable adjustment ("REA") within 30 days after the expiration of the stop-work order. The REA can request adjustments in delivery schedule, contract price or cost, or both. The CO may execute a contract modification to cover associated changes related to the stop work order.

All FAR contracts are subject to the government's right to terminate for convenience at any time, including contracts subject to stop work orders. If you receive a notice of a termination for convenience, contractors must work with the CO on a termination settlement agreement, which is a settlement that compensates the contractor for additional reasonable costs or expenses arising from the stop-work order and/or subsequent termination.[iv] Contractors should refer to the terms of its contract and keep detailed documentation on the costs directly attributable to the stopped project and termination. This means that contractors will have to keep records on costs and expenses associated with the pause in work and ensure those costs are reasonable.

2. Lapse in Funds

Certain FAR contracts are incrementally funded, and in such cases, the government may decide not to obligate additional funding to a FAR contract. When a contract has a limitation of funds clause, the contractor is permitted to perform work or provide products up to the specified funding limit. If a contractor has reached the specified funding limit and the government does not obligate additional funding, the contractor is no longer obligated to continue

performance. *See*, *e.g.* Federal Acquisition Regulation ("FAR") 52.232-22(f). Contractors may choose to continue working "at risk," but should not expect that funds will be added at a later date. If the federal government fails to provide funding and subsequently issues a termination for convenience, contractors are advised to negotiate a termination settlement (which may also require pursuit of either an REA or a claim (as outlined further below)). If the necessary funding is eventually added to the contract, contractors may wish to seek an equitable adjustment for time extensions or additional costs associated with the delay.

3. Failure to Exercise an Option

Failure to exercise an option period operates like a termination because the government is affirmatively choosing not to continue its contractual relationship with the contractor. The government has a unilateral right to exercise an option (or not). *See Sword & Shield Enter. Sec. v. GSA*, CBCA 2118, 2012-1 BCA ¶ 34,922 (internal citation omitted) (stating that "[w]hen a contract contains an option to extend its term, unless the contract provides otherwise, the Government enjoys broad discretion and is under no obligation to exercise it."). In other words, the government is not required to exercise an option just because the option is included in your contract, and the inclusion of an option period does not obligate the government to fund the option period. *See id.*

Absent express terms in your contract that would limit the government's discretion in exercising an option, contractors will have difficulty challenging the government's decision not to exercise an option. However, contractors do have options; you can challenge the government's decision by arguing that the government (1) breached the implied covenant of good faith and fair dealing, and/or (2) acted in bad faith or so arbitrary or capricious that the government abused its discretion. *See, e.g., Rivera Agredano v. United States*, 70 Fed. Cl. 564, 573 (Fed. Cl. 2006); *Brightwood Mgmt Partners v. Dep't of Veterans Affairs*, CBCA 7351, 2023-1 BCA ¶ 38,294; *Blackstone Consulting Inc. v. Gen. Serv. Admin.*, CBCA 718, 2009-1 BCA ¶ 34,103, at 168,636. To be clear, allegations that the government breached its duty of good faith is different from an argument that the government acted in bad faith. *See Sigma Servs., Inc. v. Dep't of Housing and Urban Dev.*, CBCA 2704, 2012-2 BCA ¶ 35,173, at 172,591 (stating that the covenant of good faith and fair dealing is inherent in every contract but does not require "a showing of bad faith"); *see also Brightwood Mgmt Partners v. Dep't of Veterans Affairs*, CBCA 7351, 2023-1 BCA ¶ 38,294 ("A claim based on a breach of the covenant of good faith and fair dealing is different from an allegation of bad faith.") (internal citation omitted).

Implied in every contract with the government, is the covenant of good faith and fair dealing. *Centex Corp. v. United States*, 395 F.3d 1283, 1304 (Fed. Cir. 2005). This is an "implied duty" that each party owes to the other including the "duty to not interfere with the other party's performance and not to act so as to destroy the reasonable expectations of the other party regarding the fruits of the contract." *Id.* at 1304 (internal citations omitted). The implied covenant of good faith and fair dealing, however, cannot be used to expand the party's contractual duties beyond what is expressed in the contract. *Id.* at 1306. Government officials are presumed to act in good faith. *See Sigma Servs., Inc. v. Dep't of Housing and Urban Dev.*, CBCA 2704, 2012-2 BCA ¶ 35,173 (stating that the "covenant of good faith and fair dealing is inherent in every contract" and that government officials are presumed to "exercise their duties in good faith"). Contractors can argue that the federal government breached its duty of good faith by demonstrating, amongst other things, "lack of diligence, negligence, or a failure to cooperate." *Id.* (citing *Malone v. United States*, 849 F.2d 1441, 1445 (Fed. Cir. 1988)).

Contractors may also challenge a federal agency's decision not to exercise an option by demonstrating that the government's decision was a product of bad faith or was so arbitrary and capricious that it is an abuse of discretion. *Blackstone Consulting Inc. v. General Serv. Admin.*, CBCA 718, 2009-1 BCA ¶ 34,103, at 168,636 (internal citations omitted). The burden of proof for arguments of bad faith are high; contractors have the burden to demonstrate by

clear and convincing evidence that the government official was "motivated by bad faith in the conduct of his duties." *See id*. (stating that the clear and convincing evidence standard would be evidence which "produced in the mind of the trier of fact an abiding conviction that the truth of a factual contention is *highly probable*." (emphasis in original)). In other words, contractors may face challenges in demonstrating "almost irrefragable" proof that the government's decision, not to exercise the option, was done with the intent to injure the contractor. *See Brightwood Management Partners v. Department of Veterans Affairs*, CBCA 7351, 2023-1 BCA ¶ 38,294 (citing *Sword & Shield Enterprise Security, Inc. v. General Services Administration*, CBCA 2118, 2012-1 BCA ¶ 34,922, at 171,725).

4. Termination for Convenience

In the government contracts space, there are two types of terminations: (1) termination for default and (2) termination for convenience.[v] A termination for default, covered under FAR Subpart 49.4, is when the government exercises its right to terminate, in whole or part, a contract based on the contractor's actual or anticipated failure to perform contractual obligations.[vi] A termination for convenience is when the government terminates a federal contract because it is in the government's interest, rather than due to a breach or default. The government's right to terminate for convenience arose out of the government's need to avoid large procurements when war or other hostilities dissipated. *See TigerSwan, Inc. v. United States*, 118 Fed. Cl. 447, 344 (2014) (stating that terminations for convenience arose when the government needed a mechanism to "avoid large, unneeded military procurements upon cessation of war and other hostilities." (internal citation omitted)). Terminations for convenience are now widely used by the federal government for military and civilian contracts. *See id*.

a. Settlement Proposal

When contractors first receive a notice for termination for convenience, *see* FAR 49.601, contractors should *promptly* submit a settlement proposal to the terminating contracting officer (referred to as a "TCO"). FAR 49.206-1(a).[vii] Final settlement proposals must be submitted within one year of the termination (unless the TCO extends the submission date). [viii] The settlement proposal will include all cost elements related to the termination, including subcontractor settlements and proposed profit. FAR 49.206-1(b). Contractors will need to consider the basis for their settlement.

For example, fixed-price contracts will use the inventory or total cost basis. *Compare* FAR 49.206-2, *with* FAR 49.206-3. [ix] The inventory basis, the preferred option, will include an itemized list of allocable costs related to the termination:

- Metals, raw materials, purchased parts, work in process, finished parts, components, dies, jigs, fixtures, and tooling, at purchase or manufacturing cost;
- Charges such as engineering costs, initial costs, and general administrative costs;
- Costs of settlements with subcontractors;
- Settlement expenses; and
- Other proper charges.

FAR 49.206-2(a). The total cost basis for a total termination of work, when the inventory basis for fixed price contracts is not practicable, must include itemized costs incurred under the contract up until the termination. FAR 49.206-2 (b)(2). The total cost basis for a partial termination must not be submitted until the contractor completes the portion of the contract that is still active. FAR 49.206-2(b)(3). The contractor must calculate all costs incurred to the date of completion of the continued portion of the contract. *See id.*

Under either basis for settlement under a fixed-price contract (inventory or total cost), there will be an allowance for profit and adjustments for loss. Contractors should include profit on "preparations made and work done by the contractor for the terminated portion of the contract;" this does not include settlement expenses. FAR 49.202(a). Similarly, anticipatory profits and consequential damages are not allowed. *See id.* When contractors negotiate profit with the TCO, certain factors will be considered such as the extent of the work and the difficulty of the work in comparison to the total work contemplated in the terminated contract. FAR 49.202(b). The TCO will also consider, amongst other factors, the contractor's efficiency in reducing costs and attaining quantity and quality production. *See id*. The TCO will not allow contractors to recover an amount in profit that, assuming the contract was completed in its entirety, would not have come to fruition. FAR 49.203(a). TCOs must make adjustments in profit based on expected product efficiencies and other factors. *See id.* Finally, TCOs must deduct the following from a settlement: the price of purchased or retained inventory in which the proceeds from materials sold have not been credited to the government; the fair value of lost or damaged property (such that the inventory is undeliverable); and any other amounts deemed appropriate.

In sum, contractors will receive notice of a termination, whether in part or whole. Contractors will provide a basis for its settlement proposal in accordance with its contract (which may be dictated by the contract type). Contractors will include allocable and allowable costs and related documentation to support its proposal. Contractors will use the appropriate settlement proposal form found under FAR 49.602.[x] If contractors are not satisfied with the settlement proposal outcome, contractors may challenge the termination and/or bring a claim against the government related to the settlement proposal.

b. Challenging the Termination

Contractors may challenge the termination for convenience at the appropriate board of contract appeals or the U.S. Court of Federal Claims ("COFC"). If appropriate, contractors can argue that the government acted in bad faith when it terminated the contract, or the CO abused its discretion in terminating the contract. *See TigerSwan, Inc. v. United States*, 118 Fed. Cl. 447, 345 (2014) (arguing that the DoD executed an improper termination for convenience when it issued a notice to the contractor to proceed with the work but then rescinded that notice and awarded a series of sole source contracts to a competitor). The burden of proof is on the contractor to demonstrate that the government acted in bad faith. *See id.* The contractor will have to provide clear and convincing evidence that the termination was made with the "intent to injure" the contractor. *See id.* (citing *Am-Pro Protective Agency, Inc. v. United States*, 281 F.3d 1234, 1239-40 (Fed. Cir. 2002)). In determining whether the CO abused its discretion, the court will consider the CO's bad faith (if any), reasonableness of the decision, amount of discretion delegated, and any violations of statute or regulation. *See id*. (citing *Keco Indus., Inc. v. United States*, 492 F.2d 1200, 1203-04, 203 Ct. Cl. 566 (Ct. Cl. 1974)).

Contractors may receive a notice for termination and be tempted to pursue monetary or other claims contemplated under FAR 52.233-1, by challenging the termination for convenience itself. If the contractor is pursuing a claim, it will have to file a claim with the CO first, as detailed below. The notice for termination for convenience may instruct the contractor of its right to file an appeal and may even state that the termination is the CO's "final decision." Regardless, the notice of termination "is not in and of itself an appealable contracting officer decision" within the Contract Disputes Act ("CDA"). *Blankson v. Agency for Int'l Dev.,* CBCA 8256, 25-1 BCA ¶38,726 (internal citations omitted) (stating that the appellant's arguments surrounding the termination for convenience are premature unless a claim is first submitted to the CO); *Ramirez v. Agency for Int'l Dev.*, CBCA 8210, 25-1 BCA ¶38, 728 (holding that similar to *Blankson*, a CO's decision to terminate for convenience is not an appealable contracting officer's final decision).

CLAIMS PROCESS

The CDA, implemented under FAR 52.233-1, provides a government mandated structure for resolving disputes between contractors and the federal government on nearly all contracts with the government. 41 U.S.C. §7102—7103.[xi] The process starts with a contractor submitting a written demand or assertion, defined as a claim,[xii] to the CO for a final decision ("COFD"). 41 U.S.C. §7103(a). The claim must be submitted to the CO within 6 years after the accrual of the claim.[xiii]

Contractors must include key information in the claim, or the CO will likely deny the claim. Contractors must include information such as a "sum certain" (amount of relief sought) and the basis for the claim (written demand seeking money, an adjustment or interpretation of contract terms, or other relief in accordance with the contract). FAR 52.233-1(c). For claims exceeding $100,000, the contractor must include the following certification statement: "I certify that the claim is made in good faith; that the supporting data are accurate and complete to the best of my knowledge and belief; that the amount requested accurately reflects the contract adjustment for which the Contractor believes the Government is liable; and that I am authorized to certify the claim on behalf of the Contractor." FAR 52.233-1(d)(iii). Importantly, the contractor must proceed with performance of the contract pending final resolution of the claim. FAR 52.233-1(i).

For claims over $100,000, the contracting officer must render a decision within 60 days of the request or notify the contractor of the date in which the decision will be made. FAR 52.233-1(e). For claims under $100,000, the contractor officer must render a decision within 60 days of the written request. *Id.* Once the COFD is issued to the contractor, the contractor has 90 days to appeal the denial to the appropriate board of contract appeals[xiv] or COFC. If the Contracting Officer has not issued a COFD within 60 days, or by the deadline communicated to the contractor, the contractor may deem such a failure as a denial and appeal. 41 U.S.C. § 7103(f)(5).[xv]

CONCLUSION

If they haven't already, contractors should be familiarizing themselves with the different ways that the federal government may pause or stop work. Contractors should seek to minimize costs and maintain documentation on costs associated with a pause or termination. Resolution with the contracting officer, whether through negotiated REAs or settlement proposals, would be the best option for the contractor to resolve disputes in a timely manner. If, however, these options are unsuccessful, contractors should be aware that they have options to challenge government actions and pursue appeals in the appropriate forum. K&S has extensive experience in the government contracts field, representing a wide variety of government contractors including those specializing in defense and information technology. K&S can provide essential counseling and litigation experience to assist contractors experiencing contract terminations or pauses in their work with the federal government.

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[i] Executive Order 14222 prioritizes Agency Heads to review funds dispersed under contracts and grants to foreign entities and educational institutions. 90 Fed. Reg. 11095 (published March 3, 2025).

[ii] If a grant recipient has experienced a suspension of grant money, the recipient should review the grant and the specific agency regulations applicable to the grant (the regulations vary by agency supplement). There is no equivalent to the Contract Disputes Act ("CDA") governing disputes arising under grants or cooperative agreements. Typically, under the Tucker Act, the Court of Federal Claims has jurisdiction over monetary claims against the federal government exceeding $10,000. This includes claims arising out of express or implied contracts with the federal government. Disputes arising out of procurement contracts with the federal government, however, are governed by the CDA.

[iii] *See* Federal Acquisition Regulation ("FAR") 43.205 (various clauses for changes).

[iv] Regulations governing which costs or expenses may be recovered will depend on whether the contract is terminated for convenience or default.

[v] Currently, the contracts that are being terminated are terminated for convenience—not for default.
[vi] Terminations for default are not the subject of this article, but contractors may consider whether the alleged default arose out of causes beyond the control and without the fault or negligence of the contractor. FAR 49.401(b).
[vii] The Contracting Officer and the Terminating Contracting Officer may be the same individual.
[viii] There is a different deadline for contractors to submit an inventory disposal schedule. If the terminated contract includes inventory (materials, parts, or assets left over from a terminated contract), the contractor is required to submit a complete termination inventory schedule no later than 120 days from the termination unless directed otherwise by the Contracting Officer. FAR 49.206-3; FAR 52.249-6(d). Appropriate forms are under FAR 49.602-2.
[ix] Terminations under cost reimbursement type contracts are under FAR 52.249-6. Contractors must, amongst other actions, immediately stop work and terminate all subcontracts applicable to the terminated work. FAR 52.249-6(c).
[x] Please note that there is a Settlement Proposal form (called the "Short Form"), Standard Form 1438, for fixed price contracts when the proposal is less than $10,000.
[xi] Note that the CDA, 41 U.S.C. §7101 *et seq.*, provides a structured process by which a government contractor can resolve disputes with the procuring agency. The CDA does not apply to commercial contract disputes (disputes between private parties).
[xii] The term claim is defined under FAR 52.233-1 as a "written demand or written assertion by one of the contracting parties seeking, as a matter of right, the payment of money in a sum certain, the adjustment or interpretation of contract terms, or other relief arising under or relating to this contract," but "a written demand or written assertion by the Contractor seeking the payment of money exceeding $100,000 is not a claim under 41 U.S.C chapter 71 until certified."
Please note that while the formal claims process may start with a written demand to the contracting officer, contractors may have already been discussing, and potentially disagreeing, with a Contracting Officer regarding a request for equitable adjustment which can be converted to a claim.
[xiii] This deadline does not apply to claims by the federal government against a contractor based on a claim by the contractor involving fraud. 41 U.S.C. §7103(a)(4)(B).
[xiv] The appropriate board of contract appeals will be the Civilian or Armed Services Board of Contract Appeals. Contractors should ensure that they are appealing their claim to the correct agency board as the board's jurisdiction to hear a claim is determined by the federal agency which issued the contract.
[xv] A contracting Officer's failure to issue a decision within 60 days or within a proper extension is considered a denial. *See Aetna Gov't Health Plan*, ASBCA 60207, 2016-1 BCA ¶ 36,247 (stating that the contracting officer's failure to pinpoint a decision date was considered a deemed denial allowing an appeal because "[i]t is not enough to state that a final decision will be issued within a specified number of days [from] the occurrence of some future event."); *see also Rudolph & Sletten, Inc. v. United States*, 120 Fed. Cl. 137, (2015) (holding that the contracting officer has a right to extend its initial 60 day decision deadline, but the government does not have the right to further extend that deadline so contractors "may choose to treat any further extension of the deadline as a deemed denial of its claim." (internal citations omitted)).