TERMINATION FOR CONVENIENCE

ESSENTIAL CONTRACT CLAUSES PART 1

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In this guide we will look at the termination for convenience clause.

There are many ways to legally terminate a contract. Termination for convenience can be useful in certain scenarios, but must be exercised with caution.

1 WHAT IS TERMINATION FOR CONVENIENCE?

Termination for convenience ("TFC") refers to the termination of a contract by one party without the need to provide a justifiable reason for the termination. The terminating party may terminate for any reason that it sees fit, or for no reason at all.

Many commercial contracts include a clause giving one or both parties the right to TFC.

TFC may also occur when both (or all) parties to a contract agree to terminate the contract.

2 WHY INCLUDE A TFC CLAUSE IN YOUR CONTRACT?

A TFC clause is intended to provide commercial flexibility to contracting parties.

A TFC clause provides a contracting party with a useful 'out', so their business is not constrained from evolving, moving in a new direction or taking advantage of changing market conditions.

For example, in a contract covering the ongoing provision of services, the purchaser may wish to have the flexibility to change service providers during the term of the contract. Without a TFC clause the purchaser may be locked into the contract.

A service provider may also wish to take advantage of a TFC clause. The right to TFC may provide the service provider the flexibility to stop providing a service or to change the way that it provides a service during the term of the contract.

The clause may also be useful to allow parties to end a contractual relationship when the relationship has deteriorated.

3 SAMPLE CLAUSE

Customer right to TFC

- Pro-Customer

"The Customer may immediately terminate this agreement for any reason or for no reason without liability by giving the Vendor at least 30 days' notice of such termination."

- Pro-Vendor

"The Customer may immediately terminate this agreement for any reason or for no reason by giving the Vendor at least 60 days' notice of such termination, in which event the Customer will be liable to pay the Vendor for all deliverables and services ordered up to the date of termination."

4 UNFAIR CONTRACTS

EXERCISE CAUTION!
Contract clauses that allow one party and not the other to terminate may fall foul of the Australian Consumer Law

What contracts are covered?

- Pro forma contracts;
- Contracts entered into or renewed on or after 12 November 2016;
- Contracts for sale of goods or services or an interest in land;
- Contracts where at least one party is a small business (less than 20 employees);
- Contracts where the upfront price payable is not more than AUD 300,000 or 1,000,000 if the contract is for over 12 months.

(all of the above must apply)

Fairness ruling

An aggrieved party may bring an action to the appropriate court or tribunal seeking a finding that the clause is unfair under the Australian Consumer Law.

Effect of an unfair TFC clause

If a court or tribunal finds that a TFC clause is unfair under the Australian Consumer Law, it will be void and not binding on the parties.

A termination made under a void TFC clause may be unlawful and expose the terminating party to a claim for damages.

5 WHEN CAN YOU EXERCISE THE RIGHT TO TFC?

TFC IS PERMITTED IF:

All parties agree to terminate the contract.

TIP Make sure your agreement to terminate is recorded in writing and signed. Ideally the written agreement should be formatted as a contract amendment in accordance with the procedure prescribed in the contract for amendments.

OR

The contract gives you the right to TFC.

+

You have given the required number of days' notice and followed the contractual requirements for giving of notice.

TIP Failure to properly follow the termination procedures set out in the contract may result in unlawful termination and exposure to a damages claim.

+

The termination is not made in bad faith.

TIP There may be an implied duty to act in good faith when exercising the right to TFC. See section 6 of this guide.

6 THE DUTY TO ACT IN GOOD FAITH

An implied duty?

An implied duty of good faith appears well-accepted by New South Wales courts. In several Australian law decisions* the courts have recognised that an implied duty of good faith may limit a party's right to TFC if the termination is not conducted in good faith.

However, the position under Australian law is far from clear. There have been decisions to the contrary, finding that the exercise of a TFC clause should not be fettered by an implied duty of good faith*.

What is good faith?

Even if a duty of good faith is implied into a contract, there is uncertainty as to the meaning of the term 'good faith'.

Acting unreasonably, attempting to prevent the performance of the contract or seeking to further an ulterior purpose may be considered conduct in bad faith,** qualifying the right to TFC.

Given the present uncertainty, contracting parties should exercise caution when deciding to TFC.

Each case is likely to turn on its own facts and legal advice should be sought if in doubt.

* For example, Apple Communications v Optus Mobile (2001) NSWSC 365 and Kellogg Brown Root Pty Ltd Australian Aerospace Ltd (2007) VSC 200.

* For example, Leighton v Arrogen (2012) NSWSC 1370, per McDougall J.

** Sunyaporaph v Teachers Federation Health Ltd (2008) NSWSC 1443, per Davies J.

7 WHEN TO SEE A LAWYER

We hope this guide has provided a helpful understanding of the termination for convenience clause and some of the essential legal issues to consider.

You should consult a lawyer if:

- You need help drafting or negotiating a TFC clause that adequately protects the interests of your business. Your lawyer should be able to produce some language that will protect your interests, whilst also being acceptable to the other party to the contract.
- You wish to terminate a contract, but the contract does not allow TFC. Your lawyer will advise you of what other avenues you may have to terminate the contract.
- You aren't sure whether a contract gives you the right to TFC. Your lawyer should be able to give you a definitive answer.
- The other party to the contract is disputing your right to terminate. Your lawyer will be able to advise you of your rights and assist with dispute resolution.

Disclaimer: This guide is intended to provide general information and commentary only. It should not be relied upon as legal advice. Formal legal advice should be sought in relation to matters arising from the contents of this guide.

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