

Tips For Developing a Contract “Exit Strategy”

The American Alliance of Museums offers the following information from Sharon M. Hotchkiss, Attorney at Law. The information shared here is based on the best available information as of publication. Museums are encouraged to seek legal and other expert advice on their specific circumstances, and/or any state or local requirements.

The pandemic taught us many lessons, one of them being the importance of an “exit strategy” in business contracts. Due to shelter-in-place orders and capacity limitations, many museums found themselves with a huge disruption in attendance and loss of income, but still obligated to pay vendors, lenders, and licensors. Before signing any contract going forward, you should confirm it has clear and express language allowing you to cancel should you want or need to.

Below are some tips on what to look for in contracts you are about to sign or are considering terminating.

Termination Clauses:

Many contracts will have more than one way to terminate. The three most common types of termination clauses, listed from the hardest to terminate to the easiest, are:

1. **Termination by expiration of a fixed term:** Many contracts have a definite start date and end date, with no other provision allowing for early termination.
2. **Termination for cause:** This type of termination clause allows a party to end the contract if the other party fails to perform one or more of its obligations (i.e., upon breach or default).
3. **Termination without cause:** Sometimes referred to as “termination for convenience,” such a clause allows one or both parties to end the contract for any reason, or for no reason at all.

Termination by expiration of a fixed term:

Here is an example of a clause that terminates at the end of a fixed term:

“This Agreement shall be effective as of the last date of the signatures hereto (“Effective Date”) and shall terminate one year from the Effective Date.”

In this example, the “term” of the contract is one year. If there is no other termination clause, or force majeure clause (discussed below), this is the hardest contract to exit. Also be aware that many contracts with this type of termination/expiration have an auto-renewal provision that might read something like this:

“Upon expiration of the initial term, this Agreement shall automatically renew for a period of one year unless, at least sixty (60) days prior to the end of the then current term, either party gives the other party written notice of its intent not to renew.”

If your contract contains an automatic renewal provision, make sure you have your termination notice process in place. At the very least you should mark the deadline to give notice in your calendar with at least one warning date to give you time to decide whether you want to renew.

Termination for cause:

A common example of a termination for cause provision allows one party to terminate if the other party fails to perform its important duties under the contract (referred to also as a “breach” or “default”). For example:

“Either Party may terminate this Agreement if the other Party fails to perform any material obligation under this Agreement, if such Party is not able to cure the default within 30 days of the date such Party is notified by the other Party of such default.”

There are also other types of events that can cause termination, depending on the nature of the transaction. In contracts between two businesses, for example, it is common to allow a party to terminate the contract if the other party becomes insolvent (unable to pay their debts when they become due) or files for bankruptcy.

Termination without cause (or for convenience):

This is a good provision to have if you feel uncertain as to whether you will want to stay in the contract until it expires. Keep in mind, however, that the other party might terminate for no reason also and you must consider whether that would leave you in a bind. There are instances, for example, where you may want to “lock in” a specific service at a specific rate.

An example of a termination without cause provision is:

“This Agreement may be terminated by either Party on thirty (30) days written notice to the other Party.”

Please also be aware that the party drafting the agreement might draft it so that only they can terminate early.

Force Majeure Clauses

If the contract does not have a termination without cause provision, and you are concerned that an emergency such as the pandemic will render the contract impossible or difficult to perform, you should look to see if your contract has a force majeure clause. Force majeure refers to a clause that removes liability for unavoidable catastrophes that interrupt the expected course of events and prevent participants from fulfilling their stated obligations. An “occurrence beyond a party’s reasonable control” is the crux of force majeure—a term stemming from the Latin phrase for “superior force.”

A boilerplate force majeure clause may read something like this:

“Neither party shall be responsible for any resulting loss if the fulfillment of any of the terms or provisions of this agreement is delayed or prevented due to any occurrence beyond a party’s reasonable control, including acts of God, fires, floods, wars, sabotage, accidents, labor disputes or shortages, governmental laws, ordinances, rules and regulations.”

Elements you should look to address in the force majeure clause are:

- » The **threshold** for the force majeure clause to apply.
- » The **types of events** that constitute a force majeure event.
- » **Steps either party can take** after the force majeure event.

The threshold for the force majeure clause to apply:

Parties should establish a threshold for force majeure to apply. This means to what extent the event outside your control interfered with you being able to fulfill your contractual obligations. For example, many contracts state the event must make it impossible for you to fulfill your contractual promises. This is a very high threshold to meet. If you want it to be easier to be able to rely on the force majeure clause, you should consider a lower threshold, such as the force majeure event results in “substantial interference with performance” or makes it “commercially impracticable.” Since the pandemic, many businesses have added to their force majeure clauses that they will forgive a default if it makes carrying out the contract “illegal” (for example, due to governmental mandates).

Types of events that would be considered a force majeure event:

When you are negotiating the terms of a force majeure clause, make sure to include specific examples of events that could cause you to default on your obligations—such as tornadoes, earthquakes, fire, etc.

Finally, most force majeure clauses have “catch-all” language, or something that says, “anything outside the reasonable control of the parties.” You should use language specific to your museum when writing your force majeure clause. For example, a museum now entering into an exhibition agreement should consider including issues that could arise from a pandemic and use specific terms such as “travel restrictions, pandemic, epidemic, infectious diseases, government orders and mandates.”

If your concerns include results of extreme weather, you might want to add language to that effect, for example, “delays in transportation, electrical power outages, or degradation in electronic communications systems.” Every specific condition that is included in the contract provides you with greater protection. A contract with a force majeure clause that specifically outlines causes will more likely hold up in court than those that rely solely on “catch all” language.

Explain what will happen:

Once you have the threshold allowing you to invoke the force majeure clause, and the type of event that would excuse the performance, the contract should explain what happens next. Here are examples of questions you may ask yourself:

- » Can either party temporarily suspend their performance?
- » Can either party terminate the contract if the force majeure event continues for a certain length of time?
- » Will the delay extend the contract? (Keep in mind that scheduling with a subsequent exhibit or event might prohibit this.)
- » What about future payments?
- » Will the party who paid money up front get a refund?
- » Does it allow for any renegotiation of the business terms?

As you can see, these are not simple issues, but if you address them up front with a well-drafted contract, you can avoid most disputes and unnecessary monetary losses.

Time to Terminate

If you are currently in a contract you want to terminate, you should examine the contract (including any amendments) and look for the types of clauses defined above. If your contract has a termination and/or force majeure clause, be careful to follow any applicable notice requirements closely. Any failure to comply with the contractual requirements may render the termination notice invalid.

Crafting carefully considered termination and force majeure clauses is one way that businesses can mitigate uncertainty. Ultimately the power is in the hands of each party to protect themselves as much as possible from potential future failures of performance—more effort spent in drafting thorough contracts now should materially reduce time spent resolving disputes in the future.

This summary is a basic overview of termination and force majeure clauses only. It is for informational purposes only and does not constitute specific legal advice. If you are concerned about a specific contract and its terms, please seek advice from an attorney licensed to practice in your state.