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Impact of Coronavirus Emergency on Contract Law — Special Issue

The Impact of the Health Emergency on Contract Law: National Report Peru

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Pacini Giuridica

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The global pandemic caused by Covid-19 has affected many areas of social life. One of these is undoubtedly civil, commercial and consumer contracts (B2B and B2C). The Peruvian Government declared a nationwide lockdown under art 137.1 of the Peruvian Consti-

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tution (PC),[1] which authorises the restriction or suspension of the exercise of certain fundamental rights. Such restrictions were, as far as this work is concerned, the compulsory immobilisation during time slots and the prohibition of any economic activity that did not consist of, or was not linked to, the provision of essential goods and services.[2]
The severity of the restrictions has been reduced as the lockdown has been extended. Some economic activities were later partially released, subject to constraints designed to ensure the health of the citizens. As of the writing of this report, the lockdown has been extended until 30 June 2020, and the number of economic activities allowed under e-commerce and delivery has also been expanded.[3]

I. Peruvian contract law provisions dealing with circumstances interfering with contractual performance

1. General framework

Art 1361 of the Peruvian Civil Code (CC)[4] prescribes that 'contracts are obligatory in so far as it has been expressed in them'; likewise, art 1354 provides that 'the parties can freely determine the content of the contract, as long as it is not contrary to a legal rule of a mandatory nature'. Read together, these rules provide that what the parties freely agreed upon is binding.
Both provisions derive from the principle of *private autonomy*, recognised in art 2.14[5] and the first sentence of art 62[6] of the PC. In turn, from these provisions derive the fundamental

[1] 1993 Political Constitution of Peru; for brevity, we are not quoting some provisions mentioned in the text, which could be consulted in <https://spijweb.minjus.gob.pe/>, including an official English translation of the PC.

[2] The national lockdown was declared by Supreme Decree No 044-2020-PCM (published 15 March 2020, entered into force 16 March 2020), this norm was extended by Supreme Decree No 046-2020-PCM (published 18 March 2020, entered into force 19 March 2020), determining the essential activities which could continue operating.

[3] A first set of activities which could restart operations was declared by Supreme Decree No 080-2020-PCM (published 3 May 2020, entered into force 4 May 2020), Supreme Decree No 094-2020-PCM (published 23 May 2020, entered into force 25 May 2020) annex; a second set of activities was approved by the Ministerial Resolution No 142-2020-PRODUCE (published 8 May 2020, entered into force 09 May 2020) and Supreme Decree No 110-2020-PCM (published 18 June 2020, entered into force 22 June 2020); each economic activity must follow the requirements of Ministerial Resolution No 239-2020-MINSA (published 28 April 2020).

[4] Civil Code, Legislative Decree No 295.

[5] 'Every person has the right to: … contract for lawful purposes, provided that there is no violation of public policy norms'.

[6] 'The freedom to contract guarantees that parties can validly agree according to the rules in force at the time of the contract'.

rights to decide whether or not to conclude a contract, to choose with whom to contract and to regulate the content of contracts.[7] Thus, in Peru, contracts are mandatory and must be performed exactly because they are a manifestation of the exercise of the fundamental rights of the contracting parties.[8]

It should be noted that this understanding of the binding nature of the contract harmonises the notion of respect for the fundamental rights of the contracting parties with their search for economic efficiency through the free determination of the content of the contract.

Nonetheless, it is generally held that the second sentence of art 62 of the PC, by providing that 'contract terms may not be modified by law or other provisions of any kind', would have taken up the doctrine of the *sanctity of contracts* in an absolute scheme.[9] Thus, one could claim that contract terms are immutable and that they cannot be revised under any circumstances, like a pandemic.

Yet, this statement does not correspond to the reality of Peruvian law. A harmonious reading of arts 2.14 and 62 of the PC allows us to conclude that private autonomy in contracting is subject to explicit and implicit limits so that the prohibition of modification of contractual terms in art 62 is not absolute.[10] In this sense, the principle of the bindingness of the contract is not absolute since there is a constitutional basis for an exceptional revision of contracts.

This constitutional basis has been materialised through the different provisions that the CC provides, which we develop below.

2. Impossibility of performance due to unforeseen circumstances or force majeure

Art 1315 of the CC defines the force majeure as 'the non-attributable cause, consisting of an extraordinary, unforeseeable and irresistible event, which prevents performance of the obligation or determines its partial, late or defective performance'. The foundation of the rule is common sense – by requiring non-attributable, extraordinary, unforeseeable and irresistible events, it is understood that the debtor cannot perform any conduct to comply with the contract.

In this sense, given their restrictive nature, the measures adopted by the Government can be qualified, in principle, as cases of force majeure in those contracts linked to non–es-

[7] *Instituto Superior Pedagógico Belaúnde v Ministerio de Educación* [2004] 02158-2002-AA/TC [2]; Baldo Kresalja and Cesar Ochoa, *Derecho Constitucional Económico* (Fondo Editorial PUCP 2009) 280.

[8] Manuel de la Puente y Lavalle, 'La libertad de contratar' (1996) 33 *THĒMIS-Revista de Derecho* 7, 8.

[9] Ibid. 10.

[10] *Cooperativas de trabajo v Congreso de la República y Ministerio the Trabajo* [2004] 02670-2002-AA [3(d)]; the *social market economy* model adopted in art 58 of the PC reinforces this affirmation, B Kresalja and C Ochoa (n 7) 286.

sential economic activities – and therefore not allowed –. Yet, the impossibility to perform the contract should not be understood in physical terms. On the contrary, the impossibility is *objective* – it falls on the obligation – but *relative* since distinct contracts may require variable cooperative efforts to determine the irresistibility of the event.[11] In this sense, impossibility must be conceived and interpreted with a criterion of reasonableness and evaluating the interests of the parties protected by the contract. This is also because impossibility has different legal consequences in Peruvian law, which depend on the scope of the impossibility itself.

If the impossibility is definitive or, even without being definitive, it results in the loss of utility of performance for the creditor, the consequence is that the debtor is relieved of the obligation to compensate for the breach. The same consequence shall apply if the impossibility – definitive or temporary – was only partial, but incomplete performance would be useless to satisfy the creditor's interest.

If, on the other hand, the temporary impossibility does not cause the creditor's loss of interest in delayed performance, the consequence will be that the debtor will be exonerated from liability for breach only for the duration of the impossibility and must resume performance once the impossibility disappears. Conversely, if the impossibility of performance is partial, but the creditor retains an interest in the incomplete performance, the debtor shall perform the contract on those terms, but its initial payment will be reduced proportionally, and the reduced amount must be returned if it has already been received.

These consequences of impossibility due to unforeseen circumstances or force majeure are set out in art 1316 of the CC, and are reiterated in the treatment of the *theory of risk* in the obligations to give a certain good – art 1138 CC –, in the obligations to do – art 1156 CC – and the obligations to abstain – art 1160 CC –, as well as in the regulation of contracts with reciprocal benefits – arts 1431 to 1433 CC –.

Finally, in the case of impossibility in plurilateral contracts (with more than two parties), in which obligations are autonomous – not reciprocal – the impossibility of one obligation has consequences only concerning the injured party unless that service is essential to the transaction as a whole, where total cancellation would be appropriate – art 1434 CC –.

3. Excessive onerousness of the performance or hardship

The CC also contemplates the *excessive onerousness of the performance* (hardship), in which the unforeseeable event, even if it does not make performance impossible in the agreed terms, determines that the performance entails excessive costs or sacrifices for one

[11] Gastón Fernández Cruz, 'El deber accesorio de diligencia en las relaciones obligatorias' (2005) 13 *Advocatus* 143, 155.

or both parties, which were not contemplated or assumed by them when they decided to enter into the contract. The scope and application of this figure are regulated, fundamentally, in arts 1440, 1441, and 1442 of the CC.

In Peru, the first remedy for hardship situations is the adaptation of the contract by the court or arbitral tribunal through the reduction of the performance whose execution has been increased or the increase of the counter-performance. Exceptionally, if adaptation is not possible due to the nature of the obligation or the circumstances of the case, termination of the contract may be demanded. The defendant may also request termination, in which case the court should first determine that it is impossible to adapt the contract. In any event, the effects of termination shall not extend to performance already rendered.

On the other hand, note that – unlike uniform contract law instruments – the CC does not expressly provide for renegotiations between the parties before requesting adaptation or termination at the court, yet this does not impede the renegotiation. The parties should reach an agreement to overcome the imbalance of the contract according to their interests, without the intervention of a third party. Yet, despite being the most reasonable alternative, there will not be consequences if the parties request adaptation or termination to the court.

The hardship and its remedies apply to commutative contracts of continuous, periodic or deferred performance; that is, those in which the sacrifices and benefits of the parties are agreed from the beginning and there is a lapse of time between the conclusion of the contract and its execution, or between the performance of each obligation of the parties. However, the CC contemplates some exceptions to this rule, specifying that the figure and its remedies may also be applied to (i) commutative contracts of immediate execution when the obligation of one party has been deferred for a cause not attributable to him; (ii) to aleatory contracts, when the hardship is produced by causes alien to the risk of the contract; and, (iii) to contracts with unilateral performance, in which case the adaptation may only be achieved with the reduction of the performance, without prejudice to the subsidiary remedy of termination.

Finally, the waiver of remedies for hardship is void – art 1444 CC –. Such remedies may be requested within three months after the definitive cessation of the unforeseeable events, the expiration of the period entails the loss of the rights to request the adaptation and termination of the contract – arts 1445 and 1446 –.

4. The disputed application of the *frustration of purpose*

The CC does not regulate the frustration of purpose of the contract, which is why there is no unanimity in the scholarship regarding its application in Peru.[12]

In this figure, expected performance – although possible and therefore enforceable – has lost its utility concerning the practical purpose pursued by the creditor through the contract, due to an unforeseeable event which supervenes after the conclusion of the contract. In these cases, the other party knows and assumes the practical purpose, since mere individual motives have no place.

The application of the frustration of purpose would be possible based on a broad interpretation of the hardship provision – art 1440 CC –, specifically from the language which provides that the injured party may request the court to ‘increase the counter-performance’ to cease the imbalance, and if this is not possible due to the nature of the obligation or the circumstances, ‘the contract may be terminated’. This implies assuming that the obligation of the aggrieved party is excessively onerous because it must be performed in exchange for something impossible to provide the expected utility. It is precisely because it is impossible to achieve the expected benefit that termination of the contract would be the appropriate remedy.

This questionable interpretation seems to have been rejected by the recent *Draft Proposal for the Improvement of the Peruvian Civil Code*,[13] since it proposed the independent regulation of the *frustration of the cause*, establishing different consequences according to whether the frustration is definitive or temporary. In the latter situation, the affected party may terminate the contract if the exact performance of an essential obligation is prevented.[14]

[12] In favour of the application, see Eduardo Benavides Torres, ‘Hacia una revalorización de la finalidad contractual’, in Alfredo Bullard and Gastón Fernández (eds), *Derecho Civil Patrimonial* (Fondo Editorial PUCP 1997) 169-83; against the application, mainly because there is no express rule providing it, see Juan Espinoza Espinoza, ‘La doctrine of frustration: ¿es factible su aplicación en el ordenamiento jurídico peruano?’ (2018) 49 *Actualidad Civil* 130.

[13] The draft and its explanatory statement are available in <https://www.gob.pe/institucion/minjus/informes-publicaciones/429560-anteproyecto-de-modificaciones-del-decreto-legislativo-n-295-codigo-civil>.

[14] The proposal provides ‘Article 1372-A.- Frustration of purpose of the contract: 1. If the common purpose pursued by the contracting parties is permanently frustrated due to a cause not attributable to them, the contract is terminated by right, unless otherwise agreed. 2. If the frustration is temporary, the contract will be terminated as a matter of law, only if said temporality prevents the timely performance of an essential obligation’.

II. Application of the provisions to certain contracts

1. Construction contracts[15]

It is clear that Government's measures have made it impossible for the contractor – which could be under a B2B and B2C scheme – to perform, thus creating a clear case of force majeure, the effects of which will depend on the scope of the impossibility, the nature of the obligation and the creditor's interest and practical purpose, as noted above.

The contractual remedies available to the principal are limited. He may not, during the impossibility, require the contractor to carry out the work or claim compensation for any damage caused by such impossibility. Yet, the principal is not obliged to pay the contractor any compensation during the impossibility[16]. If the contractor demands payment, the principal may invoke the *exception of non-performed contract* – art 1426 CC –, or the exception of limitation period – art 1427 CC –.

On the other hand, if the contractor has partially performed his obligation and this is useful for the principal, the agreed price may be reduced – art 1316 CC –. Moreover, it is unlikely – although not impossible – that the principal will be able to terminate the contract, since this remedy requires the breach to be fundamental,[17] and in the cases of construction, it does not seem that delayed performance will make it useless to resume it once the impossibility has ceased, unless exceptional cases.

Finally, the limitation of liability in these cases will remain until the contractor obtains the administrative authorisation to restart activities, which obviously must be requested as soon as possible. This interpretation is justified in that the force majeure requires that the impossibility of performance be irresistible – art 1315 CC –, and from the moment that the administrative permit is obtained, the impossibility ceases to be so. Note that the time

[15] We recall that our analysis addresses contracts between private parties, excluding the regulation of Public Procurement Law. Yet, one must note that according to the First Final and Complementary Provision of the Public Procurement Bylaw (Supreme Decree No 344-2018-EF) the Civil Code supplements Public Procurement Law, a view also adopted by the Supervisory Body for the Procurement with the State (OSCE for its abbreviation in Spanish) in *Legal Consultation No 17-2018-JUS/DGDNCR* [2018] para 56; moreover, practitioners expressed the view that the distancing of Public Procurement Law from the principles of private contracting leads to unfair solutions in particular cases, see Giusseppi Vera Vásquez and Carlos Aguilar Enríquez, 'Entre la teoría contractual y las normas de contratación pública: Una necesaria mirada a raíz del Covid-19' (2020) 71 *Actualidad Civil* 155.

[16] This rule is different from that provided in the Public Procurement Bylaw, in which, according to art 142.7, the principal must reimburse the expenses necessary to suspend the performance to the contractor.

[17] We believe that under Peruvian law, the attribution of the breach is not a requirement for the termination, see Manuel de la Puente y Lavalle, *El contrato en general* (vol 2, 2nd edn, Palestra 2011) 388-89; yet, we recognise that this is a disputed matter within national scholarship, see Anibal Torres Vásquez, *Teoría General de las Obligaciones* (vol 1, Instituto Pacífico 2014) 152, who argues that the breach must be attributable to the debtor in order to allow termination.

during which the administrative authority evaluates the request is still governed by the force majeure provisions, and any delay in this period is non-attributable to the contractor.

2. Contracts for the provision of educational services

The pandemic has also given rise to a discussion about the possible effects on the performance of contracts for the provision of educational services by private institutions, at school and university level. Once the lockdown was declared, private institutions – schools and universities – decided to resume educational work under the virtual scheme. This measure led to different positions on the enforceability of the service and the applicable figures to this case.

A first position argues that, with the virtual scheme, consumers would be receiving an inaccurate (partial or defective) performance regarding what was initially agreed in the contract, and would, therefore, be entitled to a reduction in the remuneration – art 1316 CC –. Besides, it could be argued that there is a fundamental breach, and consumers could terminate the contract – art 1428 CC –, obviously without compensation because the breach is not attributable. Another position supports the application of the hardship, assuming that the virtual scheme has much lower economic value than the contracted service face–to–face, which would enable to request the court for the reduction of the payment, without denying the possibility of renegotiating with the educational institution. We believe that none of these positions is correct. We do not share the idea that the virtual educational service has a lower economic value than the one agreed in the contract, justifying a reduction of payment assumed by the consumers, under the hardship provision. In most cases, universities incur in unpredictable expenses to adapt their service, which are not necessarily inexpensive than planned expenses. Likewise, although the virtual scheme is partially different from the face–to–face education, we believe that it is not a defective performance of the contract. Indeed, the practical purpose of the education contract, which is the transmission of knowledge to consumers and the achievement of learning objectives, is still achieved, at least in the majority of cases. On the other hand, the possibility – exceptional – of executing this different service derives from the fact that the educational service is an *essential public service* under Peruvian law. Such a qualification remains even if a private institution provides the service, and obliges the institutions to guarantee its accessibility, continuity and adaptability. Thus, according to the circumstances, performance under the virtual scheme is a legitimate adaptation of the institution's obligation.

The adaptation is not only based on the public and essential nature of the educational service, but also on the fact that the impossibility for force majeure, by requiring that the impediment to performing must be irresistible, obliges the debtor to make every effort to overcome it, and therefore it is reasonable to affirm that the implementation of the virtual

scheme prevented the pandemic as an event which precludes supplying educational services.[18]

The Ministry of Education seems to adopt this position.[19] After qualifying the educational contract as a B2C contract, the Ministry addressed the issue not as a force majeure event, but from the obligation of institutions to report on the costs of supplying educational services in the face-to-face and virtual schemes, and on proposals to amend the contract. With this information, users can select between continuing to receive the service, or making use of a *right to unilateral termination*,[20] demanding restitution of the registration fee, admission fees and any other advanced payment, proportionally to the time the student has been at the institution, discounting any outstanding debts.

The decision of the Ministry of Education to consider the virtual scheme as a case that enables unilateral withdrawal, which is not a remedy for breach of contract – attributable or not –, indicates that the obligation to supply educational services is not being breached. If it were considered as such, consumers would have at their disposal remedies such as the proportional reduction of the payment or the termination of the contract.

3. Lease contracts

Regarding leases, the problem is that some lessees, due to the lockdown, may experience financial difficulties in paying the rent.

Since it is a monetary obligation, it is not appropriate to affirm the existence of an impossibility for force majeure since money will never disappear. However, it could be argued that in such cases there is an *economic impossibility* for the lessee to pay, yet it is doubtful whether this figure is similar to the impossibility in the strict sense since the latter must necessarily be objective – over the obligation – and not on the subject. Thus, if the lessee does not pay the rent, the lessor may exercise the contractual remedies for breach, including specific performance and compensation for damages, since performance is not only possible, but the breach would be attributable to the debtor.

Regarding this issue, Congress is currently debating two bills regarding the economic impossibility of the lessee to pay the rent. The first one aims to suspend the payment of the rent, interests and penalties for the entire duration of the lockdown and two months

[18] It is possible to conclude differently regarding elementary school, in which the circumstances and nature of the obligation – contents and objectives of the education at this level, features of the age of the students –, would not be able to supply the service under the virtual scheme. This, of course, means that institutions are not able to resist the consequences of the force majeure event, in which case there is a non-attributable breach of the contract.

[19] Legislative Decree No 1476 (published 5 May 2020, entered into force 6 May 2020).

[20] The Legislative Decree uses the term '*resolución*', being its literal translation the term 'termination', yet the meaning of this provision is an unilateral right of withdrawal, known in other jurisdictions as *résiliation* (French law), *Kündigung* (German law) and *recceso* (Italian law).

after if the lessee demonstrates that he is unemployed, his remuneration was reduced, provoking the reduction of his income, and if the income for the use of the property has decreased by more than forty per cent.[21] The second attempts to suspend evictions during the lockdown and 45 days after for housing leases.[22] Regarding the first bill, we consider that a distinction between housing and commercial leases is necessary because as argued before, a modification of the terms of the contract through legal regulations must be justified on public interest consideration – arts 14.2 and 62 of the PC –, and arguably, protecting housing of unemployed lessees and its family is included in such goal, yet, it does not seem the case for commercial leases. Regarding the second bill, its reduced scope on housing leases makes this attempt constitutionally legitimate, yet non-payment is not the only reason for which lessors can evict lessees – art 1697 of the CC –. Thus, to suspend the eviction for other breaches different than non-payment seems problematic.

In the case of a lease for commercial purpose, if the possession is not useful, at least temporarily, to achieve the practical purpose for which the contract was concluded, the only applicable figure ends up being the frustration of the contract, through the disputed broad interpretation of the hardship provision. Yet, it must be verified whether the practical purpose was shared and whether it was frustrated.[23] Alternatively, it would be possible to argue that there is a non-attributable breach by the lessor of his obligation to maintain the lessee in the use of the property during the term of the contract – art 1680.1 CC – and consequently, he could raise the exception of non-performed contract to oppose the lessor's payment request. However, this interpretation does not seem to correspond to the design of the CC, which regulates the liability for latent defects of the goods in a different regime applicable to all contracts consisting in the transmission of property or possession.[24]

[21] Bill No 5004/2020-CR.

[22] Bill No 5238/2020-CR; note, however, that in Peru, the eviction is a right for the protection of property rights, rather a remedy for breach of contract.

[23] The good could still be useful for a purpose (eg storage), in which case there is not frustration of the contract. In this case it is also possible to argue hardship because what is being obtained is only a part of what motivated the contract.

[24] National scholarship argues, for instance, that the lessor's obligation is not permanent during the lease contract, and that when he hands over the possession, he is entitled to conditional restitution upon the termination of the lease, see Jack Bigio Chrem, 'El Contrato de Arrendamiento' (1994) 30 *THĒMIS-Revista de Derecho* 197, 205; yet, we are working in a paper which argues for a unitary concept of breach of contract within Peruvian Contract Law. From this standpoint, current solutions for problems in lease contracts provided in Property Law can also be solved by the general regime of breach of contract.