



Advocates  
& Solicitors

## **CLAIM PERIOD OF BANK GAURANTEE, NOT LIMITED TO 1 YEAR**

**Larsen & Turbo Ltd. & Anr. v. Punjab National Bank & Anr.**

<b>Case No.</b>	<b>W.P. (C) 7677/2019</b>
<b>Date</b>	<b>28 July 2021</b>
<b>Court</b>	<b>High Court of Delhi</b>
<b>Coram</b>	<b>Hon'ble Mr. Justice Jayant Nath</b>

## 1. BRIEF FACTS

- 1.1 Larsen & Tourbo (hereinafter “**Petitioner**”) one of the biggest construction company in the country, entered into a bank guarantee agreement with the Punjab National Bank (hereinafter “**Respondent No.1**”). The dispute in the present case arose when the Respondent No.1 issued communication dated 18.08.2018 stating that the Claim period in a Bank Guarantee must be for at least 12 months and in case the said claim period is less than 12 months, it would render the claim period void and will effectively increase the claim period under the bank guarantee to 3 years under the Limitation Act, 1963.
- 1.2 Further, Indian Bank’s Association (“Respondent No.2”) issued communication/circular dated 10.02.2017 addressed to the banks stating that it would be open for the banks to stipulate as a condition precedent that if the claim is not lodged before a stipulated time, the bank guarantee shall be revoked or terminated but the stipulated date cannot be less than one year in any event.
- 1.3 Bring aggrieved by the said notifications, the Petitioner filed a writ petition under Article 226 of the Constitution seeking appropriate writ to quash the Orders furnished under the mentioned letters. The Petitioner contended that based on an erroneous interpretation of section 28 of the Contract Act, Respondent bank forces a mandatory and an unalterable claim period of a minimum 12 months for the bank guarantee.

## 2. ISSUES RAISED:

- Whether the concerned Court has the territorial jurisdiction to entertain the writ petition?
- Whether the Respondent(s) can limit the validity of the claim period of minimum 12 months for the bank guarantee under the interpretation of Exception 3 of Section 28 of the Indian Contracts Act, 1872?

## 3. SUBMISSIONS OF THE PETITIONER

### A. *Jurisdiction of the Court*

- 3.1 On the issue of Jurisdiction of the particular Court, the Petitioners while filing a replication reiterated that the head office and the registered office of Respondent No. 1 is Delhi. Moreover, the letters dated 18.08.2019 & 28.03.2019 of Respondent No. 1 clearly shows that the Law Division of the Respondent No. 1 that is situated in Delhi took care of all the decisions and communications.

### B. *Interpretation of Section 28*

- 3.2 The senior counsel for the Petitioner asserted that if section 28 is interpreted in its simplest terms, it could be construed that even though extinguishment of the remedy or curtailing the time period for invoking the remedy is not permitted, extinguishment of the right was held to be not hit by section 28 of the Contracts Act.
- 3.3 Reliance was placed on the report of the Expert Committee headed by Sh. T. R. Andhyarujina. It was contended that based on this Report, Exception 3 of Section 28 was inserted in the Act which came to the rescue of the bank for curtailing the period of limitation to institute proceedings before a court of law to a period of 12 months rather than the compulsory period of 3 years or 30 years as per the Limitation Act. However, the exception does not touch upon the issue of claim period in the bank guarantee. Exception 3 of the Section 28 does not deal with the claim period at all.

C. *Exception 3 of the Section deals only with limitation period for filing of suit before a court of law*

3.4 The Petitioner relied on the case of *Explore Computers Pvt. Ltd. v. Cals Ltd. & Anr.* to interpret to scope of Section 28 of the Contracts Act. Moreover, reference was made to RBI Circulars dated 01.07.2013 & 01.07.2015 where a model guarantee bond is showcased. The Petitioner stated that there is no mention of claim period in those forms as well.

#### 4. SUBMISSIONS OF THE RESPONDENT(s)

##### A. *Jurisdiction of the Court*

4.1 The Respondent No. 1 contended that the concerned Court does not have the territorial jurisdiction to entertain the particular writ petition. It was contended that the head office of the Petitioner is in Mumbai and the letters issued by Respondent No. 1 that are in challenge in the current proceedings were issued from the Mumbai branch of the Respondent No. 1.

4.2 *Arguendo*, with reference to the maintainability of the Writ petition, the Respondent No. 1 stated that even though the concerned court entertains the writ petition, the issue between the parties are purely contractual in nature and does not have a hint of public policy in it. The dispute does not violates any of the fundamental rights of the Petitioner and shall not be maintainable.

##### B. *Interpretation of Section 28*

4.3 With reference to Exception 3 of the Section 28 of the Act, the Respondent No. 1 stated that the particular section entitles a party to stipulate a term in the bank guarantee for extinguishment of the right or discharge of any party from any liability after the expiry of such stipulation which is not less than one year from the date of occurring of a specified event.

4.4 Reliance was also placed on the counter-affidavit filed by RBI where it was stated that banks could have autonomy while taking commercial decisions in this regard and the same come under the purview of Exception 3 of the Section 28.

4.5 It was further contended that requirement of minimum claim period of one year has been endorsed by the Ministry of Finance, Department of Financial Services in consultation with RBI as conveyed in letters dated 23.04.2019 and 21.05.2019 addressed to respondent No.2.

#### 5. DECISION OF THE COURT:

##### A. *Jurisdiction of the Court*

5.1 The Hon'ble High Court observed that question as to whether a high court has territorial jurisdiction to entertain a writ petition must be answered on the basis of the averments made in the petition. By analysing the letters dated 18.08.2018 & 28.03.2018, the Court held that the communications were made through the Law Division of the Respondent No. 1 which is situated in Delhi. Hence, the infraction of the rights of the petitioner also occurs in Delhi. *"In view of the above facts, it is manifest that the part of cause of action has arisen within the territory of this court."*

- 5.2 Reliance was placed upon the case of Eastern Coalfields<sup>1</sup> to reach to a conclusion that under Article 226 (2), an order or writ can be issued by a high court in relation to territories within which the cause of action wholly or in part arises.

*B. Interpretation of Section 28*

- 5.3 The Court while determining the scope of limiting the time period of the bank guarantee placed reliance on the case Kerala Electrical & Allied Engineering Co. Ltd.<sup>2</sup> which dealt with old Section 28 of where it was held that Section 28 makes two kinds of agreements void. Those are

*“(i) an agreement which limits the time within which a party thereto may enforce his rights under or in respect of a contract by the usual legal proceedings in the ordinary tribunals; (ii) an agreement relinquishing the remedy only, by providing that if a suit is to be filed that should be filed within a time limit— the time limit being shorter than the period of limitation under Limitation Act—will be hit by S. 28”*

- 5.4 In the said Kerala High Court in Kerala Electrical & Allied Engineering Co. Ltd, it was established that limiting the time within which the rights of the party will be enforced shall be void provided that the rights continue to exist even beyond the shorter agreed period of enforcement. If beyond the shorter period that is mutually agreed by the parties and the rights are not kept alive, then such an agreement putting a time limit to sue shall not hit by section 28 of the Contract Act.

- 5.5 However, after the settled legal position about old Section 28 of the Contract Act including the aforesaid judgment of the Kerala High Court in Kerala Electrical & Allied Engineering Co. Ltd (supra), the Law Commission of India in his Ninety-Seventh Report dated 31.03.1984, recommended suitable amendment to Section 28 of the Contract Act to render invalid contractual clauses that extinguish on the expiry of a stated period the rights accruing from the contract. Thereafter, Section 28 was amended.

- 5.6 The Court observed that the newly added section 28 of the Contract Act was enacted to do away with the earlier distinction between remedy and right i.e., a clause barring the remedy only was void but a clause extinguishing a right was valid. The said clause provided that the beneficiary of the bank guarantee i.e. creditor would have time to approach the appropriate court for enforcement of his rights under the bank guarantee in terms of the provision of the Limitation Act i.e. 3 years for private parties and 30 years for government parties. However, in this background, an Expert Committee headed by T.R. Andhyarujina Committee recommended that the said period be reduced to one year for enforcing the rights under the bank guarantee after happening of a specified event. Thereafter, Exception 3 to section 28 of the Contract was added in 2013, which read as following:

***“Exception 3.—Saving of a guarantee agreement of a bank or a financial institution.—This section shall not render illegal a contract in writing by which any bank or financial institution stipulate a term in a guarantee or any agreement***

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<sup>1</sup> Eastern Coalfields Ltd. & Ors. v. Kalyan Banerjee, (2008) 3 SCC 456 (“Eastern Coalfields”).

<sup>2</sup> Kerala Electrical & Allied Engineering Co. Ltd. v. Canara Bank & Others, [1980 SCC OnLine Ker 28]

*making a provision for guarantee for extinguishment of the rights or discharge of any party thereto from any liability under or in respect of such guarantee or agreement on the expiry of a specified period which is not less than one year from the date of occurring or non-occurring of a specified event for extinguishment or discharge of such party from the said liability...”*

- 5.7 The Court held that the narration of the historical facts leading to the present section 28 of the Contract Act clearly demonstrates that exception 3 to section 28 of the Contract Act deals with the rights of a creditor to enforce his rights under the bank guarantee after happening of a specified event and it does not in any manner deal with the claim period within which the beneficiary is entitled to lodge his claim with the bank/guarantor.
- 5.8 The Court also observed that there is a clear admission by the Respondent No. 1 that Exception 3 deals with the period within which the beneficiary can invoke the bank guarantee after expiry of the validity period. Thus, it was held that Respondents erred in interpreting the scope of Exception 3 and the communications issues by the Respondents dated 18.08.2018 & 28.03.2019 are clearly vitiated.

## **6. PSL OPINION**

- 6.1 The Delhi High Court in this judgment while providing a clear interpretation of Exception 3 of Section 28, has settled the position of law so far as the claim period with respect to Bank Guarantee is concerned. This ruling of Delhi High Court will aid many infrastructure and construction companies, which generally enter into short term contracts, as they cannot now be forced to keep a minimum claim period of 12 months unnecessarily despite the contract being concluded.