

A Note on recent changes to make Claim period In all Bank Guarantee as Min One Year.



Back ground

All companies especially in project business (industrial or infrastructure) required to provide Security in form of Bank Guarantees. These Bank Guarantees not only involve cost but also blocks the Credit limits with Banks. Recently all banks have started implementing a RBI Circular No Dir.BC.12/13.03.00/2013-14 enforcing claim period to be minimum 1 year from expiry of Guarantee.

Amendment in Contracts Act

This has reference to Section 28 of Indian Contract Act 1872, whereby Banks are not absolved of its obligations to make payment under the Guarantees until expiry of claim period which is applicable to original transaction.

The amendment to Section 28 of Indian Contract Act was by insertion of exception 3 which permitted Banks and Financial Institutions to limit the period to make claim to one year.

As per newly amended Section 28(b) of Indian Contracts Act 1872, beneficiary can enforce the Guarantee till limitation period as provide in Limitation Act. Once the Bank Guarantee expires the beneficiary losses a remedy in form of an instrument to enforce the claim although the right to enforce the claim as per Limitation Act survives.

Since the Exception 3 to Section 28 is a special law and would prevail over provisions of Limitation Act, Banks shall be released from their obligation to pay for the claim, after a period of one year after the expiry of original guarantee period.

Supreme Court Judgement

The Hon'ble Supreme Court of India in Union of India V.s Indusind Bank (2016), judgement specified the claim period cannot be less than one Year after the expiry of original guarantee period.

Effect of this amendment

This puts on lot of financial burden on companies to increase their claim period to 1 year from what was agreed norm of 1 month or 3 month.

Conclusion /Remedy:

Although the amendment in the Contracts Act, the Hon'ble Supreme Court judgement and RBI circular makes it mandatory to have minimum claim period of 1 year in all Bank Guarantees issued, however if the beneficiary discharges the original Instrument of Bank guarantee back to the issuing bank, it shall mean that beneficiary has released its right to claim under the Guarantee and Bank Guarantee can be closed in their books and limits can be restored.