THE CONTINGENT FOUNDATIONS OF FINALITY: A CRITICAL ANALYSIS OF THE ENFORCEMENT PERIOD FRAMEWORK FOR BANK GUARANTEES UNDER SECTION 28 OF THE INDIAN CONTRACT ACT, 1872

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ABSTRACT

Indian banking law has a complicated relationship with time. How long can a bank be held liable under a guarantee? Who gets to decide when that liability ends? These questions have produced decades of judicial back-and-forth, legislative fixes, and commercial frustration, and Section 28 of the Indian Contract Act, 1872 sits right at the middle of it.

The provision was meant to stop powerful contracting parties from writing legal remedies out of their contracts. Simple enough. But when you apply it to bank guarantees, things get messy fast.

This paper follows the whole arc. It starts with the pre-1997 judicial distinction between extinguishing rights and barring remedies, a distinction that looked neat on paper but was deeply unfair in practice. Then comes the 1997 amendment, which killed that distinction but created fresh headaches for banks. Then the 2013 insertion of Exception 3, which was Parliament's attempt to give banks some commercial room to breathe without completely dismantling what the 1997 reform built.

The centrepiece of the analysis is the Delhi High Court's 2021 decision in *Larsen & Toubro Ltd. v. Punjab National Bank*, which drew what is now the leading distinction between validity periods, claim periods, and enforcement periods. The paper looks carefully at what that decision got right, and at something that hasn't received enough attention: the Court's interpretation rested heavily on the fact that both parties agreed with each other. That's not a great foundation for a precedent of this importance.

The argument, ultimately, is that the current framework works well enough in practice but is more precarious than it looks. It's built on interpretive choices that are still contestable, and on a selective legislative intervention that raises real questions about where Section 28 goes from here.

I. Introduction and Conceptual Framework

Time is awkward for contract law. Parties create their rights privately, through agreement. But enforcing those rights happens through public institutions, courts and tribunals, that run on statutory timelines. These two systems have to coexist, and Section 28 of the Indian Contract Act, 1872 is what manages the relationship between them. It stops parties from using contract terms to shut the courthouse doors on each other.[1]

The basic idea behind Section 28 isn't complicated: you can't contract your way out of the legal system. This matters especially when bargaining power is unequal, because the stronger party would otherwise have every incentive to draft time bars that the weaker party has no choice but to accept. Section 28 exists to prevent that.

The difficulty is that the provision has never been easy to apply. Courts have repeatedly struggled to draw a principled line between clauses that restrict remedies and clauses that eliminate rights altogether. That distinction, apparently clean, has generated persistent confusion, and nowhere more so than in the context of bank guarantees.

Bank guarantees aren't ordinary contracts. They're risk-shifting instruments. A bank guarantee tells a beneficiary: if the other side fails to perform, you'll be paid out quickly, without a fight. That's what makes them useful. But from the bank's side, a guarantee is a contingent liability sitting on its books. It can't stay open indefinitely. Capital provisioning, risk management, and basic commercial sense all demand an endpoint. The tension between protecting the beneficiary and giving the bank finality is structural. It's built into what these instruments are.

This tension is what gives real legal bite to the concepts of validity period, claim period, and enforcement period. These phrases are often used interchangeably in commercial practice, but they're legally distinct and carry very different consequences. The validity period is the window during which default must occur for the guarantee to be triggered. The claim period is the additional time after expiry within which the beneficiary must formally demand payment. The enforcement period is how long the beneficiary has to go to court if the bank refuses to pay. Three separate stages, three separate sets of legal principles, yet for most of the history of Section 28, they were treated as one question.

[1] Indian Contract Act, 1872, § 28 (as amended up to date).

A lot of the litigation under Section 28 comes from that collapse. Before the legislature stepped in, courts had developed a distinction between clauses that barred remedies (void under Section 28) and clauses that extinguished rights (valid and enforceable). The practical effect was that extinguishment clauses could strip beneficiaries of their rights long before the statutory limitation period expired, with full judicial approval. The Law Commission later described this as producing serious anomalies and hardship, apart from generating unnecessary litigation, which, given how diplomatically law commissions usually write, suggests it was pretty bad.[2]

The 97th Law Commission Report, produced on the Commission's own initiative rather than in response to a government request, is the turning point in this story. The Commission's argument was direct: the judicial distinction between limitation (which bars your remedy) and prescription (which kills your right) doesn't hold up. Both mechanisms leave you without legal recourse after a certain time. The only difference is how the clause is drafted. Allowing one while prohibiting the other was an invitation to gaming the system. The Commission called it allowing parties to create a private law of prescription, which is exactly what it was, and exactly what the Contract Act was supposed to prevent.[3]

That report led to the 1997 amendment, which brought extinguishment clauses within Section 28's prohibition. But as subsequent events showed, the cure had side effects, particularly in banking, where time-bound extinguishment isn't a tool of exploitation but a functional commercial necessity. Those side effects eventually forced Parliament to insert Exception 3 to Section 28 through the Banking Laws (Amendment) Act, 2012.

The ambiguities in Exception 3 came to a head in *Larsen & Toubro Ltd. v. Punjab National Bank* (2021), which remains the most authoritative judicial attempt to work through the overlapping temporal concepts embedded in bank guarantees and their interaction with Section 28.[4]

This paper traces the whole arc. It argues that while the current framework provides a workable degree of clarity, it rests on foundations that are more contingent than they appear.

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[2] Law Commission of India, 97th Report on Section 28 of the Indian Contract Act (1984) [hereinafter '97th Law Commission Report'].

[3] 97th Law Commission Report, *supra* note 2.

[4] Larsen & Toubro Ltd. v. Punjab National Bank, W.P.(C) 7677/2019, 2021 SCC OnLine Del 3827 (Delhi H.C., July 28, 2021) [hereinafter 'L&T v. PNB'].

II. Pre-1997 Judicial Position: Validity Through Extinguishment of Rights

The doctrinal problem that eventually forced legislative reform didn't arrive suddenly. It built up through judicial decisions that each made sense individually but accumulated into something genuinely hard to defend. Understanding the pattern matters, because it explains both why the 1997 amendment was necessary and why it went wrong in the way it did.

Section 28, before 1997, said nothing explicit about a distinction between rights and remedies. Courts constructed that distinction themselves. The reasoning went like this: Section 28 targets covenants that restrict access to legal proceedings. It doesn't apply to contract terms that define the lifespan of rights themselves. So if a clause said your rights cease to exist after a certain period rather than that you can't sue, it fell outside Section 28's reach.[5]

The Law Commission eventually boiled this judicial position down to two propositions: parties can't substitute their own limitation periods for statutory ones, but parties can provide for the extinction of the very rights that limitation periods were designed to protect. The Commission noted this was highly anomalous. That's putting it mildly.[6]

The lineage of this reasoning runs deep. As early as 1976, the Supreme Court in *Vulcan Insurance Co. Ltd. v. Maharaj Singh* affirmed, without apparent hesitation, that forfeiture clauses in insurance policies do not fall within Section 28 because they extinguish rights rather than restrict the time for enforcement. The Court treated the settled judicial position as self-evident, noting simply that it had been repeatedly held that such clauses are not hit by Section 28. There was no serious engagement with whether the distinction being drawn was actually defensible. That was the problem.[7]

The doctrine found its most consequential articulation in *Food Corporation of India v. New India Assurance Co. Ltd.* (1994). The Supreme Court upheld a clause in an insurance policy saying that no rights existed under the policy unless a claim was made within a specified period. The Court framed it as a condition precedent to the accrual of rights, not a restriction on the time to sue. Your rights didn't expire; they never fully came into existence in the first place.[8]

[5] 97th Law Commission Report, *supra* note 2, at para 4.
[6] 97th Law Commission Report, *supra* note 2, at para 4.
[7] Vulcan Insurance Co. Ltd. v. Maharaj Singh & Anr., (1976) 1 SCC 943 [hereinafter 'Vulcan Insurance'].
[8] Food Corporation of India v. New India Assurance Co. Ltd., (1994) 3 SCC 324 [hereinafter 'FCI v. New India

There's an internal logic to this, but it's worth being clear about what it actually enables. A clause saying "you cannot sue after X date" is void under Section 28. A clause saying "your rights expire on X date" is valid. Both produce identical outcomes: no legal recourse after X. The only difference is word choice. Courts were protecting the drafting rather than the substance, allowing the same outcome by the back door that the statute prohibited through the front.

The same logic was applied and extended in *National Insurance Co. Ltd. v. Sujir Ganesh Nayak & Co.* (1997), decided just months before the 1997 amendment came into effect. There, the Court upheld a clause providing that the insurer would not be liable for any loss or damage after the expiration of twelve months unless the claim was the subject of pending proceedings. The clause was held valid on the basis that it extinguished the insurer's contractual liability, rather than curtailing the time within which the insured could approach the courts. The right to sue, technically, remained intact. There was simply nothing left to sue for.[9]

What these cases share is a common method: classification by form rather than substance. The courts asked how the clause was worded, not what it actually did. And what it actually did, in each case, was leave one party without any meaningful legal recourse after a prescribed period, regardless of whether their claim had any merits.[10]

The difference between *FCI v. New India Assurance* and *Sujir Ganesh Nayak* is instructive in this regard. In *FCI*, the clause was framed as a condition precedent. In *Sujir Ganesh Nayak*, the clause was framed as a temporal limit on liability. Different drafting approaches, but the Court's analysis in both cases turned on the same question: does the clause restrict a remedy or extinguish a right? Neither court asked whether that question, as framed, was the right one to be asking.[11]

In practice, extinguishment clauses appeared across insurance policies, guarantees, commercial leases, and a range of other contracts. The Law Commission noted that they were typically presented on a take-it-or-leave-it basis, leaving weaker parties with no real ability to resist.[12]

Assurance'].

[9] National Insurance Co. Ltd. v. Sujir Ganesh Nayak & Co., (1997) 4 SCC 366 [hereinafter 'Sujir Ganesh Nayak'].

[10] FCI v. New India Assurance, *supra* note 8.

[11] Sujir Ganesh Nayak, *supra* note 9, at para 10.

[12] 97th Law Commission Report, *supra* note 2, at para 5.

The courts' job in each case was essentially classification: does this clause extinguish a right or bar a remedy? That inquiry was inherently unstable. Similar clauses, drafted in slightly different words, produced opposite outcomes. Courts were rewarding careful drafting rather than policing substantive fairness. The regime was analytically incoherent and practically unjust. Something had to change.

III. The 1997 Amendment and the Transformation of Section 28

The 97th Law Commission Report is unusual in Indian legal history. It was produced on the Commission's own initiative, and it said what it needed to say without much diplomatic padding. The prevailing interpretation of Section 28 was called an "anomalous situation" demanding urgent reform, and the Commission was direct about what courts had been doing.[13]

The central argument was that the distinction between limitation and prescription doesn't hold up. Limitation bars your remedy; prescription kills your right. Both leave you legally defenceless after a certain time. Allowing one while prohibiting the other doesn't reflect any principled difference in outcome. It reflects a difference in how cleverly the clause is drafted. The Commission described it as allowing parties to create a private law of prescription through contract, which it considered fundamentally inconsistent with what the Contract Act was for.[14]

The Contract (Amendment) Act, 1997 gave these recommendations legislative force. The new clause (b) declared void any agreement extinguishing the rights of any party, or discharging any party from liability, under or in respect of any contract, upon the expiry of a specified period so as to restrict any party from enforcing his rights.[15]

The intent was straightforward: close the loophole, abolish the rights-versus-remedies distinction, and bring contractual practice in line with the provision's protective purpose. On its own terms, as a correction to the pre-1997 position, the amendment worked.

But it was a horizontal reform, applied to all contracts, without distinguishing between contexts where extinguishment clauses were tools of exploitation and contexts where they served a legitimate commercial purpose. Bank guarantees sat firmly in the second category.

[13] 97th Law Commission Report, *supra* note 2.
[14] 97th Law Commission Report, *supra* note 2, at para 6.
[15] Indian Contract Act, 1872, § 28(b) (inserted by Contract (Amendment) Act, 1997).

Banks don't insist on time limits in guarantees to take advantage of beneficiaries. They insist on them because a guarantee is a contingent liability that has to close out at some point. Open-ended exposure creates real capital management problems. In contracts with government entities, where limitation could run to thirty years under the Limitation Act, that exposure was very real.[16]

The 1997 amendment had effectively invalidated the mechanism that gave bank guarantees their commercial functionality. The reform was right about the problem it was solving. It was just broader than the problem warranted.

IV. Bank Guarantees and the 2013 Legislative Carve-Out: Exception 3 to Section 28

The problems created by the 1997 amendment in the banking sector weren't theoretical. Banks couldn't secure legal closure on guarantees that had long expired commercially. They couldn't release collateral. They were carrying liabilities that the underlying transactions no longer justified. The mismatch between commercial practice and legal position was real and accumulating.

Bank guarantees have a specific character in commercial law. They're autonomous instruments, meaning the bank's obligation to pay is independent of disputes between the principal debtor and the beneficiary. The beneficiary isn't supposed to have to prove loss or argue causation. The bank pays; it sorts things out with its customer separately. That independence is the whole point of the instrument. But it only functions if there's temporal finality. A guarantee that never definitively closes isn't really a guarantee. It's a permanent contingent liability.[17]

Parliament's response was the Banking Laws (Amendment) Act, 2012, which inserted Exception 3 to Section 28 on the recommendations of the T.R. Andhyarujina Committee. The exception validated extinguishment clauses in bank guarantees, but subject to a floor: the stipulated period had to be not less than one year from the occurrence or non-occurrence of a specified event. The structure reflects a compromise: banks get commercial finality,

[16] Limitation Act, 1963, Article 55 (three-year limitation for suits on contract); Article 112 (thirty-year limitation for suits by government).

[17] Banking Laws (Amendment) Act, 2012 (No. 4 of 2013) (eff. Feb. 18, 2013).

beneficiaries get a minimum protected window.[18]

That's a sensible balance in the abstract. But the drafting introduced new ambiguity. Exception 3 speaks of extinguishment of rights or discharge of liability without specifying which temporal stage it's concerned with. A bank guarantee typically operates across three stages: validity period, claim period, and enforcement period. Exception 3 doesn't map explicitly onto that structure.

The Indian Banks' Association read Exception 3 as mandating a minimum one-year claim period, and circulated opinions to that effect in February 2017 and December 2018, recommending that member banks issue every guarantee with a minimum claim period of one year on top of the guarantee period. Banks including Punjab National Bank adopted this position, and began refusing to issue guarantees on any other terms.[19]

The commercial consequences were significant. A guarantee with a six-month validity period would now require an eighteen-month total commitment from the applicant, who continued to pay commission charges and maintain collateral for the full duration of the extended claim window. For large infrastructure companies like Larsen & Toubro, which issued guarantees at scale across multiple contracts, this added up to a substantial and, in their view, legally unjustified cost.

The confusion was compounded by an observation made by the Supreme Court in *Union of India v. IndusInd Bank Ltd.* (2016). While dealing with a pre-1997 guarantee, the Court noted in passing that stipulations like the one before it would pass muster after 2013 if the specified period is not less than one year. The IBA treated this observation as authority for its position. The Delhi High Court later clarified, correctly, that the *IndusInd Bank* observation was directed at the enforcement period, not the claim period, and couldn't be stretched to support the IBA's reading of Exception 3.[20]

Whether Exception 3 was intended to regulate claim periods, enforcement periods, or both was a genuinely open question. The text didn't answer it. Industry practice had settled on one

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[18]Indian Contract Act, 1872, § 28, Exception 3 (inserted by Banking Laws (Amendment) Act, 2012). The amendment was introduced on the recommendations of the T.R. Andhyarujina Committee, constituted by the Government of India to recommend changes to the legal framework governing bank guarantees.
[19]Indian Banks' Association, Circular dated February 10, 2017 and December 5, 2018, addressed to member banks, recommending a minimum claim period of one year in bank guarantees [hereinafter 'IBA Circulars'].
[20]Union of India v. IndusInd Bank Ltd., (2016) 9 SCC 720, at para 28.

interpretation, applicants were challenging it, and the courts hadn't squarely addressed it. Something had to give.

V. Judicial Clarification by the Delhi High Court: Larsen & Toubro Ltd. v. Punjab National Bank

The *L&T v. PNB* case[21] arose directly from the banking sector's post-2013 practice. Punjab National Bank, relying on the IBA circulars, insisted that guarantees furnished by Larsen & Toubro include a minimum one-year claim period. Larsen & Toubro said Exception 3 had nothing to do with claim periods. It governed enforcement periods, and nothing else.[22]

The whole case turned on one question of statutory construction: what does Exception 3 actually regulate?

The Delhi High Court read the provision contextually. Rather than treating Exception 3 in isolation, it placed it within the full legislative and judicial history of Section 28, covering the pre-1997 position, the Law Commission's intervention, and the 1997 amendment.[23] That's the right approach for a provision embedded in such a long chain of reform.

The Court's most important contribution is its articulation of a clear tripartite framework.

The validity or expiry period is the operational life of the guarantee, the period during which default must occur for the guarantee to be triggered. This is set by contract.

The claim period is a grace period after expiry, which may or may not be included in a given guarantee, within which the beneficiary can formally demand payment for a default that occurred while the guarantee was live.

The enforcement period is the time within which the beneficiary, having made a valid claim that the bank hasn't paid, can go to court. This engages Section 28 of the Contract Act and the Limitation Act, 1963.[24]

On this framework, the Court accepted L&T's position: Exception 3 concerns the enforcement

[21]L&T v. PNB, *supra* note 4.
[22]L&T v. PNB, *supra* note 4, at para 15.
[23]L&T v. PNB, *supra* note 4, at para 18.
[24]Limitation Act, 1963, §§ 3, 55.

period, not the claim period. Both parties, notably, converged on this in their pleadings. Punjab National Bank's own counter-affidavit acknowledged that Exception 3 didn't expressly mandate a one-year claim period.[25]

The Court recorded this consensus and built its decision on it. Exception 3 doesn't require banks to insist on a one-year claim period. It doesn't invalidate guarantees with shorter claim periods. The one-year floor applies to the extinguishment of rights at the enforcement stage, which is the stage of going to court, not the contractual act of lodging a demand with the bank.[26] Advisories premised on the broader interpretation were legally unsustainable to that extent.[27]

The Court also preserved the role of statutory limitation in the enforcement domain. Even where an extinguishment clause is validly protected by Exception 3, the beneficiary's right to go to court once a claim has been validly made and refused remains governed by the Limitation Act, unless separately curtailed in a way consistent with Section 28.[28]

The resulting framework holds together. Claim periods are left to commercial negotiation. Enforcement periods are subject to statutory oversight. Exception 3 does specific, limited work in the enforcement domain. Banks get the finality they need; judicial oversight survives.

VI. Critical Analysis and Conclusion

Looking at the full arc of Section 28's development in the bank guarantee context, a clear pattern appears. Each round of reform corrects the specific problem of the round before it, without ever fully resolving the underlying tension. The pre-1997 regime prioritised drafting form over substantive fairness. The 1997 amendment fixed that but disrupted legitimate commercial practice. Exception 3 restored commercial practicality but introduced new ambiguities. The Delhi High Court resolved those ambiguities, but in a way that has vulnerabilities of its own.

On one reading, the current framework is a genuine achievement. The tripartite distinction between validity, claim, and enforcement periods gives conceptual order to an area that was previously governed by intuition and inconsistent precedent. Contractual freedom is restored

[25] L&T v. PNB, *supra* note 4, at para 22.
[26] L&T v. PNB, *supra* note 4, at para 25.
[27] L&T v. PNB, *supra* note 4, at para 28.
[28] Union of India v. IndusInd Bank Ltd., (2016) 9 SCC 720, at para 28.

for claim periods. Statutory safeguards continue to apply at the enforcement stage. Banks can structure guarantees with rational time limits, and beneficiaries retain access to courts once a valid claim has been made. That's a reasonable balance.

But the foundations of that balance deserve scrutiny.

The most striking feature of *L&T v. PNB* is that its central interpretive conclusion rests on what both parties agreed, rather than on the resolution of competing arguments. Both L&T and Punjab National Bank accepted that Exception 3 governs the enforcement period. The Court recorded this convergence and built its ratio on it.[29] There was no competing construction to adjudicate between.

That's a legitimate way to decide a case. But it means the ratio hasn't been forged in the usual way. Judicial precedent normally gets its authority from reasoned adjudication between rival positions. A consensus-driven interpretation, however persuasive internally, hasn't been stress-tested in the same way. If a future litigant argues more aggressively that the one-year minimum was intended to cover claim periods as well as enforcement periods, the Delhi High Court's construction would need to be defended on its merits rather than by reference to what the parties in *L&T v. PNB* were willing to concede. The IBA's circulars, struck down as erroneous, were themselves premised on a reading of Exception 3 that at least one sophisticated institutional actor found plausible enough to act on for several years. That reading hasn't been rebutted so much as bypassed.

This risk is compounded by the text of Exception 3 itself, which doesn't explicitly distinguish between claim and enforcement periods. Its reference to extinguishment of rights or discharge of liability is broad enough to support a wider reading.[30] The Court's contextual construction narrows that breadth, but without explicit legislative language to anchor it, the door to renewed interpretive debate isn't fully closed.

There's a further structural issue. The distinction between claim and enforcement periods, while analytically clean, means finality is achieved at the contractual level but not necessarily at the legal level. A bank guarantee can extinguish liability after a contractually stipulated period, but disputes about whether that extinguishment was valid, or whether a timely claim

[29] L&T v. PNB, *supra* note 4, at para 30.
[30] Indian Contract Act, 1872, § 28, Exception 3.

was wrongly refused, can still be litigated within the statutory limitation period. Exception 3 achieves commercial finality in a narrow sense. It doesn't eliminate legal exposure altogether.

This reflects something deeper about what Section 28, even now, is actually doing. It remains fundamentally a provision about access to courts, not a provision about commercial risk allocation. Exception 3 suspends its invalidating effect in a specific domain, but doesn't change its character. The law is still caught between its protective origins and its accommodation of commercial necessity. It has adapted to each crisis as it arrived, without resolving the underlying conflict.

The selectivity of Exception 3 also raises policy questions that haven't received enough attention. The carve-out was justified by concerns about banks and financial institutions: their capital management obligations, their commercial sophistication, their systemic role. The 97th Law Commission, by contrast, was concerned with inequality and economic justice. Exception 3 consciously departs from that.[31]

That departure may be justified. But the logic that justified it doesn't obviously stop at banks. A sophisticated infrastructure company could make a structurally similar argument for an equivalent carve-out on grounds of commercial necessity. The doctrinal logic of Exception 3 supplies no obvious answer. If the exception becomes a template for further carve-outs, the normative core of Section 28 could be eroded incrementally, each individual carve-out reasonable, the cumulative effect transformative.

There is also a dimension that the L&T v. PNB judgment touches on but doesn't fully resolve: what happens when a bank refuses to pay a validly made claim, and the beneficiary's right to approach the court is itself subject to an extinguishment clause protected by Exception 3? The framework the Court articulated treats enforcement finality as the domain of Exception 3, but the practical interaction between a contractually agreed enforcement period and the residual role of the Limitation Act remains underexplored. Future litigation will almost certainly have to address this.

None of this is an argument that the current position is bad law. Compared to the pre-1997 regime, it's substantially better, more transparent, more analytically disciplined, and less susceptible to drafting games. The rights/remedies distinction has been abandoned. The Delhi

[31] 97th Law Commission Report, *supra* note 2, at para 9.

High Court's temporal framework provides real analytical clarity.

But the evolution of Section 28 is best understood as an ongoing dialogue between legislature and judiciary, not as a story moving toward a settled destination. Each intervention responds to specific problems revealed by practice. Each settlement creates new questions.

The present legal position on bank guarantee periods is carefully balanced, but contingent. Exception 3 and its judicial interpretation have restored commercial functionality to an important class of financial instrument. They've done so, though, on interpretive foundations that remain open to challenge, and through a selective legislative intervention that leaves larger questions about Section 28's future unanswered.

The clarity the Delhi High Court achieved is real and valuable. Whether it endures depends on how courts respond to future challenges, and on whether the legislature is willing to provide more explicit guidance before the next crisis forces its hand. The story of Section 28 isn't one of problems permanently solved. It's one of problems managed, and that distinction matters for anyone trying to understand where the law actually stands.