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Why Standard Project Finance Safeguards Do Not Disqualify Debenture Holders from the Committee of Creditors

<p>The intersection of structured finance and insolvency law continues to generate significant judicial discourse, particularly on the question of when a financial creditor ceases to be a mere lender and becomes a related party of the corporate debtor. A recent ruling by the National Company Law Tribunal, New Delhi Bench, in Rishi Gupta and Anr. […]</p>

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PUBLISHED 5 August 2026

The intersection of structured finance and insolvency law continues to generate significant judicial discourse, particularly on the question of when a financial creditor ceases to be a mere lender and becomes a **related party** of the corporate debtor. A recent ruling by the National Company Law Tribunal, New Delhi Bench, in **Rishi Gupta and Anr. v. IDBI Trusteeship Services Ltd. and Ors.** offers important clarity on this issue.

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Case Overview and Bench Details

Decided on 10 July 2026 by a Bench comprising Shri Mahendra Khandelwal and Shri Atul Chaturvedi, the order addresses the delicate balance between **lender protection mechanisms** and the statutory disqualification imposed by Section 21(2) of the Insolvency and Bankruptcy Code, 2016.

The case arose from the corporate insolvency resolution process initiated against Shree Vardhman Buildprop Private Limited, a real estate developer that had raised funds through two separate tranches of non-convertible debentures to complete its residential project in Gurugram.

The ex-directors of the corporate debtor sought the removal of the debenture holders from the **Committee of Creditors**, arguing that the extensive rights and controls exercised by the lenders under the debenture trust deeds effectively made them related parties under Section 5(24) of the Code.

Background: Structured Real Estate Financing and Debenture Issuance

The factual matrix of the case was rooted in a fairly typical **structured real estate financing arrangement**. The corporate debtor had issued debentures to the financial creditors, with IDBI Trusteeship Services acting as the security trustee.

The financing documents created a comprehensive framework of lender protections:

- Escrow accounts for project revenues and fund use
- Sole signatory rights granted to the security trustee over those accounts
- Reserved matters requiring lender approval for specified corporate actions
- Broad inspection and monitoring rights over the project, its accounts, and its records

Following defaults in repayment, the debt was restructured through a **second debenture trust deed** in 2021, which maintained similar protective covenants.

The applicants, who were the suspended directors of the corporate debtor, contended that these arrangements were not merely security measures but evidence of *pervasive control*. They pointed to WhatsApp communications, cheque collections, and the involvement of lender representatives in sales activities as proof that the financial creditors had effectively assumed the role of co-promoters.

This, they argued, disqualified the financial creditors from participating in the Committee of Creditors.

Applicants' Arguments: Pervasive Control by Lenders

The tribunal was called upon to determine whether the rights and controls retained by the debenture holders under the trust deeds amounted to **management or policy control** within the meaning of Section 5(24) of the IBC.

The applicants argued that the constitution of the Committee of Creditors was the very foundation of the insolvency resolution process. Any statutory violation in its composition, they submitted, could be raised by any stakeholder, including suspended directors.

They emphasized that the **second proviso to Section 21(2)**, which protects financial creditors who become related parties solely on account of debt-to-equity conversion, did not apply to their case.

Respondents' Defence: Standard Protective Covenants

The respondents, on the other hand, maintained that the suspended directors lacked **locus standi** to challenge the Committee of Creditors. They also argued that the issue was barred by res judicata.

On the merits, the respondents contended that the contractual rights in question were **standard protective covenants** in project finance transactions that did not equate to management control.

Tribunal's Ruling on Locus Standi and Res Judicata

The tribunal first addressed the question of locus standi. It held that **suspended directors**, despite the suspension of their powers under Section 17 of the IBC, do not cease to be participants in the insolvency process.

Since the applicants were challenging the legality of the Committee of Creditors' constitution rather than its commercial wisdom, their objection was held to be maintainable.

The tribunal also rejected the plea of **res judicata**. It observed that a challenge to the composition of the Committee of Creditors arises only after the commencement of the corporate insolvency resolution process and the actual constitution of the Committee.

It could not have been adjudicated at the admission stage of the Section 7 petition or in an appeal against the admission order.

Substantive Analysis: Related Party Status Under Section 5(24)

Purpose of Escrow Mechanisms and Reserved Matters

Turning to the substantive question of related party status, the tribunal conducted a careful examination of the debenture subscription agreement and the trust deeds. It observed that the **escrow mechanisms**, reserved matters, and inspection rights were primarily intended to:

- Safeguard the use of funds advanced by the financial creditors
- Ensure completion of the financed project
- Monitor project revenues
- Prevent diversion of funds

The tribunal noted that such stipulations are commonplace in **structured project finance transactions**, particularly in the real estate sector where lenders routinely insist upon escrow arrangements, monitoring mechanisms, reporting obligations, and approval requirements for specified financial transactions.

The existence of these mechanisms, by themselves, could not establish management control over the corporate debtor.

Day-to-Day Management Remained With the Corporate Debtor

The tribunal further emphasized that the transaction documents indicated that the **day-to-day execution of the project**, the operation of the Project Operating Account, construction activities, and the management of the corporate debtor's affairs continued to remain with the management of the corporate debtor.

The Project Operating Account, through which actual project expenses were incurred, remained under the control of the corporate debtor's management. The requirement of lender approvals for transfer or use of funds was characterized as a **commercially negotiated safeguard** intended to protect the lenders' financial exposure rather than an assumption of management or policy control.

The tribunal cautioned that if every lender insisting upon affirmative covenants, reporting obligations, escrow controls, and approval rights were to be treated as exercising management control, *virtually every secured project finance lender* would become disentitled from participating in the Committee of Creditors. This would be wholly inconsistent with the scheme and object of the IBC.

Examination of WhatsApp Communications and Documentary Evidence

The tribunal also examined the evidence relied upon by the applicants, including WhatsApp communications and copies of cheques. It held that even if taken at face value, these merely indicated **monitoring of project implementation** and customer collections.

They did not establish that the financial creditors assumed control over the management, policy decisions, or corporate governance of the corporate debtor.

Significantly, no material was placed before the tribunal demonstrating that the financial creditors possessed the power to:

- Appoint or remove directors
- Dictate the composition of the board
- Determine business policy
- Otherwise substitute themselves for the management of the corporate debtor

The tribunal found that the applicants had neither produced the amended articles of association demonstrating that the lenders acquired the right to appoint or remove directors, nor established that the lenders supplanted the **board of directors** in managing the corporate debtor.

Role of the Resolution Professional

The tribunal also considered the role of the **resolution professional**, who had stated that the claims submitted by the financial creditors were duly verified together with declarations regarding their status as unrelated financial creditors before their admission into the Committee of Creditors.

In the absence of cogent material establishing that the statutory ingredients of Section 5(24) were satisfied, the tribunal found no fault with the resolution professional's decision to admit their claims and constitute the Committee of Creditors.

The tribunal concluded that the contractual rights relied upon by the applicants remained **protective in nature** and did not render the financial creditors related parties of the corporate debtor.

Outcome: Application Dismissed

The judgment ultimately reinforces the principle that the existence of **contractual approval rights** over specified transactions cannot automatically be equated with the control contemplated under Section 5(24) of the IBC.

The tribunal's analysis underscores the need to distinguish between genuine management control and commercially negotiated safeguards designed to protect a lender's security interest.

By holding that the applicants had failed to establish that the financial creditors exercised **pervasive management or policy control**, the tribunal upheld the constitution of the Committee of Creditors and the participation of the debenture holders therein.

The application was dismissed as devoid of merit, with no order as to costs.

Implications for Structured Finance and Real Estate Lending

This ruling carries significant implications for the Indian structured finance and real estate sectors. It provides **judicial comfort to secured lenders** that standard protective covenants – including escrow controls, reserved matters, and monitoring rights – will not be lightly construed as management control that disqualifies them from the insolvency resolution process.

Key takeaways from the judgment include:

- The burden of proving related party status under Section 5(24) remains a high threshold, requiring evidence of *actual control* over the corporate debtor's management and policy decisions rather than mere contractual oversight of fund use.
- Standard protective covenants in project finance – escrow controls, reserved matters, and monitoring rights – do not by themselves amount to management control.

- Suspended directors retain the ability to raise jurisdictional challenges regarding the constitution of the Committee of Creditors, even though their operational powers stand suspended during the insolvency process.

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