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Structuring the answer: the Cayman Islands' response to private credit

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1. Market update

Private credit has crossed from an alternative allocation into a structural component of the credit system. The Alternative Credit Council, whose annual *Financing the Economy* series remains the most cited survey in the industry, records the global market at approximately US$3.5 trillion in assets under management, with US$592.8 billion of capital deployed at the end of 2024, an increase of 78 per cent from the previous year.[1] Growth comes from three directions. Banks are shedding exposure under Basel capital rules and through significant risk transfer,[2] insurers want long-dated yield and borrowers face a refinancing wall in leveraged finance and real estate while artificial intelligence, defence and the energy transition compete with sovereign issuance for a pool of savings that is no longer abundant.[3]

The composition of growth has changed in the last few years. Direct lending is no longer the fastest-expanding part of the market. Asset-based finance leads now, secured against pools that run from equipment leases to music royalties and sports franchises. Hybrid capital has found its market among sponsors facing compressed exits, blending contractual cash flows with equity upside. Credit secondaries and distressed strategies are raising record capital into the cycle. Whole sectors are being financed that nobody was financing five years ago, among them data centre securitisation, defence and litigation funding.

Documentation is becoming more standardised as the market grows. The Loan Syndications and Trading Association published its first model terms for direct lending in final form on 21 July 2026, fixing the boilerplate of senior secured facilities while leaving covenants and baskets, where the underwriting is done, to negotiation.[4]

Some of this is meeting resistance. Direct lending now matches the broadly syndicated loan market in size and where the two compete the syndicated market sets the price and drags direct lending spreads down with it. The illiquidity premium has nonetheless held at 150 to 250 basis points, against the 100 to 150 common before 2018.[5] It is claimed that the liquidity that premium is meant to compensate for has not improved and PIMCO concludes that investors in corporate private credit are often not paid for the illiquidity they accept, doubting too that the premium can be recovered by engineering a secondary market.[6] Private credit loans transfer only with the borrower's consent and that consent, or the absence of it, governs both how the loans move and how a financier takes security over them. G7 bond yields rose sharply through 2026,[7] and for a floating-rate asset class higher base rates compress interest coverage without any change in credit quality, while payment-in-kind features absorb the difference and postpone its appearance.[8] Fitch reports a trailing 12-month default rate of 6 per cent, the highest in its measurement history.[9]

2. Regulatory update

The systemic question

In June 2024, the Federal Reserve Bank of New York reported that the growth of non-bank financial institutions (**NBFIs**) depends on banks for funding and liquidity support[10] and concluded that the activities and risks of the two are therefore interwoven.[11] The nexus that results, on that reading, carries systemic risk in both directions.[12]

The Alternative Credit Council answered[13] that bank lending to funds transfers risk instead of creating it, because the bank takes the senior position and fund equity absorbs the first loss. The Federal Reserve's June 2025 exploratory analysis supported that reading, finding that bank exposures to NBFIs carry no systemic threat even under a severe recession.[14] The position has since changed. In January 2026, the House of Lords Financial Services Regulation Committee (the **Committee**) found the evidence insufficient to say whether private credit is systemic, having been unable to obtain detailed data on the scale of bank interconnection with private markets.[15] It did not call the market dangerous, only unmeasured.

The current criticism

In its April 2024 assessment, the International Monetary Fund (**IMF**) identified five vulnerabilities, namely fragile borrowers, liquidity mismatch in semi-liquid vehicles, layered leverage, valuation opacity and deepening interconnection.[16]

Interconnection dominates the literature. The word is used in three separate senses and the writing rarely distinguishes between them.

The first is bank funding of funds. Banks have moved within the field instead of leaving it, shifting from principal lender towards wholesale funder and partner, originating and distributing, co-lending and financing the funds that lend. The Financial Stability Board (**FSB**) captures around US$220 billion of drawn and undrawn bank credit lines to private credit funds, with further indirect exposure through revolving facilities to companies that are also borrowing from those funds and through synthetic risk transfer.[17] Apollo's lending programme with Citi, and its arrangement with JPMorgan and Goldman Sachs to trade its investment-grade paper, show a relationship that is competitive and cooperative at the same time.[18]

The second channel runs through insurance and it is the one supervisors return to most often. Long-dated private credit and asset-backed exposure migrates onto life and annuity balance sheets through rated note feeders (**RNFs**) and collateralised fund obligations (**CFOs**). Fitch put United States insurers' holdings of privately rated securities at around US$350 billion at the end of 2023, roughly 7 per cent of their total bond holdings and up from US$300 billion a year earlier.[19]

The third is the web of strategic partnerships and cross-holdings binding managers, banks, insurers and private equity sponsors together, which follows neither of the other two lines cleanly and is the hardest of the three to measure.

Valuation is the second concern and the market produced its own illustration of it. In late 2025, Blue Owl abandoned the merger of a non-traded vehicle into its listed business development company. The portfolios overlapped by some 98 per cent, yet the listed vehicle traded at roughly a 20 per cent discount to the net asset value at which the merger was to be struck,[20] which is the distance between a reported net asset value and the price a buyer will actually pay.

The regulatory turn across the principal markets

The United States, the United Kingdom, the European Union and the Gulf have each answered in a different register and each reaches Cayman Islands structures by a different route.

Washington has taken two positions at once. Executive Order 14330 of August 2025[21] and the Department of Labor's subsequent proposed rule[22] opened defined-contribution capital to private credit, conditioned on liquidity and reliable valuation, and both conditions fall to be satisfied in the fund's constitutional documents and not in the underlying loan. The Chairman of the Securities and Exchange Commission[23] and the Treasury Secretary have each said that private credit poses no systemic problem,[24] while the Federal Reserve has asked banks for detailed data on their exposure to private credit firms and insurers.[25]

The United Kingdom is testing before it legislates. The Bank of England launched a system-wide exploratory scenario on private markets in December 2025 and in June 2026 sent participants a severe five-year global recession scenario, with a final report due in early 2027.[26] The Committee has asked the Bank to assess valuation accuracy and the link between insurance and banking.[27]

Brussels has moved in two directions at once. The Alternative Investment Fund Managers Directive 2.0 (**AIFMD 2.0**), effective 16 April 2026, imposes leverage caps, risk retention and concentration limits, a standardised liquidity-management toolkit and enhanced reporting on loan-originating funds.[28] One layer down, at securitisation, the movement is the other way. Amendments to the Securitisation Regulation expected around June 2027 would release third-country issuers, Cayman Islands collateralised loan obligations, and rated note vehicles among them, from the prescribed European disclosure templates, leaving the European investor to satisfy itself that what it receives is substantially equivalent.[29]

The Gulf regulates private credit to attract it. The Dubai Financial Services Authority introduced a credit fund regime in June 2022, the Abu Dhabi Global Market's regulator issued Private Credit Fund Rules in May 2023[30] and it consulted in November 2025 on whether that framework remains fit for purpose.[31] Both set limits on fund borrowing, but the systemic-risk anxiety driving the other three regimes is absent. For a Cayman Islands vehicle, the Gulf matters less as a regulator than as a source of capital, supplied as investor and, increasingly, as lender.

Fund design cannot answer all of this. Borrower quality, underwriting standards and the aggregation of exposures across the system lie beyond it and Cayman Islands structures touch them only at the margins. Liquidity mismatch, valuation, the containment of loss and leverage, together with the bank and insurance channels, are another matter and that is where fund and financing structures matter most.

3. Cayman Islands structural solutions

Capital wants liquidity and supervisors want that liquidity evidenced. The reconciliation happens in the structure and the case made here for the Cayman Islands is a functional one. It rests on the breadth of the vehicle types available, the depth of the structured-credit technology built around them and a sophisticated common law that favours creditors. Together, these answer several of the criticisms set out above, though not all of them. The market has made its own assessment and it is visible in the registration figures; 31,145 regulated funds at the end of the second quarter of 2026, of which 18,132 are private funds.[32]

Closed-ended and open-ended funds

Closed-ended structures commit capital, draw it down over time and distribute as assets are realised. The Cayman Islands exempted limited partnership, with its seven-to-10-year term and contractual freedom over waterfalls, recycling and successor-fund mechanics, remains the most popular vehicle for a credit strategy. It also draws the least of the liquidity concern, since capital locked up for the life of the fund performs little maturity transformation. What it leaves unanswered is the investor who wants interim access or to rebalance a portfolio.

Open-ended funds answer that by dealing at net asset value, with gates, lock-ups and slow payout mechanics matched to the underlying assets. Applied to private credit, the model carries the mismatch the official sector has identified. Investors can exit at a net asset value struck on assets that do not trade

and cannot be sold quickly, so a wrong mark prices every subscription and every redemption wrongly and value moves between the investors who leave and the investors who stay. This needs structuring.

Evergreen and hybrid structures

Evergreen and hybrid vehicles blend open- and closed-ended features with periodic liquidity and they are the ones that draw supervisory concern. They are also where Cayman Islands structuring has most to offer. The toolkit is a familiar one: lock-ups; gates at investor and fund level; redemption windows and notice periods; slow-pay and holdback mechanics; side pockets; and in-kind or run-off classes, each matched to the asset-liability profile of the book. After the Financial Conduct Authority's liquidity work and the mandated toolkit in AIFMD 2.0, these are the features a supervisor will ask to see, and Cayman Islands vehicles have been operating them for decades. None of it works any better than the discretion behind it. Under Cayman Islands law, a board that gates, or lifts a gate, must act in good faith and for a proper purpose.

Valuation is answered in the same place. Rules made by the Monetary Authority under the Private Funds Act and the Mutual Funds Act already fix what a net asset value must be, requiring it to be calculated or verified independently and audited regularly.

The segregated portfolio company (SPC) and statutory ring-fencing

Managers running multiple strategies within a single legal entity commonly use the Cayman Islands SPC, which suits multi-strategy and ring-fenced pools. A single exempted company creates portfolios whose assets and liabilities are separate by statute and not by contract. A creditor of one portfolio has recourse first to that portfolio's assets, then, unless the articles of association prohibit it, to the general assets of the company only so far as those general assets exceed any minimum capital a Cayman Islands regulator requires.[33] A liquidation must give effect to the segregation notwithstanding any statutory provision or rule of law to the contrary.[34] Compare a multi-class umbrella fund, where segregation is internal and contractual and collapses on a winding up; that difference is the reason managers choose the structure and it answers a narrower version of the contagion question than the one in section 2 above. Risk still moves between institutions, it does not move between the strategies of a single manager who has segregated them by statute.

All of that holds where Cayman Islands law is the law being applied. The boundaries of the statute are where the risks sit and there are two of them. Segregation is a creature of Cayman Islands law with no automatic effect abroad and a court administering a foreign insolvency may apply its own collective rules to assets within reach, so cross-border transactions should carry limited recourse and non-petition wording that replicates the statutory result in every relevant forum.[35] The second boundary is the host entity itself. A portfolio has no separate legal personality, so it cannot contract or sue in its own name and every act intended to bind it must be executed by the company in the name of that portfolio.[36]

Special purpose vehicles (SPVs), private structured credit (PSC) and trust structures

Beneath the fund sits the orphan SPV. A Cayman Islands exempted company whose shares are held by a professional trustee under a charitable or STAR trust has no beneficial owner connected to the originator or manager, cannot be consolidated and isolates the assets it holds from every credit risk but their own. The bankruptcy remoteness of a Cayman Islands orphan SPV rests on settled law and long practice. Issuing SPVs are frequently incorporated as SPCs, which lets several tranches or risk-transfer trades run through a single issuer with each pool separately ring-fenced. PSC is built on that framework. Tranched notes issued by such vehicle and listed on the Cayman Islands Stock Exchange qualify for the United Kingdom Eurobond exemption, which preserves gross interest to international noteholders.[37] The structured note is the central instrument, shaped around the risk-return preferences of institutional investors. RNFs and CFOs are built on the same vehicles.

Tokenised funds

On 24 March 2026, the Cayman Islands brought into force a dedicated framework for tokenised investment funds. They are regulated inside the existing Mutual Funds and Private Funds regimes instead of as virtual-asset service providers, with tailored record-keeping and inspection powers for the Monetary Authority.[38] Tokenisation changes how an interest is recorded and how it is transferred. It leaves untouched what the interest is worth and how quickly the underlying loan can be sold. For a manager facing retail demand, it offers fractional ownership and distribution without stepping outside the supervisory perimeter the fund already sits in.

4. Fund finance solutions

Interconnectedness with banks

Banks lend to private credit funds against uncalled commitments, against the loan book and against both at once. A fund of any size will be running several such facilities in parallel. The supervisory literature treats them as a single exposure. The IMF's October 2025 stress test assumes bank credit and liquidity facilities to non-banks are drawn down by as much as 100 per cent at the same moment,[39] which is a defensible way to size a bank's liquidity need and a poor way to describe what the bank is holding. Drawn and lost are not the same number.

Collateral is the dividing line. A subscription facility is secured on investors' unfunded commitments and on the lender's right to call and enforce them, so it rests on a contractual obligation to pay and not on a valuation. A fall in portfolio values leaves it untouched. Net asset value loans, warehouse lines, back leverage and repurchase facilities are secured on the portfolio itself, so valuation pressure and borrowing base pressure arrive together, as detailed below. Hybrids sit between the two and carry a fund from commitments to assets as it invests. There is a limit to the resilience of the subscription facility. Calling capital in a stressed market is where the IMF's assumption has force. A simultaneous full drawdown of subscription lines is a simultaneous capital call and the pressure moves onto the pension funds and insurers whose uncalled commitments the IMF counts as an exposure of their own.[40]

All of it depends on the enforceability of the security, which for most of these funds is a question of Cayman Islands law and the analysis is the same whether the lender is a bank or, increasingly, another private credit fund. The questions arise well before enforcement.

In an exempted limited partnership, the right to call capital vests in the general partner and is frequently delegated to the manager, so a security package reaching only the general partner's right may reach nothing that will be exercised. In an exempted company, the right vests in the company and the further question is how the uncalled commitment is recorded and whether anything could impede an issue of shares when a call is made. A limited liability company leaves it with the manager unless it has been delegated. Diligence then runs in the same order, asking whether the constitutional document permits borrowing and security over the call right itself and not merely its proceeds, whether a lender may exercise the call in the general partner's place and whether investors have kept rights of set-off or, in the case of sovereign and public pension investors, immunity. A negative answer rarely defeats a transaction, though it usually moves the advance rate or the exclusions once the economics have been agreed.

Security at portfolio level begins with the transfer restrictions in the underlying loan documents. A credit fund rarely holds its loans directly and a credit agreement requiring consent to assignment can leave a lender with no way to take the assets themselves. The usual structural answer is an asset-holding SPV, sometimes a double SPV, with the borrowing secured over its shares. The initial transfer into that vehicle tends to be permitted as a transfer to an affiliate and enforcing share security afterwards moves the company and not the loans. Where the shares cannot be secured, or alongside it, the lender takes security

over the fund's right to distributions and the accounts they are paid into, which reaches the cash without touching title. Whether the fund may grant any of it turns to the constitutional documents.

Gulf capital adds a layer to all of this. Where the limited partner or the lender is a Gulf institution, the facility must be capable of *Shari'ah*-compliant execution, most often through commodity *murabaha* or *wakala* in place of an interest-bearing advance. The Cayman Islands vehicle is indifferent to the choice, and the security and enforcement analysis does not change.[41]

Interconnectedness with insurers

Insurers reach private credit as investors and they usually buy notes instead of fund interests, because of how the two are treated for regulatory capital.

A Cayman Islands RNF issues tranches of notes, and sometimes equity, to its investors and invests in a master fund or a pool of interests. The insurance investor's capital treatment depends on those notes being debt, with interest paid in kind until distributions arrive. The CFO does the same for a pool of fund interests, with the assets moving to an asset-holding vehicle and the notes issued by another. The second vehicle is there because transferring a Cayman Islands law governed fund interest generally needs general partner consent, even where only the right to distributions is assigned, and making the asset holder an affiliate of the sponsor brings the transfer inside permissions the fund documents already contain. The issuer is orphaned and bankruptcy-remote, so noteholders and the rating agency look to defined cash flows and not to an operating balance sheet. Capital calls and recallable distributions need express treatment, since no standard partnership agreement contemplates recycling payments out to noteholders.

Whether those notes are debt has become a harder question. The bond definition applied by United States insurance regulators asks whether an instrument has the economic characteristics of a bond.[42] There is a fund finance question too. If the notes are debt, the investors holding them are creditors of the feeder. A subscription lender then needs to know whether its claim on called capital ranks behind them. The point is better settled at formation, in the constitutional documents. Subordination agreed after commitments are drawn depends on the consent of the investors whose ranking is being surrendered. Consent of that kind is rarely available at a price the transaction can bear.

Valuation and the borrowing base covenant

Private credit portfolios are marked by one of two methods. A discounted cash flow model takes expected cash flows across the holding period and discounts them at a chosen rate. The alternative model benchmarks the position against leveraged loan indices or the high yield market as a proxy for comparable credits. The first carries the manager's own assumptions with it, since both the projections and the discount rate are the manager's.[43] In a Cayman Islands fund, the mark has to, in any event, meet the statutory valuation requirements described above, independently calculated or verified and audited.

A financed portfolio is marked again, by the lender, on terms set in the facility agreement and not in the valuation policy. Eligibility criteria admit an asset to the borrowing base only if it meets tests such as senior secured status, a minimum credit estimate and the capacity to be assigned to the facility agent and to a purchaser on enforcement. A loan on non-accrual, in covenant breach, in arrears or carrying an exercised payment-in-kind toggle may drop out at the next determination date. Eligible value is taken at the lower of par and the agreed mark, multiplied by an advance rate driven by the credit estimate, less concentration excess and reserves. A loan-to-value covenant is tested against that number on each determination date. A deficiency has to be cured, by prepayment, by posting collateral, or by contributing assets funded from a capital call. Failing that, distributions and drawings stop and the deficiency matures into an event of default, at which point the enforcement analysis set out above applies.

The same loan is therefore valued twice, once by the manager and once by a counterparty with money at stake if the number is wrong. The supervisory literature treats the two processes separately.

The second valuation is less independent than it appears. The lender starts from the manager's figure instead of producing a value of its own, so an inflated mark produces an inflated borrowing base and leaves the lender well secured against the wrong number. The advance rate turns on a credit estimate and credit estimates are private ratings, some of them from the smaller agencies whose reliability supervisors have themselves questioned, so the lender's number depends on the same class of input as the manager's.[44]

The Cayman Islands legal architecture

Security over a credit fund's loan book runs over receivables, contract rights and the accounts into which collections are paid, which makes it an assignment of choses in action. A legal assignment needs an absolute written transfer, not expressed as a charge, with written notice to the underlying obligors. Most security takes effect in equity. Notice fixes priority against competing assignees under the rule in *Dearle v Hall*.[45]

The two vehicles keep different registers. An exempted company keeps a register of mortgages and charges at its registered office, but failure to enter a charge attracts a penalty and not invalidity, no time limit applies and inspection in practice requires consent.[46] The result is a company record with none of the qualities of a public registry. The register of security interests kept by the general partner of an exempted limited partnership is open to any person during usual business hours and security over a partnership interest must be noted there once valid notice is received.[47] It tells a subscription lender whether an investor has charged the commitment it is lending against. Security the partnership has itself granted over its loan book or its call rights is a different matter. Where the general partner is a Cayman Islands company, that charge belongs in its own register of mortgages and charges, which is the private record described above.

Priority depends on timing and on the form the security takes. A fixed interest ranks ahead of a later floating charge absent notice of a negative pledge, fixed charges rank by date of creation, and security over choses in action and over a partnership interest ranks by the date notice was given.[48] Contractual subordination is recognised on a liquidation by statute, deeds of priority govern ranking between secured creditors. Non-petition and limited recourse provisions hold.[49] There is no general doctrine of substantive consolidation. Separate legal personality is disregarded only in the narrow circumstances identified in *Prest*.[50]

Layering matters only where it is unintended, since tranched structures put the bank's claim ahead of the junior lender's by design. The difficulty arises where the loans sit in a subsidiary that has borrowed on its own account without the fund-level lender pricing for it. The asset-level lender then ranks ahead. Enforcing the fund-level security triggers a change of control that the asset-level facility almost certainly prohibits, so enforcement accelerates the debt ranking ahead of it. The remedy belongs in the articles of the asset-holding company at incorporation, restricting transfer of the secured shares, removing the directors' discretion to refuse registration on enforcement, disapplying the company's lien and requiring the lender's consent to any amendment. A limited partnership interest has no equivalent remedy, because creating and enforcing the security will each usually constitute a transfer requiring the general partner's consent. The transferee takes the obligations attached to the partnership interest together with the rights.

5. Conclusion and the next 12 months

Part of the remedy is integration, and the market is already supplying it. The leading practices have drawn fund formation, private credit and fund finance into single groups, so the same advisers design the structure, the vehicle, the financing and the security package. A fund built that way has liquidity terms, valuation governance and leverage that fit one another instead of being reconciled after the event. None of that settles whether private credit is systemic. This question will be answered by the aggregation the FSB has recommended, the exposure data the Federal Reserve has requested and the Bank of England's exploratory scenario, not by fund architecture.

This premise is also the reason to be cautious about the most prescriptive regulatory responses. A framework dictating the mechanics of every loan-originating fund may reduce visible variance, but it does so at a cost to the product's capacity to finance the parts of the economy banks now reach less readily. Private credit has given borrowers a flexible source of capital and has given investors a return that correlates differently with public markets and it has done so on modest fund-level leverage with the greater part of its capital locked up. Better structuring, honest valuation, evidenced liquidity and integrated advice are a proportionate answer to the present moment and Cayman Islands law supplies the statutory requirements against which the first three can be tested.

Four things are worth watching over the coming 12 months. The Bank of England will publish the findings of its private markets exploratory scenario across 2026 and into 2027. The centre of gravity is likely to be valuation and redemption mechanics rather than leverage. The Department of Labor's rule moves towards finalisation, opening defined-contribution capital on conditions of liquidity and valuation discipline. AIFMD 2.0's loan-origination provisions, transposed from 16 April 2026, will raise onshore valuation standards, as will the forthcoming International Organization of Securities Commissions valuation recommendations, bringing those standards closer to the statutory requirements Cayman Islands funds already meet.[51] Asset-based finance is likely to continue leading product growth, carrying the rated-note and CFO structures with it.

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47 Exempted Limited Partnership Act (2026 Revision), section 31.

48 Exempted Limited Partnership Act (2026 Revision), sections 31(4) and 32(9).

49 Companies Act (2025 Revision), section 140(2).

50 *Prest v Petrodel Resources Ltd* [2013] UKSC 34.

51 AIMA, "Loan origination funds: from AIFMD II to Luxembourg's bill 8628" (November 2025), https://www.aima.org/article/loan-origination-funds-from-aifmd-ii-to-luxembourg-s-bill-of-law-8628.html



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Agnes Molnar is a partner at Collas Crill in the Cayman Islands, where she leads the firm's fund finance and private credit offering. She is admitted in the Cayman Islands, England and Wales and Hungary, and has more than 20 years of experience in financing private capital.

She advises sponsors, asset managers and their financiers on private capital liquidity solutions across the entire lifecycle of a fund, bringing fund finance, private credit and structured private credit together as an integrated approach to private capital.

At formation, Agnes structures the Cayman Islands vehicles that later borrow, invest and issue, including exempted limited partnerships, exempted companies, segregated portfolio companies, rated note feeders, co-investment vehicles and the SPVs. During the investment period, she advises on subscription facilities. As portfolios mature, her work extends to NAV and hybrid facilities, asset-based finance, preferred equity and GP financing. In the later life of a fund, she advises on the financing of secondaries and continuation vehicles, collateralised fund obligations and management fee, capital call and other portfolio cash flow securitisations. Her work extents to loan-on-loan portfolio financings and *Shari'ah*-compliant structures.

She acts for both sponsors and lenders across the United States, the United Kingdom, Europe and the Middle East, with Cayman Islands structuring at the centre of her work, including the regulatory perimeter that now attends private credit vehicles registered there. Agnes has spent seven years as a partner in the Cayman Islands, following 15 years in London, Vienna and Budapest at leading international law firms and in-house at a global financial institution.

Agnes is an International Fellow of the American College of Commercial Finance Lawyers and has spoken before the American Bar Association's Fund Finance Subcommittee on capital call securitisation. She has been ranked in *Chambers and Partners* for banking and finance and was named a Rising Star for fund finance in *The Legal 500 2019*. She writes regularly on fund finance and private credit, including chapters for *Global Legal Insights*.

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