Proskauer

Risk #1: Private Credit under the Microscope – Why Vigilance Matters

The Capital Commitment on **March 24, 2026**

Private credit has spent a decade rising from niche alternative to central pillar in global finance. It has become a multi-trillion-dollar engine of corporate lending, infrastructure finance, asset-based credit, specialty finance, and opportunistic capital. While financial regulators have so far taken a relatively hands-off approach, elements of the market and the financial press have raised concerns about longer-term risks arising from the growth in private credit.

Common concerns stem from, among other things, valuation and liquidity risks, rising use of payment-in-kind (PIK) interest as evidence of weakening loan quality, an increasing number of lenders taking over private companies, new products and the increasing involvement of retail investors, increasing use of leverage, and interconnections with banks. Exacerbating these concerns is a perceived lack of regulatory transparency into the private credit markets.

A balanced look at recent events suggests neither crisis nor complacency is justified. Instead, private credit managers must realize that rising sentiment – whether justified or not – calls for vigilance and discipline.

Regulatory Approaches: UK Leads, US Evolves

While regulators on both sides of the Atlantic are converging on concerns that opacity in the private credit markets may amplify stress in a downturn, their approaches are diverging. UK regulators are taking a more proactive stance: the Bank of England (“BOE”) is now conducting system-wide stress tests of private equity and private credit to evaluate how economic shocks could cascade through leverage, valuation practices, and funding relationships, placing the UK at the forefront of integrating private markets into systemic risk surveillance. Major US private credit/alternative asset managers have reportedly agreed to voluntarily participate in the BOE’s stress testing, likely for practical, strategic and regulatory-signaling reasons.

In contrast, the U.S. regulatory posture remains more cautious and is still evolving. While the Financial Stability Oversight Council and Federal Reserve have acknowledged the rapid growth of private credit and its increasing interconnectedness with banks and insurers, oversight has so far centered on data gathering, monitoring, and targeted supervisory attention rather than formal stress testing or prudential frameworks. SEC Chair Paul Atkins has further downplayed systemic risk concerns, characterizing recent disruptions as isolated "blips" and signaling a preference for a light-touch regulatory approach while expanding access for retail investors to private markets.[1] The US approach thus continues to evolve through analysis and debate, even as regulators overseas move forward with concrete steps to assess how stress in private credit could transmit across the financial system.

Market Events — Signals or Outliers?

Regulatory responses are often driven by market events rather than preemptive risk assessments. Recent, widely publicized failures in segments of the private credit market—marked by borrower bankruptcies and alleged financial irregularities—strike familiar themes: weaker underwriting, reliance on short-term or structured funding and questionable practices in the face of liquidity pressure. Market leaders have cautioned that such visible failures may not be isolated—"when you see one cockroach, there are probably more"—even as large institutions emphasized that their own private credit exposures remain diversified and high-grade.

But these episodes may also be limited to intentional frauds rather than underlying credit-market stress. For example, the recent federal indictment charging the CEO and several top executives of Tricolor alleges that the subprime auto lender orchestrated a years-long scheme to defraud its lenders. The alleged fraud includes double-pledging the same collateral to multiple lenders and manipulating loan data to make ineligible, near-worthless assets appear to meet lender requirements. On its face, the indictment suggests an egregious fraud outlier rather than a systemic weakness in the credit markets.

Regardless of whether or not a case like Tricolor signals systemic weakness, it certainly will capture the attention of regulators and prosecutors who may feel compelled to respond and scrutinize private credit. In fact, one notable prosecutor has already entered the picture. On November 25, 2025, Jay Clayton, the US Attorney for the Southern District of New York and former Chair of the SEC, publicly warned that "sketchy marks" in private market valuations have drawn prosecutorial attention. The message is unmistakable: valuation practices are moving from supervisory concern to potential enforcement priority.

What Managers Should Do Now — A Fiduciary Standard of Vigilance

Even without convergence on a common regulatory framework, private credit managers face rising expectations driven by market events, regulatory signaling, and heightened public scrutiny. The central takeaway is that adherence to core fiduciary principles—particularly as it relates to accurate valuations, transparent disclosures, and rigorous underwriting diligence—is essential in maintaining trust with investors and regulators. Dispersion of the valuation of the same credit across managers, limited documentation or overly flexible mark-to-model practices may be interpreted as control weaknesses rather than inherent features of illiquid markets. This expanding focus, combined with visible enforcement activity, means managers should expect closer supervisory and investigative interest even absent evidence of systemic distress.

What managers should consider doing now:

- Review valuation policies and procedures to ensure actual practices conform to written policies.
- Strengthen valuation governance, documentation and third-party review processes.
- Assess liquidity and leverage assumptions, particularly where timing mismatches exist.
- Review bank and counterparty exposures to identify potential risk areas.
- Enhance transparency around valuation methodologies and liquidity terms, especially for products being offered to retail investors.
- Prepare for regulatory or enforcement inquiries as a component of prudent fiduciary oversight.

The current environment calls for sustained discipline, not complacency.

Read more of our Top Ten Regulatory and Litigation Risks for Private Funds in 2026.

---

[1] The two remaining SEC Commissioners have similarly deemphasized the risks. *See* SEC.gov | SIFMA's Private Markets Valuation Roundtable (Uyeda Speech, 9/4/2025); SEC.gov | Temporarily Terrified by Thomas: Remarks on Private Credit (Peirce Speech, 10/15/2024).

Related Professionals

- **Margaret A. Dale**
  Partner
- **Mike Hackett**
  Partner
- **Dorothy Murray**
  Partner
- **Joshua M. Newville**
  Partner
- **Todd J. Ohlms**
  Partner
- **Robert Pommer**
  Partner
- **Seetha Ramachandran**
  Partner
- **Anna Maleva-Otto**
  Partner
- **Nathan R. Schuur**
  Partner
- **Robert H. Sutton**
  Partner
- **John Verwey**
  Partner
- **Jonathan M. Weiss**

Partner

- **Edward Lister**
  Special Regulatory Counsel
- **Rachel E. Lowe**
  Partner
- **Adam Farbiarz**
  Senior Counsel
- **Adam L. Deming**
  Senior Counsel
- **Michael Guggenheim**
  Associate
- **Corey I. Rogoff**
  Associate
- **Hena M. Vora**
  Associate