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CMBS Distress & Special Servicing: What Borrowers Need to Know

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The Scale of the Problem

Commercial mortgage-backed securities (CMBS) distress has been a market-wide reality for some time. Across KBRA's rated universe of CMBS transactions, the loan distress rate — the combination of loans 30 or more days delinquent and loans that are current but have already been transferred to special servicing — closed 2025 at 10.6%, up from 9.3% at year-end 2024 and 6.7% at year-end 2023[1]. Office remains the epicenter, with a distress rate of 16.4% at year-end, up from 14.8% the year before and roughly triple the all-property average[2]. That elevated distress has persisted, though eased somewhat, through the first half of 2026: KBRA's monthly performance data placed the overall distress rate at 10.2% in April 2026, with further declines in May and June, while the office sector remained near its year-end level, registering a 17.0% distress rate in May 2026[3]. Retail, multifamily, and lodging loans have each seen meaningful upticks in distress as well, and maturity default — borrowers reaching their balloon date without being able to refinance or sell — now accounts for a substantial share of newly distressed loans, rather than pure cash-flow insolvency[4].

For a borrower who has never dealt with a securitized loan in default, the practical reality of what happens next often comes as a surprise. There is no single lender to call, no relationship banker with discretion to work things out, and no simple renegotiation. Understanding who is actually making decisions about a distressed CMBS loan — and what legal and contractual constraints bind them — is the necessary starting point for any workout strategy.

Who You're Actually Dealing With: The Special Servicer's Duties

Every CMBS loan is originated, pooled with other loans, and contributed to a securitization trust — a real estate mortgage investment conduit, or REMIC — that issues certificates to investors. Day-to-day administration of performing loans in the pool is handled by a master servicer, essentially a payment-processing and reporting function. The moment a loan defaults, is transferred for imminent monetary or non-monetary default, or otherwise becomes distressed, servicing authority shifts to the special servicer, a separate entity whose sole function is to resolve troubled loans.

The single most important fact for a distressed borrower to internalize is this: the special servicer's duty runs to the certificateholders of the trust — the bondholders who own the securitized debt — not to the borrower. Special servicers are generally required to act in accordance with a servicing standard that obligates them to maximize recovery to the trust as a whole, typically measured through a net present value, or NPV, analysis comparing the expected recovery from a modification against the expected recovery from foreclosure or a discounted payoff[5]. A modification only gets approved if the special servicer's NPV analysis shows it outperforms liquidation — not because it is fair to the borrower, and not because the property has a viable long-term business plan.

Layered on top of that is a structural conflict of interest that borrowers should understand going in: special servicers are typically compensated through servicing and workout fees that accrue only while a loan remains in special servicing, and many pooling and servicing agreements give the special servicer (or its affiliates) a right of first refusal to acquire the loan or the underlying asset at a discount if the special servicer determines the loan cannot be salvaged. Recent commentary has highlighted these dynamics, including the emergence of real estate operating companies themselves acting as special servicers on competitors' distressed loans[6]. None of this means a workout is impossible — it means borrowers should not assume the special servicer is motivated to see the loan return to performing status quickly, and should structure their requests and their record accordingly.

The Pooling and Servicing Agreement: The Rulebook for Every Decision

Every securitization is governed by a Pooling and Servicing Agreement, or PSA — a lengthy, deal-specific contract

among the depositor, master servicer, special servicer, trustee, and (in most deals) an operating advisor who reviews certain special servicer decisions for reasonableness. The PSA is not boilerplate the special servicer can waive; it is the source of the special servicer's authority, and it typically enumerates, in granular detail, what categories of modification the special servicer may approve unilaterally, what requires operating advisor consultation or consent, and what — if anything — is off the table entirely regardless of the merits.

This matters enormously for how a borrower should approach a workout request. A request that would be routine with a balance-sheet lender — say, a maturity extension paired with a partial paydown and a cash management trigger — may be entirely permissible under one PSA and functionally unavailable under another, depending on how that particular deal's PSA defines the special servicer's discretion. Before making any specific ask, borrowers and their counsel should, where possible, obtain and review the operative PSA (available for public conduit deals through the trustee or via SEC filings) rather than assuming standard market terms will apply.

Getting a copy of that PSA is not always straightforward, and it bears emphasizing at the outset: a borrower is not a party to the PSA and has no independent contractual right to demand a copy. For registered conduit deals, EDGAR generally solves the problem outright. For privately placed, unregistered deals, however, production sits squarely within the servicer's discretion — not an entitlement — and in practice, trustees and servicers are often reluctant to hand the full agreement to a non-party, particularly outside an active workout dialogue. Borrowers and counsel should treat that reluctance as the realistic baseline rather than the exception, and plan around it rather than count on it. Where the operative document itself proves difficult to obtain, a useful fallback is to know what a PSA typically provides: while every deal has its idiosyncrasies, most conduit-era PSAs share a common architecture — the same NPV-driven servicing standard, similar categories of unilateral versus operating-advisor-consent modification authority, and similar REMIC-driven limits on principal or maturity changes — so that counsel experienced across multiple deals can meaningfully benchmark a proposed ask against market-standard terms even without the specific document in hand. With that context, the practical channels for actually obtaining a copy, roughly in order of ease, are:

- **SEC EDGAR, for registered conduit deals**. The PSA is typically filed as an exhibit to the depositor's Form 8-K around closing, and is sometimes referenced in the free writing prospectus or 424B filings as well. Search EDGAR's company database by the trust or issuing entity name (for example, a series designation such as "BMARK 2022-C15" or "WFCM 2021-C61"), or by SIC code 6189 (asset-backed securities) if the exact trust name is not known. This is the most reliable source when it is available, since it produces the actual executed agreement.
- **The trustee's or certificate administrator's website**. Every PSA obligates the trustee or certificate administrator — commonly Wells Fargo, U.S. Bank, Citibank, or Computershare — to post deal documents, including the PSA and any amendments, on a dedicated investor reporting site (Wells Fargo's CTSLink is one of the more commonly encountered platforms). Access is technically limited to "Privileged Persons" as the PSA defines that term, generally certificateholders and their designees, which does not automatically include the borrower — but registration is often permitted for a party who can demonstrate a legitimate interest, such as borrower's counsel.
- **The servicer, directly.** The primary route for privately placed (Rule 144A) deals that were never publicly registered and will not appear on EDGAR at all — though not a guaranteed one. A request to the master servicer (if the loan is still performing) or the special servicer (once transferred), or to their counsel, for the PSA itself — or more narrowly, for the specific provisions governing modification authority, the operating advisor's role, and the servicing standard — is worth making, and is more likely to be honored once a borrower is in active workout discussions and the servicer has its own incentive to be forthcoming. It should not, however, be counted on as a routine or reliable source before that point.
- **Commercial data platforms.** Trepp, Bloomberg, and Intex aggregate deal documents, including PSAs, for subscribers. Useful where the firm already has access; rarely worth acquiring solely for a single deal.
- **Know the market-standard terms as a fallback**. When the document itself cannot be obtained, counsel with broad CMBS experience — or a CRE restructuring advisor who reviews PSAs regularly — can often identify how a particular deal is likely structured from observable characteristics: the securitization vintage, the identified special servicer (many of whom apply consistent internal practices across their book), and the loan's size and property type. This is not a substitute for the actual document, but it lets a borrower calibrate a realistic ask — and spot an unusually restrictive or unusually permissive PSA — even before a copy is in hand.

Starting with EDGAR costs nothing and requires no one's permission. If the deal is not registered, asking the servicer directly is worth doing but should not be the borrower's only plan — pairing that request with a working knowledge of market-standard PSA terms gives counsel a credible basis for a negotiating position even if the request is declined or goes unanswered.

The REMIC Overlay: Why Tax Law Limits What Even a Willing Servicer Can Do

Even a special servicer that wants to accommodate a borrower faces a second, independent constraint that has

nothing to do with the PSA: the federal tax rules governing REMICs. A REMIC is a pass-through entity for tax purposes, and it must hold only qualified mortgages to preserve that status. Under the REMIC regulations, if a mortgage loan held by the trust undergoes a significant modification — generally, any change substantial enough to be treated as an exchange of obligations under the general tax principles that apply to debt modifications — the modified loan is treated as a newly issued obligation[7]. If that newly issued obligation does not itself qualify as a qualified mortgage, the deemed disposition of the original loan can be a prohibited transaction, taxed at a 100% rate on any gain, and potentially threatening the REMIC's tax status altogether.

The regulations carve out a meaningful exception for exactly the scenario a distressed borrower is in: modifications occasioned by a default, or by a *reasonably foreseeable* — commonly shorthanded as *imminent* — default generally will not cause the modified loan to lose its qualified-mortgage status[8], and IRS guidance issued in 2009 substantially expanded the list of permitted modifications available under this exception, including maturity extensions, interest rate changes, and certain releases or substitutions of collateral[9]. The practical significance is this: a borrower who is current and simply wants better terms is asking for something the REMIC rules make very difficult to grant tax-efficiently. A borrower who can credibly demonstrate that default is imminent absent relief has a real, defensible path for the special servicer to pursue a modification. Documenting the imminence of default — through rent rolls, updated operating statements, refinancing quotes, and a clear-eyed narrative of what happens without relief — is not just persuasive, it is often the specific factual predicate the special servicer's own counsel needs to get comfortable proceeding.

It bears emphasis that satisfying the REMIC imminent-default exception does not, by itself, obligate the special servicer to do anything — it simply removes one obstacle. The special servicer still must conclude, independently, that the requested modification passes the PSA's authority limits and produces a better NPV outcome for certificateholders than the alternatives[10].

What Borrowers Can Realistically Request

Within those constraints, special servicers do have room to work — and, particularly in a market with distress rates this elevated, have strong institutional incentives to resolve viable loans rather than take back real estate. Requests that are commonly achievable, assuming the borrower can support them with real numbers, include:

- **Maturity extensions**. Typically the most readily available accommodation, especially where the underlying asset is performing operationally but cannot refinance in the current rate and capital markets environment. Extensions are frequently conditioned on partial paydowns, additional reserves, a rate adjustment, or a springing cash management structure.
- **Forbearance.** Short-term relief from enforcement while the parties negotiate a longer-term resolution, usually paired with a forbearance fee and continued accrual of default interest.
  Cash management and lockbox changes. Special servicers will often accept a shift to hard or springing cash management, giving the trust greater control over property-level cash flow, in exchange for other concessions.
- **Partial paydowns in exchange for relief**. Where a borrower or a new capital partner can inject fresh equity, a partial curtailment paired with an extension or rate modification is one of the more consistently approvable structures, since it directly improves the NPV analysis.
- **Reserve and escrow adjustments**. Modifications to tax, insurance, or capital expenditure reserve requirements are generally lower-friction changes that do not implicate the REMIC significant-modification analysis as acutely as principal or maturity changes.

What Borrowers Should Not Expect

Borrowers should calibrate expectations accordingly on requests that are structurally difficult regardless of the merits:

- **Principal write-downs**. A permanent reduction in principal is the single hardest modification to obtain. It is the most clearly a significant modification for REMIC purposes, it directly reduces recovery to certificateholders in a way an NPV test will rarely favor over a discounted payoff or foreclosure, and it typically requires operating advisor or even certificateholder-level consent under many PSAs. It is not impossible, but borrowers should not treat it as a realistic opening position.
- **Interest-rate relief unmoored from a broader restructuring**. A standalone rate reduction, absent an extension, paydown, or other trade-off, rarely clears the NPV threshold on its own.
- **Speed**. Special servicers are working through a high volume of distressed loans industry-wide, and every substantive modification typically requires NPV modeling, appraisal or updated valuation work, and often operating advisor review. Borrowers should plan for a process measured in months, not weeks.
- **Sympathy for market conditions alone**. "Rates went up" or "my last lender would have worked with me" is not, by itself, a basis for a special servicer to deviate from the PSA and the NPV test. Requests need to be grounded in demonstrable numbers.

The Discounted Payoff Alternative

For many borrowers, a discounted payoff — a negotiated agreement in which the trust accepts a lump-sum payment less than the full outstanding loan balance in exchange for a release of the debt and lien — can be a faster and procedurally simpler path than a modification when a special servicer is willing to agree to one. A DPO sidesteps much of the REMIC significant-modification analysis entirely, because the loan is being paid off and retired rather than modified and continued; it is a liquidation event for the trust, not a workout of a continuing obligation. That comparative simplicity, combined with the certainty of an immediate cash recovery, can make a DPO more attractive to a special servicer than a multi-year modification with ongoing performance risk — particularly for an asset the special servicer's NPV model does not view as a strong long-term credit.

Borrowers should not, however, treat a DPO as the likely outcome. Data tracking the composition of the CMBS special-servicing pipeline shows DPOs remain a distinctly minority resolution: as of December 2025, DPOs accounted for roughly 2.1% of the specially-serviced pipeline by balance, up from 0.9% a year earlier — a meaningful increase in relative terms, but still a small fraction of overall workout activity[11]. Over that same period, foreclosure — not DPO — became the dominant resolution path, rising from 17.3% to 29.1% of the pipeline, an increase of more than 68% year over year, while REO grew from 7.3% to 9.7%. Modification and extension activity, by contrast, ticked up only modestly, from 16.6% to 17.3%, and note sales declined slightly. Read together, the data suggests special servicers are increasingly concluding that consensual resolutions are not viable for a growing share of distressed loans, and are shifting toward enforcement rather than negotiation. A borrower should walk into a workout conversation clear-eyed about that shift: a DPO is a genuine option worth pursuing where the numbers support it, but it is not the default outcome, and foreclosure risk should be treated as a real and rising possibility rather than a remote one.

A DPO typically requires the borrower (or a new capital source) to arrange replacement financing or fresh equity to fund the discounted payment, and the special servicer will generally require a current appraisal or broker opinion of value to benchmark the offer against the NPV of the alternative (foreclosure and sale of the real estate). Borrowers considering this path should be aware of two practical issues that are easy to overlook in the moment: first, forgiveness of the discounted portion of the debt will generally produce cancellation-of-indebtedness income for tax purposes, which can be a meaningful and sometimes underappreciated cost of the transaction; and second, a DPO does not resolve exposure under a separate non-recourse carve-out or completion guaranty unless the guaranty is expressly released as part of the settlement — that release should be a non-negotiable deal point in any DPO negotiation.

If Workout Talks Fail: Enforcement and Guaranty Exposure

Where a modification or DPO cannot be reached, special servicers hold the same fundamental enforcement toolkit as any secured lender, exercised through the trustee: acceleration of the debt, appointment of a receiver to take control of the property and its cash flow, and foreclosure. Because most CMBS loans are structured as non-recourse with carve-outs (so-called "bad boy" guaranties), the loan itself is generally non-recourse to the borrower's principals — but the carve-out guaranty converts specific categories of conduct into personal recourse liability. Common triggers include voluntary bankruptcy filings by the borrower entity, waste, misappropriation of rents or insurance proceeds, unauthorized transfers or additional liens, and, in many current-generation loan documents, springing full recourse for a borrower's interference with the lender's enforcement rights or failure to maintain single-purpose-entity status.

This is one of the most important — and most frequently underappreciated — practical realities for a distressed borrower's principals: actions taken during a workout negotiation, including how the borrower entity is managed, how cash is handled, and how the entity responds to a receivership or foreclosure action, can themselves trigger personal recourse exposure that did not otherwise exist. Any distressed-loan strategy should be developed jointly with counsel who can map the specific carve-out and guaranty language in the loan documents against the contemplated course of conduct before, not after, decisions are made.

Practical Takeaways

- **Engage early**. Special servicers and their counsel are considerably more receptive to a borrower who reaches out before a payment or maturity default than one who waits until the loan is already delinquent. Framing a request around the REMIC's imminent-default standard is far easier to do proactively than reactively.
- **Build the record**. Come to the table with current financials, a credible business plan, and — where relevant — a specific, quantified explanation of why default is reasonably foreseeable absent relief. This is the evidentiary foundation for both the REMIC analysis and the special servicer's own NPV model.
- **Know the PSA before you ask**. What is achievable varies deal by deal. Understanding the specific special servicer's authority, the operating advisor's role, and any deal-specific quirks will shape a realistic ask rather than a wasted one.
- **Weigh a DPO honestly, early**. Where the underlying asset's value has genuinely declined, a modification that simply extends an unsustainable capital structure may cost more in the long run than a well-negotiated discounted payoff — particularly once the tax and guaranty-release terms are priced in correctly.

- **Protect the guaranty position at every step**. Personal recourse exposure is often created or avoided by decisions made during the workout process itself, not just by the original loan documents. Every material decision in a distressed CMBS matter should be screened against the carve-out and guaranty language before it is made.

CMBS distress at current levels is not a passing anomaly — it reflects a structural mismatch between loans underwritten in a very different rate environment and a maturity wall that keeps arriving. Borrowers who understand the special servicer's actual incentives, the PSA's actual limits, and the REMIC's actual constraints are in a materially better position to negotiate a workable outcome than those who assume a distressed CMBS loan will behave like a distressed bank loan. It generally will not — and the sooner that is accounted for, the more options remain on the table.

As CMBS distress levels remain elevated and refinancing challenges continue across multiple asset classes, borrowers must be prepared to navigate a highly structured workout process governed by special servicer obligations, pooling and servicing agreements, and complex REMIC tax rules. Early engagement, careful planning, and a well-supported strategy can often make the difference between preserving value and facing enforcement actions. Leech Tishman regularly advises borrowers, investors, developers, and property owners in connection with CMBS workouts, loan restructurings, discounted payoffs, distressed real estate matters, and commercial finance transactions. For assistance or additional information, please contact Forrest T. Passerin, a member of our Real Estate and Corporate Groups at fpasserin@leechtishman.com.

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[1]KBRA, CMBS Trend Watch (Jan. 9, 2026) (reporting the year-end 2025 CMBS loan distress rate — delinquent plus current-but-specially-serviced loans — across KBRA's rated transactions).

[2]Id. (office distress rate at 16.4% at year-end 2025, up from 14.8% at year-end 2024).

[3]KBRA, CMBS Loan Performance Trends: April 2026 (May 1, 2026) (distress rate at 10.2%, down from 10.3% the prior month); KBRA, CMBS Loan Performance Trends: May 2026 (Jun. 1, 2026) (distress rate declining a further 17 basis points; office distress rate at 17.0%); KBRA, CMBS Loan Performance Trends: June 2026 (Jul. 1, 2026) (distress rate declining a further 14 basis points).

[4]KBRA, CMBS Loan Performance Trends: December 2025 (Jan. 2, 2026) (property-type distress rates and volume of newly distressed loans).

[5]Janover Pro, Special Servicer (describing the net present value test governing a special servicer's choice among modification, discounted payoff, and foreclosure).

[6]See, e.g., Commercial Observer, More Commercial Real Estate Owners See Value in Special Servicing Platforms (Jul. 2026) (discussing special servicer fee structures and potential conflicts of interest disclosed in a July 2025 Fitch report).

[7]Treas. Reg. § 1.860G-2(b)(1)–(2) (a significant modification of a qualified mortgage held by a REMIC is generally treated, for tax purposes, as a deemed exchange for a newly issued obligation under the principles of section 1001).

[8]Treas. Reg. § 1.860G-2(b)(3) (excepting, among other things, changes occasioned by a default or reasonably foreseeable default, or by the exercise of a right reserved in the original loan documents, from significant-modification treatment).

[9]Rev. Proc. 2009-45, 2009-40 I.R.B. 471 (describing the conditions, including the liberalized "reasonably foreseeable default" standard, under which modifications to commercial mortgage loans held by REMICs and other securitization vehicles will not be challenged by the Service or treated as prohibited transactions).

[10]Seyfarth Shaw LLP, IRS Announces New REMIC Rules (noting that even where the REMIC regulations permit a modification, the master and special servicer remain separately bound by whatever narrower authority the PSA gives them).

[11]CRED iQ, Special Servicer Workout Strategies Shift Toward Resolution as Foreclosures Surge (Jan. 16, 2026) (comparing the composition of the CMBS special-servicing pipeline by workout strategy, December 2024 to December 2025