

Investment Management & Funds Regulatory Update - October 2025

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In this issue, we discuss a recent [no-action letter](#) relating to the use of state trust companies as permitted custodians for crypto assets under relevant Advisers Act and Investment Company Act custody rules.

Industry update

SEC staff issues no-action relief regarding regulated funds' and registered advisers' use of state trust companies as custodians for crypto assets

On September 30, 2025, the SEC staff issued a [no-action letter](#) permitting registered investment advisers and registered funds (including business development companies) to custody crypto assets, and related cash and cash equivalents reasonably necessary to effect transactions in crypto assets, with state trust companies, subject to the conditions described below. State trust companies, as described in the no-action letter, are entities organized under state law that are supervised and examined by state authorities having supervision over banks, and are permitted to exercise fiduciary powers under applicable state law.

As discussed in the letter, Rule 206(4)-2 of the Advisers Act requires registered investment advisers that have custody of client funds or securities to maintain such client funds and securities with a "qualified custodian," which is defined to include a "bank" as defined in Section 202(a)(2) of the Advisers Act. Similarly, Sections 17(f) and 26(a) of the Investment Company Act require regulated funds to maintain their securities and similar investments with certain specified custodians, including a "bank" as defined in Section 2(a)(5) of the Investment Company Act. In order to meet the definition of a "bank" under the Advisers Act and Investment Company Act, a state trust company must meet certain requirements, including a requirement that "a substantial portion" of its business consist of "receiving deposits or exercising fiduciary powers similar to those permitted to national banks under the authority of the [OCC]." In its inquiry letter, the requesting party noted that such "bank" definition requires a facts and circumstances analysis and presents uncertainty in determining whether a given state trust company can meet the requirement that a "substantial portion" of its business consist of receiving deposits or exercising such fiduciary powers. The requesting party noted that in recent years, state trust companies have implemented sophisticated controls and procedures to ensure safekeeping of crypto assets, which have evolved in response to due diligence demands of registered investment advisers and regulated funds seeking to use them as custodians for crypto assets.

In its response, the SEC staff granted no-action relief permitting registered investment advisers and regulated funds to treat a state trust company as a "bank" as defined in the Advisers Act and Investment Company Act, and therefore to treat a state trust company as a permitted custodian under Rule 206(4)-2 and Sections 17(f) and 26(a), provided that:

1. Prior to engaging the state trust company and on an annual basis, the registered investment adviser or regulated fund, as applicable, has a reasonable basis, after due inquiry, for believing that:

- a. the state trust company is authorized by the relevant state banking authority to provide custody services for crypto assets and related cash and/or cash equivalents; and
 - b. the state trust company maintains and implements written internal policies and procedures reasonably designed to safeguard crypto assets and related cash and/or cash equivalents from the risk of theft, loss, misuse, and misappropriation, with such policies and procedures addressing, among other topics, private key management and cybersecurity. In making such a determination, the registered investment adviser or regulated fund:
 - i. receives and reviews the state trust company's most recent annual financial statements and confirms that such financial statements have been subject to an audit by an independent public accountant and have been prepared in accordance with GAAP; and
 - ii. receives and reviews the state trust company's most recent written internal control report prepared by an independent public accountant during the current or prior calendar year (e.g., SOC-1 report or SOC-2 report) and confirms that such internal control report contains an opinion of such independent public accountant that controls have been placed in operation as of a specific date, are suitably designed, and are operating effectively to meet control objectives relating to custodial services, including the safeguarding of crypto assets and related cash and/or cash equivalents during the year;
2. The registered investment adviser or regulated fund, as applicable, enters into, or causes its client to enter into, as applicable, a written custodial services agreement with the state trust company, which provides that:
 - a. the state trust company will not, directly or indirectly, lend, pledge, hypothecate, or rehypothecate any crypto assets (or related cash and/or cash equivalents) held in custody for the client or regulated fund, as applicable, without the prior written consent of the client or regulated fund, and then only for the account of such client or regulated fund; and
 - b. all crypto assets (and related cash and/or cash equivalents) held in custody for the client or regulated fund, as applicable, will be segregated from the state trust company's assets;
 3. The registered investment adviser discloses to its clients or the regulated fund discloses to the members of its board of directors or trustees, as applicable, any material risks associated with using state trust companies as custodians of crypto assets (and related cash and/or cash equivalents); and
 4. The registered investment adviser (with respect to its client) or the regulated fund (and, as applicable, its board of directors or trustees), reasonably determines that the use of the state trust company's custody services is in the best interest of such client or regulated fund and its shareholders, as applicable.

The staff noted in its response that the SEC is considering rulemaking regarding the requirements applicable to registered investment advisers and regulated funds with respect to the custody of crypto assets.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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