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SEC proposes amendments to its custody rules for investment advisers and regulated funds

The Securities and Exchange Commission (SEC) proposed new amendments intend to accommodate crypto assets (both securities and non-securities), expand the universe of qualified custodians available to advisers and funds, and make it easier for advisers to offer a variety of asset classes and structures to clients.

5 insights you should know

State trusts would be considered qualified custodians: The proposal would allow state trust companies (STC) to serve as qualified custodians for advisory client and regulated fund crypto assets if: (1) the STC is authorized by its state banking authority for crypto asset custody; (2) the STC has reasonable policies and procedures to safeguard crypto assets and related cash or cash equivalents from theft, loss, and misappropriation; and (3) current audited financials and internal controls report are reviewed by the relevant adviser or fund.

Adviser "self custody" would be permitted under certain conditions: The proposal would allow advisers to directly hold crypto assets for their clients, including funds, if: (1) a permitted custodian is not available; (2) the adviser has the relevant, documented expertise to maintain a self-custody arrangement; (3) the adviser segregates client assets; (4) the adviser implements adequate cybersecurity practices, which are updated annually; (5) the adviser obtains annual internal control reports; and (6) account statements are sent at least quarterly to each of the adviser's clients.

Recordkeeping via digital ledger: The amendments would allow the records of a distributed ledger or crypto network satisfy the recordkeeping requirements of the Investment Advisers Act of 1940 (Advisers Act) and the Investment Company Act of 1940 (Investment Company Act) with certain conditions.

Changes to Form ADV and Form N-CEN: The proposal includes updates to Form ADV and Form N-CEN to collect information about custody for crypto assets and tokenized fund shares.

Changes to auditor requirements: The proposal would eliminate requirements for auditors engaged under the custody rule to be registered with and subject to the oversight of the Public Company Accounting Oversight Board (PCAOB). It would also provide an exception from the independent verification requirement for an adviser with custody of funds solely via a standing letter of authorization.

5 considerations to evaluate

1. **Expanding the pool of qualified custodians:** Taking into consideration evolving technology and the unique custodial considerations for crypto assets, the proposal would expand the pool of qualified custodians that can custody assets for advisers and funds to include state trust companies. When selecting a qualified custodian for crypto assets, firms and advisers should evaluate the features of the asset and the practices, procedures, and regulatory guardrails that apply to the custodian, including its internal control report.
2. **Self custody as a last resort:** Advisers would be permitted to custody client and fund crypto assets, but only if a qualified custodian isn't available for the asset. Advisers would need to ensure that they have the expertise needed to appropriately safeguard the crypto assets and implement related internal procedures to ensure compliance with the various conditions associated with self-custody, including obtaining an internal control report within six months of taking self-custody.
3. **The network is the record**: Under the proposal, records on the network would satisfy a firm's recordkeeping requirements. Before electing to leverage the network for their recordkeeping (and custody needs), firms should conduct due diligence into its maintenance model (proof of stake vs. proof of work), cyber protocols (including forking and interoperability standards) and the tokenization model of the asset (e.g., an asset natively issued on a blockchain or tokenized under a third-party model).
4. **Align reporting obligations:** Firms will need to align their reporting processes to ensure that they accurately record and report on any new custody arrangements that arise because of the proposal.
5. **Consider a custodian's audit quality:** Regardless of regulatory oversight structure, assessing audit quality and the quality of a qualified custodian's internal control report should be a consideration for firms when selecting a qualified custodian.

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Endnotes

1. Securities and Exchange Commission (SEC), "Adviser and Regulated Fund Custody Rules; Crypto Custody Rules", October 6, 2026.

Roy Ben Hur
Managing Director
Deloitte & Touche LLP
rbenhur@deloitte.com

Mike Marzelli
Audit & Assurance Partner
Deloitte & Touche LLP
mmarzelli@deloitte.com

Ryan Moore
Audit & Assurance Partner
Deloitte & Touche LLP
ryanmoore@deloitte.com

Dan Rooney
Audit & Assurance Partner
Deloitte & Touche LLP
danrooney@deloitte.com

Deloitte Center for Regulatory Strategy, US

Maria Gattuso
Investment Management Leader
Principal
Deloitte & Touche LLP
mgattuso@deloitte.com

Lananh Nguyen
Research & Insights Director
Managing Director Deloitte Services LP
lananhnguyen@deloitte.com

Meghan Burns
Research Leader
Deloitte Services LP
megburns@deloitte.com

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