

January 22, 2021

*Submitted electronically to IMOCC@sec.gov*

Ms. Vanessa Countryman  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-1090

Re: **Custody Rule and Digital Assets**

Dear Ms. Countryman,

Fidelity Digital Asset Services, LLC ("Fidelity Digital Assets") appreciates the opportunity to provide comments to the Securities and Exchange Commission ("SEC" or "Commission") in response to the staff release titled "WY Division of Banking's 'NAL on Custody of Digital Assets and Qualified Custodian Status'" dated November 9, 2020 (the "Statement").<sup>1</sup> The Statement requests input relating to the definition of "bank" and "qualified custodian" under the Investment Advisers Act of 1940 (the "Advisers Act") and rule 206(4)-2 thereunder (the "Custody Rule").

Fidelity Digital Assets is a New York state limited liability trust company that provides custody and trade execution services for digital assets. As a highly regulated banking institution supervised by one of the leading state banking regulators in the country, Fidelity Digital Assets strongly believes that entities operating as New York state limited-liability trust companies satisfy all of the elements to be considered a qualified custodian under the Custody Rule, and we encourage the Commission to publicly confirm that conclusion.<sup>2</sup>

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<sup>1</sup> See *Staff Statement on WY Division of Banking's "NAL on Custody of Digital Assets and Qualified Custodian Status"* (Nov. 9, 2020), available at <https://www.sec.gov/news/public-statement/statement-im-finhub-wyoming-nal-custody-digital-assets>.

<sup>2</sup> Notwithstanding that the Custody Rule does not apply to the custody of digital assets that are not considered securities for purposes of the Securities Act of 1933, as amended, or the Investment Company Act of 1940, as amended, registered investment advisers take comfort in delegation of custody of such assets to institutions that are otherwise eligible to be considered qualified custodians. It is therefore important that the Commission clarify its position regarding state-chartered trust companies.

## **I. EXECUTIVE SUMMARY**

The Statement specifically seeks input on the following two sets of issues, among other things:

- Do state chartered trust companies possess characteristics similar to those of the types of financial institutions the Commission identified as qualified custodians? If yes, to what extent?
- In what ways are custodial services that are provided by state chartered trust companies equivalent to those provided by banks, broker-dealers, and futures commission merchants? In what ways do they differ? Would there be any gaps in – or enhancements to – protection of advisory client assets as a result of a state chartered trust company serving as qualified custodian of digital assets or other types of client assets?

With respect to first question, New York trust companies are indistinguishable in any meaningful way from national banks regulated by the Office of the Comptroller of the Currency (“OCC”) in terms of both their authority to provide custody services and the type of supervision to which such custody services are subject. With respect to the second set of questions, the custodial services provided by New York trust companies are also indistinguishable in any meaningful way from custodial services provided by banks, broker-dealers and futures commission merchants. Indeed, New York trust companies have taken the lead in setting a standard for digital asset custody services that other qualified custodians seek to emulate. We focus in this comment on the comparison to national banks and trust companies chartered by OCC because they operate most similarly to New York trust companies.

## **II. CUSTODIAL SERVICES PROVIDED BY NEW YORK STATE CHARTERED TRUST COMPANIES ARE INDISTINGUISHABLE FROM OTHER QUALIFIED CUSTODIANS IN ANY MEANINGFUL WAY**

Custody of securities provided by New York state chartered trust companies is no different from custody provided by other regulated providers of custody services, particularly national banks and trust companies. The fact that the regulation and supervision of Fidelity Digital Assets’ custody is done by a state agency responsible for the supervision of banks and trust companies rather than a federal regulatory agency is irrelevant to this analysis. If Congress had not intended state-chartered entities to be treated on a par with national banks, it would not have specifically included both state banks and state trust companies in the definition of “bank” in the Advisers Act.

First, with respect to general custody services for a variety of financial assets, New York state chartered institutions are among the leading providers of custody in the country. For

example, one the largest custody providers in the nation is The Bank of New York Mellon, a New York chartered entity. It could hardly be said that the regulator responsible for the supervision of The Bank of New York Mellon, a New York state chartered entity organized in 1784, and now with more than \$350 billion of assets and more than \$27 trillion in custody, and Depository Trust Company, another New York chartered entity, has insufficient experience in overseeing complex and innovative custody activities. Moreover, the New York Department of Financial Services (“NYDFS”) remains on the forefront of financial supervision, chartering new internet-based banks like Goldman Sachs Bank (\$282 billion in assets), creating a new regulatory regime for nonbank entities engaged in virtual currency activities, and taking wide-ranging and aggressive enforcement positions in cases of alleged compliance failures. Overall NYDFS oversees approximately 1,500 banking and other financial institutions with assets totaling more than \$2.6 trillion, as of Dec. 31, 2019, making it an appropriate primary regulator for a qualified custodian. In many ways it would be more appropriate to ask whether the services of other custody providers match what is provided by New York chartered entities than vice versa. Furthermore, while The Bank of New York Mellon does act as full service institution, it is actually chartered as trust company and its custody services are offered under the same authority and the same oversight as those offered by limited purpose trust institutions such as Fidelity Digital Assets. New York trust companies offer the same custody services as New York “banks” because their authority to provide such service and the regulation of those services is identical.

Second, in relation to custody of digital assets in particular, New York state trust companies like Fidelity Digital Assets are providing the model that other providers of digital asset custody are likely to follow. As the OCC explains in its recent interpretive letter acknowledging the authority of national banks to provide custody of digital assets, these custody services, while based on the general power to hold real and personal property for customers, involves a specific set of services linked to the technology underlying such assets: “[A] bank ‘holding’ digital currencies on behalf of a customer is actually taking possession of the cryptographic access keys to that unit of cryptocurrency. ... Holding the cryptographic access key to a unit of cryptocurrency is an electronic corollary of these traditional safekeeping activities.”<sup>3</sup> Moreover, as the OCC goes on to explain, the nature of those key custody services, including for digital asset securities,<sup>4</sup> is expected to be similar, if not identical, to the types of private key custody provided by Fidelity Digital Assets under its New York state trust company charter:

Banks may offer different methods of providing cryptocurrency custody services, depending on their expertise, risk appetite, and business models.

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<sup>3</sup> OCC Interp. Ltr. #1170, at 8 (July 22, 2020), <https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2020/int1170.pdf>.

<sup>4</sup> *Id.* at n.48 (noting that the subset digital asset custody related to digital asset securities would also be subject to Federal securities laws).

Some banks may offer to store copies of their customers' private keys while permitting the customer to retain their own copy. Such services may be more akin to traditional safekeeping and would permit the customer to retain direct control over their own cryptocurrencies. Other banks may permit customers to transfer their cryptocurrencies directly to control of the bank, thereby generating new private keys which would be held by the institution on behalf of the customer. Such services may be more akin to traditional custody services, but as with traditional custody, would not permit the customer to maintain direct control of the cryptocurrency. Banks may also offer other custody models that may be appropriate.<sup>5</sup>

Fidelity Digital Assets manages omnibus wallets with client assets segregated at the books and records level, meaning clients do not have access to their own personal public/private keys. Fidelity Digital Assets maintains both online ("hot") wallets as well as various proprietary offline wallets (a/k/a "cold" or "deep cold"). The proprietary design of the various offline wallets allows for risk segmentation with varying service level standards, geographic dispersion, and number of associates required to initiate transactions; with the majority of assets held in the most secure "deep cold" storage. Fidelity Digital Assets is solely responsible for managing the allocation between online/offline wallets. This compares favorably to the types of hot and cold storage that the OCC suggests may be appropriate for national bank custodians.<sup>6</sup>

In addition to the core safekeeping aspects of custody, the OCC also explains that "The services national banks may provide in relation to the cryptocurrency they are custodialing may include services such as facilitating the customer's cryptocurrency and fiat currency exchange transactions, transaction settlement, trade execution, recording keeping, valuation, tax services, reporting, or other appropriate services."<sup>7</sup> Similarly, New York trust companies may provide any or all of these services. For example, in connection with its custody of digital assets, Fidelity Digital Assets also provides trade execution, reporting and other related services.

The Statement also indicates that a critical attribute of qualified custodians is that all such entities are subject to "extensive regulation and oversight" and asks if there would be any gaps in protections of client assets when those are held in custody by state-chartered trust companies. New York state trust companies are subject to equally rigorous oversight to other types of entities that hold customer assets. Like national banks, they must obtain specific approval of their primary regulator for the exercise of their fiduciary powers. Moreover, limited purpose trust companies engaged in the custody of digital assets are

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<sup>5</sup> *Id.* at n.37.

<sup>6</sup> *See id.* at 5.

<sup>7</sup> *Id.* at n.39.

subject to even more stringent requirements than national banks which, following initial approval of trust powers, generally can exercise those powers broadly without further approval of the OCC. In contrast, NYDFS requires in their approval orders that limited purpose trust companies obtain separate approval for all material changes in business. Even the mere custody of a new type of digital asset requires separate NYDFS approval if that asset has not already been “greenlisted” by NYDFS.

Indeed, much like federal savings associations that the Supreme Court characterized as being subject to “cradle to grave” regulation and oversight,<sup>8</sup> New York state trust companies are subject to the extremely broad discretion of the NYDFS in supervision for the purpose of both ensuring the safety and soundness of the organization and protecting the public interest. In this regard, the New York Banking Law (“NYBL”) provides: “The superintendent is hereby authorized and empowered to make such general rules and regulations as may be necessary and proper to effectuate the provisions of this chapter relating to the formation and operation of limited liability trust companies.”<sup>9</sup> Furthermore, NYDFS has virtually unbounded authority to issue rules, regulations and orders<sup>10</sup> to implement the general policy that “the business of all banking organizations shall be supervised and regulated through the department of financial services in such manner as to insure the safe and sound conduct of such business, to conserve their assets, to prevent hoarding of money, to eliminate unsound and destructive competition among such banking organizations and thus to maintain public confidence in such business and protect the public interest and the interests of depositors, creditors, shareholders and stockholders.”<sup>11</sup>

For example, NYDFS has promulgated an extensive cybersecurity regulation that is even more detailed than the data security regulations applicable to national banks. It includes specific requirements for cybersecurity programs and policies, mandates the appointment of a chief information security officer, requires an annual certification of cybersecurity compliance and includes detailed provisions related to: penetration testing and vulnerability assessments, audit standards, access privileges, application security risk assessments, training and monitoring, encryption, incident response plans, use of multifactor authentication, etc.<sup>12</sup>

Similar, notwithstanding that New York trust companies are subject to effectively the same anti-money laundering requirements as national banks,<sup>13</sup> including adoption and implementation of anti-money laundering (“AML”) and customer identification programs,

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<sup>8</sup> See *Fidelity Fed. S. & L. v. De la Cuesta*, 458 U.S. 141, 145 (1982).

<sup>9</sup> NYBL § 102-a(4).

<sup>10</sup> *Id.* at § 14.

<sup>11</sup> *Id.* at §10.

<sup>12</sup> See 23 NYCCR Part 500.

<sup>13</sup> See 31 C.F.R. Part 1020.

NYDFS has adopted its own detailed AML requirements applicable to trust companies, which include maintaining a transaction monitoring program for potential AML violations and suspicious activity reporting, maintain a filtering program to prevent transactions that are prohibited by federal sanctions regimes, and submitting annually to NYDFS a certification regarding compliance with the foregoing requirements.<sup>14</sup>

In addition, the NYDFS routinely issues Industry Letters setting forth standards and requirements on a wide range of internal control and risk management topics, as diverse as audit standards,<sup>15</sup> vacation policies,<sup>16</sup> COVID risks<sup>17</sup> and climate change.<sup>18</sup>

Finally, in addition to enforcing specific regulatory reporting requirements,<sup>19</sup> NYDFS consistently exercises its broad authority to examine trust companies for compliance with law, risk management and general safety and soundness considerations,<sup>20</sup> including to assess items such as the internal controls, client records and segregation of assets topics that the Statement indicates are important to the ability of an entity to act as a qualified custodian. In this regard, Fidelity Digital Assets is subject to annual examination, with specific attention to its internal controls and risk management systems. Thus, a registered investment adviser should have at least the same level of comfort that client records are being properly maintained when relying on Fidelity Digital Assets for custody of assets as when relying on other banks, federal savings associations or broker-dealers, many of which are not nearly as sophisticated and experienced in the custody of digital assets as Fidelity Digital Assets.

### **III. NEW YORK STATE CHARTERED TRUST COMPANIES ARE NOT DISTINGUISHABLE FROM OTHER QUALIFIED CUSTODIANS IN ANY MEANINGFUL WAY**

As indicated above, the Statement requests input on the following questions: “Do state chartered trust companies possess characteristics similar to those of the types of financial institutions the Commission identified as qualified custodians? If yes, to what extent?” New York state chartered trust companies, such as Fidelity Digital Assets, do indeed possess characteristics similar, if not identical, to those of other financial institutions that the Commission has considered to be qualified custodians.

The Commission’s regulations define five types of qualified custodians: banks, federally insured savings associations, registered broker-dealers, futures commission merchants and

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<sup>14</sup> See 3 NYCCR Part 504.

<sup>15</sup> See <https://www.dfs.ny.gov/legal/industry/il010126.htm>.

<sup>16</sup> See <https://www.dfs.ny.gov/legal/industry/il960822.htm>.

<sup>17</sup> See

[https://www.dfs.ny.gov/industry\\_guidance/industry\\_letters/il20200310\\_coronavirus\\_vc\\_business\\_oper\\_fin\\_risk](https://www.dfs.ny.gov/industry_guidance/industry_letters/il20200310_coronavirus_vc_business_oper_fin_risk).

<sup>18</sup> See [https://www.dfs.ny.gov/industry\\_guidance/industry\\_letters/il20201029\\_climate\\_change\\_financial\\_risks](https://www.dfs.ny.gov/industry_guidance/industry_letters/il20201029_climate_change_financial_risks).

<sup>19</sup> See *id.* at §125.

<sup>20</sup> See *id.* at §36.

certain foreign financial institutions.<sup>21</sup> For this purpose, the term “bank” is defined by cross-reference to section 202(a)(2) of the Advisers Act, which includes, among other things, “any other banking institution, savings association, as defined in section 1462(4) of title 12, or trust company, whether incorporated or not, doing business under the laws of any State or of the United States, a substantial portion of the business of which consists of receiving deposits or exercising fiduciary powers similar to those permitted to national banks under the authority of the Comptroller of the Currency, and which is supervised and examined by State or Federal authority having supervision over banks or savings associations, and which is not operated for the purpose of evading the provisions of this subchapter....”<sup>22</sup>

By definition, a New York trust company is a “trust company” doing business under the laws of a state, i.e., New York.<sup>23</sup> Furthermore New York trust companies are supervised and examined by the same regulatory body that examines and supervises full-service state banks and savings associations doing business in New York.<sup>24</sup> Accordingly, the only other statutory condition for a *bona fide* New York trust company like Fidelity Digital Assets to be eligible to be treated as a qualified custodian is the question whether “a substantial portion of the business of [the trust company] consists of receiving deposits or exercising fiduciary powers similar to those permitted to national banks under the authority of the Comptroller of the Currency.” The analysis whether a “substantial portion” of an institution’s activities consist of the exercise of fiduciary powers requires a case-by-case review of the activities of the individual institution. We therefore address below the broader remaining question whether the custody activities of New York trust companies more generally constitute (i) an exercise of fiduciary powers that (ii) is similar to those permitted for national banks.

As a New York State trust company operating pursuant to Section 102-a of the NYBL, Fidelity Digital Assets may engage in all activities described in Sections 96 and 100 of the NYBL, with the exception of accepting deposits and making loans.<sup>25</sup> Section 100 of the NYBL, which bears the title “Fiduciary Powers,” lists the “fiduciary powers” granted to New York trust companies. This statutory designation of fiduciary powers includes, among other things, the power to (i) “act as ... agent of any person or corporation, foreign or domestic, for any lawful purpose,” (ii) “take, accept and execute any and all such trusts, duties and powers of whatever nature or description as may be conferred upon or entrusted or committed to it by any person or persons, or any body politic, corporation, domestic or foreign, or other

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<sup>21</sup> See 17 C.F.R. § 275.206(4)-2(d)(6).

<sup>22</sup> 15 U.S.C. § 80b-2(a)(2)(C)(emphasis added).

<sup>23</sup> New York trust companies are chartered and supervised pursuant to Article III of the New York Banking Law.

<sup>24</sup> See [https://www.dfs.ny.gov/who\\_we\\_supervise](https://www.dfs.ny.gov/who_we_supervise).

<sup>25</sup> See NYBL §§ 96, 100 and 102-a. New York limited purpose trust companies are permitted to make loans which arise directly from the exercise of their fiduciary powers granted in Section 100 of the NYBL. See Information and Procedure for the Organization of a Trust Company for the Limited Purpose of Exercising Fiduciary Powers, available at <http://www.dfs.ny.gov/banking/iaus1b.htm>

authority by grant, assignment, transfer, devise, bequest or otherwise. . . ,” and (iii) “receive, take, manage, hold, and dispose of . . . any property or estate, real or personal.”<sup>26</sup>

Although the word “custody” does not appear in the foregoing litany, each of the foregoing references encompasses a broader set of authorizations for which acting as a custodian (with or without discretion) is an included subset. For example, custody may be considered a subset of the broad authorization of “agency” services above. As the OCC Handbook on Custody Services provides: “Custody relationships are contractual in nature and are essentially directed agencies. The customer is the principal, the custodian is the agent.”<sup>27</sup> Consistent with that generally held understanding of the nature of custody, the NYDFS has opined that acting as a “custodian or bailee” is an exercise of fiduciary powers under the broad “agency” and related language of the NYBL.<sup>28</sup>

Accordingly, the remaining question to be addressed is whether those fiduciary powers are similar to those permitted to national banks under the authority of the OCC. Under the National Bank Act, the OCC is authorized to permit national banks, “the right to act as trustee, executor, administrator, registrar of stocks and bonds, guardian of estates, assignee, receiver, or in any other fiduciary capacity in which State banks and trust companies . . . which come into competition with national banks are permitted to act under the laws of the State in which the national bank is located.”<sup>29</sup> As a result, the defined fiduciary powers for national banks are, in the case of powers derived from preceding highlighted language, “determined by reference to the law of the state in which the bank acts in a fiduciary capacity.”<sup>30</sup> In other words, a national bank located in New York would be expressly authorized to act in any “fiduciary capacity”<sup>31</sup> in which Fidelity Digital Assets is permitted to engage. It is therefore effectively a tautology that the fiduciary powers exercised by a New

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<sup>26</sup> NYBL §100(1), (5).

<sup>27</sup> Comptroller’s Handbook for Custody Services at 8; <https://www.occ.gov/publications-and-resources/publications/comptrollers-handbook/files/custody-services/pub-ch-custody-services.pdf>.

<sup>28</sup> See NYDFS Legal Interpretation LI 3, § 3.1; New York State Banking Department Memorandum, January 5, 2010 (“[U]nder its fiduciary powers, the Bank would clearly have the authority to act as a custodian or bailee.”). There is a distinction between the statutory authority of a trust company under the NYBL and the duties owed to customers as a matter of contract.

<sup>29</sup> 12 U.S.C. § 92a(a). Moreover, the OCC has determined that several custodial- and trust-related services (e.g., operating custody trust ledger deposit account programs and offering nationwide trust services) are treated as fiduciary activities that are authorized under 12 U.S.C. § 92a(a). OCC, Activities Permissible for National Banks and Federal Savings Associations, Cumulative, at 51 (Oct. 2017).

<sup>30</sup> OCC IL #866 (Oct. 8, 1999), at 5; OCC Comptroller’s Licensing Manual: Fiduciary Powers, at 10 (May 2017) (“The extent of fiduciary powers is the same for both out-of-state and in-state national banks and FSAs. That extent depends on what powers the state grants to the fiduciaries in the state with which national banks and the FSAs compete.”).

<sup>31</sup> The National Bank Act uses the terms “trust powers” and “fiduciary capacity” and not “fiduciary powers,” which is the term used in the Advisers Act, but there is no doubt that the “trust powers” authorized by 12 U.S.C. § 92a are “fiduciary powers” within the intent of the Advisers Act cross-reference.



Secretary, Securities and Exchange Commission  
January 22, 2021  
Page 9 of 9

York trust company are “similar” to those authorized to a national bank, because a national bank located in New York would be authorized to exercise precisely those identical fiduciary powers through the federalization of state law via the National Bank Act.

Thus, by the plain language of the statute and regulation, a New York limited liability trust company would satisfy the definition of a qualified custodian as long as a substantial portion of its business consisted of the exercise of its fiduciary powers. As the foregoing indicates, not only would there be no gaps in the protection of advisory client’s securities from custody by a New York trust company, the specialization of trust companies like Fidelity Digital Assets in the custody of digital assets promises to provide substantial enhancement to the overall protection of a client’s digital assets. Fidelity Digital Assets has implemented industry-leading technology for the safekeeping of digital assets, making Fidelity Digital Assets a preferred custody solution for sophisticated institutional investors. The SEC should acknowledge this critical role of Fidelity Digital Assets and other New York trust companies and ensure that registered investment advisers and their advisory clients continue to have access to the superior custody services provided by Fidelity Digital Assets.

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Fidelity Digital Assets would be pleased to provide further information, participate in any direct outreach efforts the Commission undertakes, or respond to questions the Commission may have about our comments.

Sincerely,



Tom Jessop  
President