FMA
FINANCIAL MARKETS AUTHORITY
TE MANA TĀTAI HOKOHOKO

JUNE 2026

Discussion paper: Review of law and practices relating to custody of assets

About this consultation

The Financial Markets Authority – Te Mana Tātai Hokohoko (**FMA**) is undertaking a review of law and market practices relating to the custody (safeguarding) of money and assets in financial markets. Custody services[1] are fundamental to maintaining confidence in New Zealand's financial markets, ensuring that client assets are securely protected and readily accessible.

This discussion paper aims to start a conversation with interested stakeholders. It provides an overview of the custody market and regulatory framework, summarises key insights from our monitoring and misconduct reports, and identifies some issues and risks we have identified.

We invite you to share your views on whether current settings are fit for purpose as markets, business models and technology evolve.

Your feedback is important for shaping informed future regulatory approaches and ensuring that custody practices remain robust and effective. The perspectives provided will play a key role in informing the FMA's ongoing regulatory efforts and any recommendations we make to the Ministry of Business, Innovation and Employment (MBIE). As the lead policy agency for financial markets conduct, MBIE is responsible for any decisions regarding changes to laws or regulations.

How to respond

Please use the feedback form provided on the web page for this consultation at www.fma.govt.nz/business/focus-areas/consultation. Note that all feedback received is subject to the Official Information Act 1982 and may be made available on our website or other external channels. See the feedback form for more information about your privacy and confidentiality options.

Submissions close at 5pm on Monday 27 July 2026.

Next steps

We intend to hold an in-person workshop on 19 August 2026 to explore the issues raised in this paper with industry participants and other stakeholders. If you are interested in attending, please email us at events@fma.govt.nz by 10 July 2026. Numbers will be limited. After the workshop, we will publish submitter feedback together with any initial comments from us.

This consultation is for investors, custodians, financial service firms and interested persons.	It sets out issues relating to custody of assets, for discussion and feedback.

[1] We use the term 'custody services' in this paper to refer generally to custody services that are regulated under the Financial Markets Conduct Act 2013.

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Overview

The FMA's main objective is to promote and facilitate the development of fair, efficient, and transparent financial markets. One of our key functions is to promote the confident and informed participation of businesses, investors, and consumers in those financial markets. Our regulatory approach is pro-innovation, flexible and technology neutral.

Custody services underpin investing, saving and payments by holding client assets and funds. Confidence in financial markets depends on trust that these assets are safe and accessible. Delays in accessing assets, or any loss of assets held in custody, could undermine public confidence in financial markets.

This paper describes the custody market and current regulatory settings, summarises insights from monitoring and misconduct reports, and identifies issues and risks for feedback.

We spoke with several firms and individuals before publication of this document[2]. A common theme we heard was the need to clearly define the problem before settling on solutions. The purpose of this paper is to identify issues and ask questions, rather than proposing options or solutions.

Why we are looking at custody services

Custody is largely unseen by the public, but it plays a critical role in protecting people's assets when they invest or make payments. Effective custody arrangements help safeguard client money and assets from fraud, operational failures, and insolvency. Where a custody regime is weak, these protections are reduced, potentially putting assets at risk.

Custody regulation in New Zealand is lighter and less developed than comparable overseas jurisdictions; yet our regime is also complex and fragmented, and obligations and oversight are uneven. We have seen that this can result in confusion, increased costs and poor conduct where firms don't understand their obligations. There is also duplication. When licensed firms appoint a custodian, they retain responsibility for oversight and compliance by the custodian and assume a quasi-supervisory role (e.g. a FAP outsourcing custody to an external custodian). This builds additional cost into the system that is ultimately met by clients.

Given these issues with the regime, we think it is worth considering whether efficiency and consumer protection could be improved by rationalising and streamlining the regime to:

- Ensure more information is available on entities providing custodial services
- Provide a single, clear set of obligations that apply for all custodians[3]
- Reduce complexity, overlapping obligations and dual supervision

[2] A summary of early feedback is on page 31.
[3] As with all regimes, specific tailoring or exceptions may be needed to recognise different sectors, sizes or types of firms or activities.

- Address the issues and risks identified in this paper – including regulatory gaps (such as lack of operational resilience and cyber security obligations)
- Future-proof the regime to allow firms to innovate and grow, and address risks arising from market developments and emerging technologies.

The current regulatory settings were introduced following the 2008 Global Financial Crisis and have not kept pace with market growth or change. Since then, the amount of money held in custody has increased substantially and more New Zealanders hold assets through custodial arrangements – particularly through KiwiSaver and other managed investment schemes (**MIS**). There were over 3.4 million KiwiSaver members as at March 2026[4]. KiwiSaver assets grew from $16.4 billion in March 2013 to $142.9 billion in December 2025[5]. With policymakers' support for increased contributions, these funds will likely continue to grow exponentially. More broadly, the total value of investment in MIS in December 2025 was $369.1 billion, up 13.1% since the previous year[6].

Investment options and market structures have also evolved. Retail platforms increasingly provide direct access to domestic and overseas markets, markets are more interconnected, and transactions occur faster. New technologies and business models – such as developments in payments and virtual assets – have introduced new custody arrangements and new risks, such as heightened cyber risk, that are not clearly addressed by current regulation.

Market structure also matters. A large proportion of client assets is ultimately held by a small number of wholesale custodians that are not regulated in New Zealand, raising concentration risk.

Why now

Strengthening protections for assets held in custody is one of the FMA's regulatory priorities for FY2025/26[7], and we have been increasing our focus on the custodial sector. This is important given increasing levels of assets in custody and exposure of client assets held in custody in unregulated payments and virtual assets areas.

In 2017 as part of its review of New Zealand's financial system stability[8], the International Monetary Fund (**IMF**) observed that there were weaknesses in New Zealand's custody services regulation. The report recommended that, within 1-3 years, custody services in the asset management sector should be licensed and supervised. This recommendation has not yet been addressed. IMF is due to complete a further review in 2027-28. It is likely that custody regulation will be a focus of this, which makes a review of custody regulation timely.

Reforms in the digital assets and payment services space are under active consideration in Australia and more recently in New Zealand. Custody of client funds held for payments and digital assets will need to be addressed as part of these reforms. This interlocking work makes now a sensible time to take a fresh look at custody regulation in New Zealand.

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[4] Datasets for KiwiSaver statistics | Inland Revenue
[5] KiwiSaver: Assets by sector (T43) | Reserve Bank of New Zealand
[6] Managed Funds Survey - Q4 2025 | Reserve Bank of New Zealand
[7] 2025 Financial Conduct Report | Financial Markets Authority
[8] New Zealand: Financial Sector Assessment Program -- Financial System Stability Assessment; IMF Country Report No. 17/110; April 10, 2017

Feedback sought

We welcome feedback on whether this paper identifies the key risks and issues associated with custody services in New Zealand, what aspects of the current regime are working well, where there are gaps or weaknesses, and what changes could strengthen the regulation of custody of client assets.

Market landscape

Traditional custody services and arrangements

Custody services support a wide range of investments and financial services, including MIS (such as KiwiSaver), investment advice services, investment platforms, lending platforms, and derivatives. While the arrangements differ, all involve holding or controlling client money or assets on behalf of investors.

- For retail MIS, a licensed supervisor is responsible for ensuring scheme assets are held appropriately. In practice, supervisors often appoint an external custodian. Scheme assets may include a wide range of asset types and are often held across multiple jurisdictions, which can require the use of overseas custodians and sub-custodians.
- For discretionary investment management services (DIMS), providers generally appoint an independent custodian to hold client assets, but may have an arrangement for a related party custodian approved as a condition on their licence. In that case, alternative controls to reduce conflict of interest risks are put in place. Custody arrangements may also sit within investment platforms that provide administration and reporting services alongside custody.
- In addition to custody arrangements within MIS and DIMS structures, there is a significant segment of custody services provided directly to retail and wholesale clients outside these frameworks. This includes custody associated with investment platforms, broking arrangements, and direct client portfolios. While comprehensive data on the size of this segment is limited, industry feedback indicates that assets held in custody outside MIS and DIMS may be material, and in some cases exceed the amount held within these structures. This highlights the broader role of custody services across financial markets and the importance of considering whether current regulatory settings appropriately capture the full range of custody activities.
- Custody arrangements for other financial services such as crowdfunding and peer-to-peer lending (and derivatives[9]) also commonly involve holding or controlling client money or property, either directly or through external custodians.

Across these services, custody arrangements can be complex and often involve multiple parties and legal structures.

Size and composition of the New Zealand custody market

The New Zealand custody market is diverse, ranging from a small number of large global banks holding significant volumes of assets to a long tail of small local firms that provide custody as part of broader financial services.

[9] This paper does not discuss custody of derivatives investor client money or property. There is a bespoke regime in Subpart 6 of Part 6 of the Financial Markets Conduct Regulations 2014 (**FMC Regulations**).

As at February 2026, there were 274 custody service registrations on the Financial Service Providers Register (FSPR). This breaks down into different types of custody registrations:

- Registered scheme custodians – 29
- DIMS custodians – 14
- Retail custodians – 125
- Wholesale custodians – 106[10].

Provider types and business models

Custody services are provided by a mix of trustee companies, specialist custodians, banks, and related party or nominee structures. Rather than operating as a standalone function, custody is often bundled with related services such as fund administration, registry, portfolio reporting, and trustee or supervisor services.

Where custody, administration and reporting are provided within the same group, integrated service models can blur functional and governance boundaries. This can create control gaps as one function may rely on another function to take certain action or assume another function will mitigate a risk. However, an integrated services model may result in some efficiencies. For example, it may be easier for a MIS manager to engage with an integrated supervisor and custodian (usually legally distinct entities) for certain matters.

As in other jurisdictions, multilayered custody chains are common, especially for managed funds. Each additional layer introduces complexity and can make effective oversight more difficult if roles, responsibilities and controls are not clear. Where sub-custodians are used, reliance on assurance reports[11] may not provide full visibility over all material risks. Assurance reporting may not cover control failures or emerging issues that sit outside the defined control environment, creating a gap in oversight and limiting ability to identify and address issues in a timely manner.

Role of wholesale custody in retail MIS investment

Retail MIS typically invest in wholesale funds through unit holdings, to achieve operational efficiencies and access overseas markets.

When retail MIS invest in wholesale funds, most custody risk sits at the wholesale level, where the underlying assets are held. As a result, retail investors may be indirectly exposed to risks that arise in wholesale custody arrangements. The supervisor of the retail MIS typically relies on look-through assurance reporting obtained from the wholesale custodian. Such reporting is generally provided pursuant to commercial contractual arrangements, which may constrain its scope and the level of direct oversight available.

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[10] Some firms are registered in multiple categories, and we do not have information on whether all those registered actively provide services. The names for the FSPR categories are not the same as the terms used in the FMCA. While the number of wholesale custodians registered on the FSPR is high, we understand most wholesale assets are held by a small number of large, international custodians.

[11] A custodian assurance report is an independent report prepared by a qualified FMC auditor that provides assurance on a custodian's systems, controls, and compliance with its legal obligations in holding client money or property, as required under FMC Regulations.

Market concentration

In some parts of the custody market, a small number of providers hold a large proportion of assets. As at June 2025:

- $246 billion of retail MIS assets in custody were held with about 10 custodians, with three large custodians holding direct or indirect title to around 80% of these assets.
- Of the $56.2 billion of retail funds held in custody in the DIMS sector, four custodians/business groups[12] managed 52% of these assets, with three of these managing 45% of total assets.

In the wholesale sector, we are aware that there is a small number of large offshore custodians ultimately holding a significant proportion of New Zealand client assets.

Concentration increases the potential impact if a major custodian experiences operational or financial difficulties, as disruptions or a failure could affect many investors at once. High concentration can also make it more difficult to transfer assets to alternative providers if a custodian fails, increasing the risk of delays and uncertainty for investors.

Cross-border custody and overseas assets

Many New Zealand investment schemes hold assets overseas. This means custody arrangements often rely on chains of overseas custodians and sub-custodians operating under overseas legal and market frameworks.

While New Zealand law requires retail assets to be held on trust and imposes conduct, reporting and assurance obligations on local firms, New Zealand regulators have limited ability to directly oversee the overseas entities that ultimately hold assets. In practice, protection of overseas assets depends on due diligence, contractual arrangements and assurance, rather than direct regulatory supervision. For retail MIS, ongoing monitoring of sub-custodians is primarily the responsibility of the appointed independent specialist custodian and is generally supported through assurance engagements over key custody and settlement controls. Although MIS managers and supervisors are involved in the establishment of sub-custodian arrangements, ongoing monitoring and settlement liaison are not typically performed directly by them and instead rely on the custodian's control framework and assurance reporting.

Overlapping obligations and supervisory complexity

Where a licensed entity outsources custody to a third-party custodian, the licensed entity retains responsibility and liability for obligations in relation to the safeguarding and administration of client assets under the New Zealand regime. It cannot step back once it has chosen and appointed an appropriate custodian; instead, it is required to supervise the custodian's performance and compliance. This creates a significant degree of overlap, with more than one party required to implement controls, monitoring arrangements, and accountability mechanisms. There is also an overlap with the role of the regulator.

[12] Made up of associated or related companies.

The costs of this duplication are ultimately borne by clients, either directly through higher fees or indirectly through reduced service efficiency, raising questions about whether the current regime is efficient.

Additionally, where a small, licensed entity, such as a small advice business, outsources custody to a large custodian, its ability to oversee the custodian and influence its behaviour will be minimal, meaning the advice business has liability without necessarily having effective control over provision of the service.

Custody regime

Regime shaped through incremental change

Custody regulation in New Zealand has developed incrementally rather than as a purpose-built regime. Early protections relied on trust law and corporate trustee models, with independence and fiduciary duties used to safeguard investor assets. This approach was formalised in the Unit Trusts Act 1960, which focused on requiring scheme assets to be held by an independent trustee rather than regulating custody as a service. As markets evolved and intermediaries increasingly held client money and securities directly, limitations in relying solely on trust law became apparent.

The Financial Advisers Act 2008 and supporting regulations introduced some modest conduct-based custody obligations, including segregation, reconciliation, reporting and independent assurance. When the FMCA was introduced, licensing of custodians was considered but ultimately rejected in favour of imposing obligations without licensing to achieve similar outcomes at lower cost – with oversight resting on those appointing custodians and on independent assurance requirements[13].

Subsequent reforms in 2021 shifted financial advice and broking (client money or property services) into Part 6 of the FMCA largely through a lift-and-shift exercise, rather than a fundamental redesign of the custody framework.

Overview of current regulatory settings

As discussed above, custody services themselves are not licensed in our regime[14] but custodians have rules they must comply with. These rules are complex and fragmented, with different parts of the FMCA and FMC Regulations applying depending on the investment sector concerned.

The client money or property services (**CMPS**) custodial services regime is in Part 6 of the FMCA and the FMC Regulations. Broadly speaking, the regime applies where someone is holding a financial advice product, or money received in connection with acquiring, holding or disposing of a financial advice product, in trust for a client[15]. However, there are many exclusions, and different levels of obligations apply depending on whether the service is wholesale or retail, and other factors.

Most elements of the CMPS custodial services regime are incorporated into the rules for DIMS custody. A separate regime applies for custody services for retail MIS under Part 4 of the FMCA.

Here is a very high-level overview:

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[13] Review of Securities Law Regulatory impact statements - February 2011 | Ministry of Business, Innovation & Employment

[14] One exception is that supervisors providing custody for a retail MIS must be licensed for their supervisor role (which includes custody and other functions).

[15] See definition of “custodial service” in s431W of the FMCA.

- **Registration**: All custodians and sub-custodians (retail and wholesale) must be appropriately registered on the FSPR[16] and, if they have retail clients, belong to a dispute resolution scheme. Licensing is not required.
- **Fair dealing**: FMCA Part 2 fair dealing obligations apply for all types of custody services (retail and wholesale).
- **High-level duties**: High-level conduct obligations (e.g. duty of care, diligence and skill) apply for CMPS custodial services (wholesale and retail).
- **Baseline safekeeping duties**: All custodians with retail clients[17] must hold client assets on trust and keep them separate from the custodian's own assets. This provides protection if the custodian becomes insolvent. Other obligations they have include record keeping and reconciliation, client reporting, and obtaining an independent annual assurance engagement of the custodian's systems and controls. This last obligation is a key requirement where a qualified FMC auditor will assess whether a custodian's systems and procedures are suitably designed to meet the relevant statutory obligations and are operating effectively.

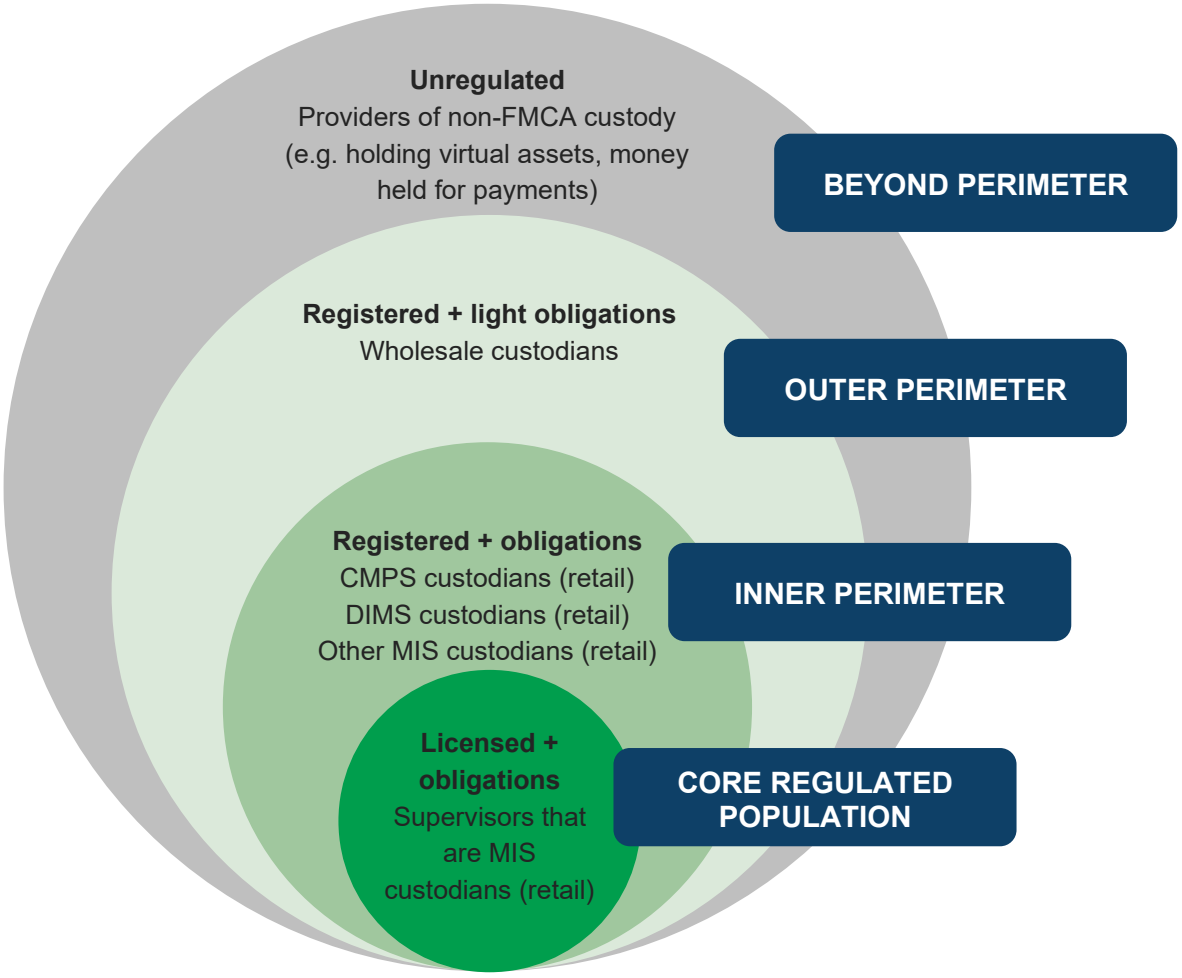
In general, appointing and supervising custodians is the responsibility of the appointing firm:

- For retail MIS, the licensed supervisor is the custodian unless custody is outsourced. A supervisor can outsource custody of scheme property to an independent custodian. For retail DIMS, the licensed DIMS provider must select an independent custodian (or a related party custodian if permitted in their licence conditions). In each case, the entity-appointed custodian must be appropriate to hold and safeguard the scheme property. The supervisor or DIMS provider is jointly and severally liable with the custodian they appoint for performance of the function.
- For CMPS custodial services under Part 6 of the FMCA, no independence or appointment criteria apply. However, a business outsourcing a custodial service to another person is treated as the provider of the service having the obligations and has a duty to ensure that person complies with regulatory requirements and will be held responsible if they fail to do so.

Further information on custody regulation can be found in the Appendix on page 32.

[16] For international custodians and sub-custodians an exemption may apply in some cases under the Financial Service Providers (Registration and Dispute Resolution) Act 2008, s7A.
[17] These duties also apply for some wholesale clients relying on their investment activity status (e.g. eligible investors) – see page 35.

The following diagram gives a high-level view of how custody services are regulated in New Zealand[18].



Licensing versus obligation-based regulatory regimes

Custodians in New Zealand are subject to legal obligations, but they are not licensed[19]. In many comparable overseas jurisdictions, licensing is required and is the main way regulators oversee custodians, manage risks, ensure consistency of practice and protect investors. When custody services are not licensed, regulators may face more limits on what they can do. This can weaken oversight and increase risks for investors.

Key consequences of not having a licensing regime may include:

- **Weaker oversight**: Regulators may have more limited ability to supervise firms on an ongoing basis, meaning issues may be more likely to be identified only after harm occurs.
- **No entry screening**: Firms may be able to enter and operate without checks on capability or resourcing, increasing the risk of unsuitable providers.

[18] This does not include regulation of custody for peer-to-peer lending, crowdfunding or derivatives issuers
[19] Except for supervisors

- **Blunt intervention tools**: Regulators may have fewer proportionate options to address issues early, which could increase the risk of delayed or disproportionate action.
- **Reduced visibility**: Regulators may rely more on complaints and self-reporting, which could increase the possibility that risks go undetected.
- **Higher investor risk**: Consumers may face weaker protections, greater fraud risk and more limited access to redress.
- **System-wide risks**: A large unlicensed sector may undermine confidence in the regulatory system and create risks that are harder to identify and manage.

On the other hand, licensing regimes may impose costs on firms that might act as a barrier to entry for smaller entities, or see increased costs passed on to clients. There can be mitigants for this such as:

- Deemed licences being granted for entities that have already been recognised as meeting the required standard or recognition of overseas licences
- A streamlined, proportionate risk-based application process that avoids highly prescriptive criteria or assessment
- A scaled approach to entry criteria, licence conditions and ongoing obligations, to take account of the size and nature of an applicant and its activities, and the risk it poses.

There might also be some efficiencies that can be identified where licensing removes the need for other obligations to apply. For instance, the need for an appointing entity (e.g. a FAP outsourcing custody to a custodian) to supervise the custodian it appoints could be removed if a custodian is licensed and supervised by the regulator.

Comparing New Zealand regime with international regulation

Although New Zealand is broadly aligned with comparable overseas jurisdictions on baseline safekeeping obligations, it appears to have more limited regulatory oversight and intervention tools for custodians than some comparable jurisdictions.

Most overseas jurisdictions require custodians to be licensed or authorised, and impose obligations that require a regulated entity to have organisational capability to operate safely and reliably (i.e. obligations around operational resilience, outsourcing controls, cyber security, and minimum financial resources).

For example:

- In Australia, custodians generally require an Australian Financial Services (**AFS**) licence with a custodial or depository authorisation. AFS licensees authorised for custodial/depository services are subject to minimum standards relating to organisational structure, adequate staffing capabilities and having adequate capacity and resources to perform core administrative activities[20].
- In the UK, firms holding or controlling client money or assets in custody require Financial Conduct Authority (**FCA**) authorisation and are subject to the Client Assets Sourcebook (**CASS**), plus UCITS/AIF depositary regimes for relevant managed funds. These firms must meet and continue to comply with

[20] See Regulatory guide 133 | Australian Securities & Investments Commission

mandatory threshold conditions, set out in COND 2 of the FCA Handbook[21]. These include requirements covering being capable of effective supervision, having appropriate resources, fit and proper obligations, and having a sound business model. Firms must have sufficient financial and operational resources – including capital, skilled personnel, robust systems, and effective risk and compliance controls – to operate soundly, meet client obligations, and withstand financial and operational stress.

As noted on page 28, some overseas jurisdictions have extended custody regulation to address custody of virtual assets and client money held by payment service providers. Our New Zealand CMPS custodial services regime only covers custody of financial advice products[22] and client money received relating to buying, selling, or holding those products.

[21] FCA Handbook | Financial Conduct Authority
[22] See definition of "financial advice products" in FMCA, s6.

Custody failures, monitoring, and examples of poor conduct

Custody failures

There have been some significant custody-related custodian failures in New Zealand that resulted in loss of client funds or delayed the return of client assets.

- Ross Asset Management Limited collapsed in late 2012 after investigations identified serious concerns about the existence and custody of client assets. The FMA obtained court orders freezing assets and appointing receivers, and worked jointly with the Serious Fraud Office (**SFO**), which subsequently prosecuted David Ross for operating what was found to be New Zealand's largest Ponzi scheme. David Ross was convicted and sentenced in November 2013. The case revealed a fundamental structural weakness: David Ross exercised both discretionary control over client portfolios, and custody of client money and assets, enabling the prolonged concealment of losses and fictitious returns. Investor losses were ultimately estimated at over $100 million, with recoveries amounting to only a fraction of amounts believed to be invested.

  The case directly informed subsequent regulatory changes requiring independent custody arrangements for DIMS, embedding separation of control and custody as a core safeguard for client assets.
- Barry Kloogh was a financial adviser who exploited both the trust and goodwill of his clients, and weaknesses in the regulatory regime to run what amounted to a Ponzi scheme. This included arranging fictitious external investments to be entered and reported on via third-party wrap platforms, holding out bank accounts as those of the custodians, and intercepting client reporting of funds legitimately held in custody to defraud his clients. Nearly $16 million was misappropriated from clients[23]. In October 2023, we published a report on findings from our inquiries, and asked MBIE to consider whether the regulatory settings for custodians in New Zealand should be reconsidered, including whether potential harms in this area indicate that increased regulation, such as licensing, is required.[24]
- In the case of licensed derivatives issuer Halifax New Zealand, client money was not properly segregated. Funds were mixed across clients, platforms, and related companies in New Zealand and Australia. When the Halifax group collapsed in 2018, it was not possible to clearly identify individual entitlements. As a result, client funds had to be pooled and distributed proportionately, delaying clients' access to money.
- Weak custody arrangements have also been exposed through cyber security failures. In 2019, the unregulated cryptocurrency exchange Cryptopia was hacked, resulting in the theft of about $30 million worth of cryptocurrency. The firm entered liquidation in May 2019. Although some distributions have since been made, the liquidation process has been lengthy and is still ongoing.

[23] Investment Fraud | Serious Fraud Office
[24] Lessons learned from Barry Kloogh Ponzi | Financial Markets Authority

- Poor governance and record-keeping has also led to investor losses. Digital Asset Exchange Ltd (trading as 'Dasset') operated an unregulated cryptocurrency trading platform in New Zealand, allowing users to buy and sell cryptocurrencies (digital assets) using New Zealand dollars. Dasset collapsed in 2023 after serious weaknesses were identified in how client assets were recorded and managed. Liquidators found that most investor assets could not be accounted for, affecting around 5,000 people. An investigation by the Serious Fraud Office is ongoing.

Recent monitoring of custody services

As signalled in our 2025 Financial Conduct Report[25], oversight and provision of custody services has been a key supervisory focus this financial year. We have assessed:

- how licensed supervisors have responded to the findings from our 2019 thematic review of MIS custody arrangements (see below), including whether they have reviewed custody functions delegated to MIS managers or administrators and their oversight of outsourced custody arrangements
- how licensed DIMS providers and financial advice providers (**FAPs**) oversee outsourced client money or property handling. Where they hold client funds directly, we have also been evaluating the robustness of their own processes.

MIS supervisors

In December 2019, we published a thematic review that we commissioned into MIS custody, which found retail scheme assets are, with very few exceptions, being held appropriately in custody. It did not suggest that client money is currently at risk but noted some practices that could be improved to strengthen the safeguarding of client money.[26]

We conducted a review of licensed MIS supervisors' custody arrangements this year, focusing on how supervisors meet their custody responsibilities, including their oversight of outsourced or delegated custodial functions and their response to the improvement areas highlighted in the 2019 thematic review. The assessment covered a range of custody models, asset classes, and oversight approaches. Overall, we found no material weaknesses in supervisors' custody arrangements or oversight practices.

The following observations describe prevailing practices, providing insight into how oversight mechanisms operate in practice and the multiple layers of control and assurance involved. They do not indicate gaps or deficiencies; rather, they reflect that effective oversight is inherently complex and depends on a combination of controls, assurance frameworks, and third-party inputs.

- Retail MIS exposure to wholesale assets is indirect via registry-held units, with custody assurance supported by reconciliation controls, layered governance (where applicable as wholesale trustee), due diligence on custodians, and reliance on external assurance reports.
- For certain assets, such as over-the-counter derivatives, custody objectives are typically met through the supervisor remaining a direct contractual counterparty under ISDA Master Agreements, including associated Credit Support Annexes (CSAs), with collateral management responsibilities operationalised

[25] 2025 Financial Conduct Report | Financial Markets Authority
[26] Thematic review of MIS custody arrangements | Financial Markets Authority

via tri-party arrangements. Another example is private assets held within a trust structure e.g. direct property, loans and equity including shareholder agreements.

- Supervisors appoint specialist custodians – typically large global institutions – and apply an oversight framework that includes independent due diligence (including legal review), reliance on assurance reports for ongoing monitoring, and structured recurring engagements. Where custody functions are not fully outsourced, supervisors rely on independent assurance reports, and for delegations of limited operational functions, the associated risks are managed through ongoing supervisory oversight and quarterly attestation from MIS managers.
- Audit firms may apply differing methodologies when assessing custodial controls. Such variability can reflect the exercise of professional judgement within relevant assurance and auditing standards; however, all approaches are expected to be supported by sufficient and appropriate evidence in line with those requirements.

DIMS providers and FAPs

We also undertook monitoring of selected licensed FAPs and DIMS providers, with a focus on client money and property services. We assessed the entities' oversight of third-party providers, governance and controls, record keeping, custody reporting, and disclosure of fees.

We saw some examples of weak oversight when custody is managed in-house. Risk management and governance arrangements did not always encompass client money and property services. Some entities using a third-party provider did not appear to do sufficient due diligence to ensure the services were effective and compliant, both initially and on an ongoing basis. We also saw examples of poor understanding about who retains obligations when using a third-party custodian, and lack of ongoing oversight of custody providers.

Good practices included firms having constructive relationships with custodians that enabled them to suggest improvements to their services, and encouraging uptake of client portals to improve clients' ability to review their portfolio and access independent custodial reports.

We will be publishing our monitoring insights later this year, outlining our observations and expectations for the FAP and DIMS sectors to ensure appropriate protections are in place.

Examples of poor conduct

This section summarises recent instances of poor conduct we have identified that present a risk of harm to clients; in some cases, we are still considering the conduct, and may take proportionate action in response where client harm has occurred. The conduct includes failure to segregate assets held in custody, apparent fraud, not obtaining an assurance engagement, failing to report to investors, and failure to exercise due care diligence and skill contributing to loss of client assets. Some of the conduct has been identified by FMA monitoring that has not yet been finalised.

This conduct relates to failures to comply with the current regime. However, some of these examples also demonstrate the need to streamline and simplify the regime to clarify obligations and improve visibility and oversight of custodians.

- **Small unregistered firm with no assurance engagements**: A small firm acted as a custodian for some clients without being registered and without required annual assurance from an independent

auditor. There were instances where client funds appeared to be commingled with the firm's funds and later transferred.

- **Assurance engagement found key failures**: A firm that offered a range of services including custody received an adverse assurance engagement opinion due to non-compliance with baseline safekeeping duties:
  - assets in custody not segregated
  - lack of evidence that appropriate reviews, reports and reconciliation were completed.
- **Significant reporting failure**: System errors at a custodian resulted in clients not being sent six-monthly custody reports about their investments for several years. This reporting provides the investor with an independent verification of their holdings, separate to the reporting they might receive from a DIMS provider, financial adviser, or retail investment platform.
- **DIMS custodian assurance engagement deficient**: The law requires a custodian to have an annual control assurance engagement, which must include objectives about proper management and oversight of sub-custodians. However, the custodian failed to include these objectives in the audit scope, meaning the audit report did not address whether the sub-custodian was managed or monitored.
- **DIMS provider failed to appoint independent custodian**: A licensed DIMS provider appointed an associated person as custodian in breach of the law, as there was no condition on its licence permitting use of a related party as a custodian.
- **Peer-to-peer lending platform custodian did not obtain required assurance engagements**: A custodian for a peer-to-peer lending platform did not obtain the required annual assurance engagements for five years running. The reason for the failures appeared to be that it was unaware that it was a custodian and therefore that it needed to comply with this obligation.
- **Employee fraud**: Unallocated funds on a retail investment platform were stolen by an employee through fraud. The employee exploited processes they were directly responsible for overseeing. Their role and system access allowed the employee to manipulate internal controls and carry out unauthorised transactions without immediate detection.

Key issues and risks

We have identified several features of the current regime that may pose risks to the safeguarding of client assets. In this paper, we are seeking feedback on whether these risks and issues are present in the market and, if so, which sectors or activities are affected. We are not proposing reform options or solutions at this stage, but we invite views on how any identified issues or risks might best be addressed, while recognising solutions might be different for different issues. We also recognise that different risks, structures and activities are relevant across various sectors. To avoid unnecessary complexity, we have taken a high-level approach in this paper. However, we encourage submitters to distinguish between sectors and activities in their feedback, where relevant.

Complex, fragmented and uneven

Although described as 'light and underdeveloped'[27], New Zealand's custody regime is also complex, fragmented and uneven.

Requirements for custody are spread across various provisions of the FMCA and FMC Regulations. This makes interpretation difficult, raising uncertainty and increasing compliance costs[28].

For example, under CMPS custodial service regulation, outsourced custody providers are not regulated. Instead, regulation and liability under the regime sit with the business that has contracted with the client. This has led to confusion in the market about who is responsible, due to the number of parties or entities that can be involved in a transactional chain. For instance, there may be a client, then a financial adviser, along with other intermediaries such as a wrap platform, a provider, and a custodian. In some cases, the intermediaries involved may dispute who is legally responsible. If it is unclear who is responsible for complying with the law, this increases risk for clients.

Complexity can lead to non-compliance when market participants don't understand their obligations. Earlier in this paper we identified some examples of poor conduct where participants did not understand their obligations (see pages 18-19). Complexity can also increase compliance costs as businesses may undertake unnecessary compliance activity or require legal advice to understand the regime and manage regulatory risk.

The custody regime is also uneven. The rules that apply for custody services depend on the legal form of the investment, meaning investors may have different protections or risks even when they ultimately invest in the same products and have the same economic exposure.

[27] See post by Cygnus Law: Updated FMA guidance for custodians (31 July 2024)
[28] Lengthy guidance has been issued to help market participants navigate the regime: Guide for providers of client money or property services | Financial Markets Authority

Case study: Comparing investor experiences

Scenario: Anna and Ben both want to invest $10,000 in a mix of equities. Anna invests indirectly through her bank's global equity fund (a retail MIS), while Ben chooses a direct investment on a retail investment platform.

Anna's investment: Anna invests as a member of a scheme. Her assets are held by an independent custodian that is 'appropriate to hold and safeguard the scheme property' and selected by the licensed supervisor. The custodian must hold Anna's assets on trust separate from its own assets, conduct regular reconciliations, and obtain annual assurance on its processes. The licensed supervisor (which is in turn supervised by the FMA) has oversight of and is responsible for the custodian's compliance.

Ben's investment: His assets are held by the platform custodian. No independence or other criteria apply to the custodian's appointment. The custodian must keep Ben's assets on trust and separate from its own assets, conduct regular reconciliations, and obtain annual assurance on its processes. However, there is no oversight of the custodian or the retail platform (which is unlicensed). Ben's assets could be at greater risk, including from potential conflicts of interest.

This example highlights how the legal form and investment route affect the level of regulatory protection, with investment through a retail MIS offering more protection in terms of custody than investment through a retail investment platform.

Simplifying and streamlining regulation for all types of custody with a single regime would create greater certainty, reduce compliance costs and reduce the risk of inadvertent non-compliance.

Question 1: Recognising that there are different legal structures in the different sectors in the custody market, do you think the custody regime is complex, fragmented and uneven? Please explain the reason for your answer.

Limited oversight, intervention and enforcement tools

Acting as a custodian is a market service under the FMCA[29]; however, it does not require a licence. Because there is no licensing requirement, oversight depends more on the licensed entity responsible for appointing the custodian (where relevant) and commercial agreements than would be the case with a licensing regulatory model.

[29] See "market service" as defined in s 6(1) of the FMCA. Note that an entity providing custody may (or its related company may) hold a licence for a different financial service (e.g. licensed derivatives issuer, licensed DIMS provider or licensed FAP).

The obligations-only regulatory model reduces the information available for supervision of custodians. Information about a custodian is not obtained during a licensing process or ongoing supervisory relationship. Unlicensed entities are not required to complete annual regulatory returns, which provide valuable insights about the licensed population and its activities.

This model also reduces options for influencing behaviour and enforcement. There is no power to impose licence conditions, and tools such as censure, action plan, and licence suspension and cancellation are not available. This may lead to delayed detection of non-compliance, and less proportionate and nuanced regulatory responses to poor conduct.

However, there are some benefits from an obligations-only regulatory model. This model can support flexibility, innovation, and lower compliance costs by avoiding prescriptive entry requirements and allowing firms to tailor their compliance to their business model. It places responsibility on the market to achieve appropriate outcomes, rather than focusing on adherence to detailed rules, and may be more adaptable to evolving markets and technologies. However, these benefits depend on effective governance within firms, visibility and strong enforcement mechanisms.

Assurance engagements

The requirement for an annual assurance engagement over a custodian's systems and controls provides independent testing to assess whether those controls are well designed and functioning effectively. We have been told that in practice (particularly in institutional custody arrangements), assurance can operate as an ongoing supervisory mechanism embedded in governance and contractual arrangements, providing disciplined, iterative calibration of the control environment.

However, while assurance engagements provide valuable information for the supervision of custodians and are a key protection under the regime, they may not be an adequate substitute for the ongoing regulatory oversight that a licensing regime offers. Assurance engagements are time-bounded, limited in scope, and may not be sufficient to support comprehensive second-line risk oversight. Specifically, the engagements may not provide assurance over broader risk areas such as non-financial risks, and the use of the 'carve-out' method may exclude key downstream services from the scope, resulting in significant controls sitting outside the ISAE 3402 report (the report provided as part of the assurance engagement).

Question 2: Assurance engagements may increase trust and transparency through independent verification of a custodian's systems and controls. To what extent do assurance engagements provide an effective substitute for ongoing regulatory oversight?

Question 3: What regulatory model is most appropriate for the oversight, intervention, and enforcement of custodians in New Zealand (for example, an obligations-only model, a licensing model, a combination of both, or something else)? Please explain your reasoning. Could any of these models have unintended consequences for other regulatory or non-regulatory settings or arrangements in the market?

Question 4: Should regulatory settings for custodians differ across market segments or types of custodial activity (for example, between retail and wholesale activities, or between different types of custody providers or activities)? If so, how and why?

Independence

There are gaps in the custody regime in relation to conflicts of interest. A custodian for a retail MIS or DIMS is required to be independent[30]. However, independent custody is not required for CMPS retail custody or wholesale custody and certain other types of custody[31].

Lack of independence is a risk because it weakens a core safeguard designed to protect investors. Independent custody separates asset holding from asset management, reducing conflicts of interest and ensuring the custodian can act solely in the interests of clients. Where a custodian is a related party, commercial or group interests may compromise its willingness or ability to challenge instructions, identify breaches or escalate concerns, increasing the risk of errors, misconduct, or fraud going undetected. Concentration of functions within one group can also reduce segregation of duties, impair transparency and reporting, and make asset records harder to verify. In stress or failure scenarios, this may make it more difficult to isolate, transfer or recover client assets. Overall, lack of independence undermines investor confidence and diminishes the effectiveness of custody as a protective control within the regulatory system.

In some retail MIS arrangements, supervisors may delegate certain operational custody functions – such as settlement or record-keeping – to the fund manager or entities within the same group. Where the manager also performs fund administration functions, this can result in a concentration of roles that weakens effective segregation between asset management, administration, and custody. While legal responsibility for custody remains with the supervisor, this degree of functional integration may reduce the practical independence of custody as a safeguard, increasing the risk that errors, conflicts of interest, or control weaknesses are not identified or escalated in a timely manner.

Question 5: How are conflicts of interest dealt with currently in the market and is this effective to protect client assets? If not, how could the regulatory settings be improved?

Gaps in regulation and oversight of wholesale custody

A large proportion of New Zealand retail investors' assets are ultimately held in wholesale investments. This means a significant part of the actual custody risk lies with custody of the assets of the underlying wholesale funds (typically equities and debt securities).

Custody for (institutional) wholesale clients is largely unregulated in New Zealand. This is not unusual. Regimes often regulate wholesale services differently from retail services due to differences in investor capability, market structure, and the availability of existing safeguards. Retail investors typically rely on regulatory protections, including prescriptive requirements such as asset segregation, trust structures, and independent oversight (e.g. through supervisors). By contrast, wholesale investors are generally more sophisticated and able to negotiate contractual protections, and custody arrangements in this segment often rely on market discipline, institutional governance, and offshore regulatory frameworks.

[30] An exception is where a DIMS provider is permitted by its licence to appoint a related party as custodian. However, in this case, alternative conditions will be imposed to ensure functional independence, risk mitigation, and equivalent investor protection.
[31] Independence is not required for custody by crowdfunding and peer-to-peer platforms, and derivatives issuers.

While custody for (institutional) wholesale clients is largely unregulated in New Zealand, offshore global custodians will usually be licensed overseas and protections may also exist under trust deeds and contractual arrangements, and overseas regulation.

The FMA has very little sense of the size, structure, practices or risks in the wholesale sector. Wholesale custodians have no New Zealand law requirements to hold assets in trust or segregated from their own assets. While we understand anecdotally that wholesale funds are typically established under a unit trust structure and their trust deeds would generally stipulate that underlying investments should be held with a specialist custodian, this is a matter of business practice and not a regulatory requirement.

Prime brokerage arrangements can create additional risks in wholesale custody settings. In these arrangements, prime brokers may provide integrated execution, financing, and custody services, and can reuse or substitute client assets (for example through rehypothecation). While this can support efficient trading and financing, it may mean that specific assets are not held directly or continuously for the fund. As a result, when a wholesale fund manager seeks to withdraw or transfer assets, there may be delays, reliance on the prime broker's ability to return equivalent assets, and increased operational and counterparty risk, particularly in stressed conditions.

Institutional wholesale custody services are generally provided by overseas global custodians that are typically well resourced, and, as noted above, licensed and supervised in their home jurisdictions. This provides some confidence that client assets will be safeguarded. There may also be some oversight from MIS supervisors where retail MIS are investing into wholesale funds where the supervisor also acts as wholesale trustee.

However, wholesale custodians are not subject to direct regulatory oversight in New Zealand. There is a risk that their systems may be designed for larger offshore markets and do not adequately accommodate New Zealand-specific legal structures or requirements. Also, the use of layered sub-custodial arrangements can further dilute effective oversight and make it harder for New Zealand managers or supervisors to independently verify assurances provided by overseas entities.

These risks are compounded by prioritisation and enforceability challenges. New Zealand assets may represent only a small proportion of a global custodian's overall business, creating a risk that New Zealand-specific issues are not prioritised and sufficient resources will not be allocated to investigate or remediate problems if they arise. In the event of operational failures or misconduct, differences in legal frameworks, contractual terms, and jurisdictional boundaries may limit New Zealand regulators' ability to intervene quickly or secure timely remediation or compensation, particularly where custodians are unlicensed and only lightly regulated in New Zealand.

Question 6: What, if any, regulatory requirements should apply to wholesale custody in New Zealand? Please explain the reasons for your answer.

Question 7: Could there be any unintended consequences for investors or financial markets in New Zealand if additional requirements were imposed for wholesale custody?

Minimal entry conditions

The current regime does not set universal or standard entry conditions or require a regulator check for custodians entering the market. Despite the complexity and importance of the custody role, responsibility for vetting a custodian falls to those appointing the custodian. For DIMS, the licensed DIMS provider must

appoint a custodian. For retail MIS, the licensed supervisor has responsibility for appointing a custodian unless the supervisor holds the scheme property itself. In each case, the custodian appointed must be independent and considered appropriate to hold and safeguard the relevant assets. Supervisors carry out independent due diligence when appointing a custodian for a retail MIS.

Otherwise, there are no regulatory controls on who takes on a custodian role. The current settings create a risk, particularly for small or start-up custodians that may lack the scale, structure, systems (including technology) and skills to separate and protect assets, and implement effective conflict of interest management and controls.

Question 8: Do current settings adequately ensure that custodians are capable of effectively performing their role? Please provide reasoning for your answer. Does your answer differ depending on the market sector?

Question 9: Should custodians be subject to minimum entry standards (for example, governance, capability, systems, and controls), and should these standards vary at all by size, client type, or services provided?

Financial resources

Custodians are not subject to financial resource or insurance obligations, and there is no assessment of their financial resources (or insurance) through a licensing process[32]. For large custodial businesses this creates risk, given the complexity of a custody operation, the cost of the systems, processes and resources required to operate effectively, and the high operational exposure to risk of financial losses. Even where client assets are protected from a custodian's insolvency through trust and segregation requirements (which may not be the case for wholesale custodians), the failure of a large custodian can still create significant risks and disruption for investors and markets. These include the risk of delays in accessing assets, difficulties in reconciling records, and uncertainty while assets are transferred to a replacement custodian. Operational failures can result in loss or corruption of data, errors in asset registers, and breakdowns in reporting and corporate action processing, which may require time-consuming and costly remediation. In the absence of adequate financial resources or insurance, a custodian may be unable to fund remediation, absorb operational losses, or support an orderly wind-down or transition, increasing the risk that costs are ultimately borne by clients or other market participants.

Question 10: Do custodians have sufficient financial resources or insurance in place to mitigate the risks referred to above? If necessary, distinguish between different sectors of the custody market.

Question 11: Should custodians, or some types of custodians, be required to maintain minimum financial resources and/or insurance? Please explain the reasons for your answer.

[32] Some custodians may hold other licences relating to other services that means they are subject to financial resources or operational resilience obligations (e.g. registered banks or licensed supervisors). Overseas custodians may also be subject to requirements in their home jurisdiction.

Business continuity and operational resilience

Custodians have no business continuity or operational resilience obligations[33], yet operational resilience in custody services is essential for protection of client assets and financial market stability. Cyber risk is an increasing threat, particularly with the rapid rise of artificial intelligence, and weaknesses can disrupt client transactions, damage trust, and undermine confidence in market services. Custodians (particularly MIS custodians) operate in a high-risk operational environment due to high volumes of daily transactions, range and complexity of assets (sometimes held in multiple jurisdictions), complexity of systems and processes, and high levels of manual intervention to perform key processes. Failure of a large custodian would significantly impact clients due to complex data, reconciliation and regulatory challenges. The concentrated custodian market and lengthy customer transition period (which could be up to three years[34]) mean that adequate operational risk settings, and regulatory oversight of these, is important[35].

This compares with requirements for FMCA licensed market service providers (which usually do not even hold client assets) where operational resilience is assessed at licensing and licence conditions require the licensee to have a business continuity plan appropriate to the scale and scope of its service, ensure critical technology systems are operationally resilient, and notify the FMA of material incidents.

Question 12: Do custodians have adequate operational resilience arrangements to protect clients during disruption events or cyber-attacks, including ensuring continuity of service and the ability to transfer assets to an alternative custodian in a timely and orderly manner?

Question 13: Should operational resilience, cyber security, incident reporting and business continuity obligations apply to custodians? Please explain your reasoning.

Concentration risks and regulatory gaps in ancillary services

Businesses related to custody services, such as online investment platforms, wrap platforms and fund administration and registry services, play a significant role in the market. While risks in these services are not custody-specific, the combination of high market concentration and limited regulatory oversight may create vulnerabilities that could affect custody clients, including vulnerabilities from fraud or cyber risk.

For example, operational errors, system outages, business continuity events or cyber-attacks affecting a fund administrator that services a large proportion of the market could have widespread impacts on investors including:

- delays or restrictions on timely access to assets
- administrative errors impacting the calculation and/or distribution of assets
- exposure of personal information.

[33] See footnote 34 above
[34] For example, see NAB to shutter custody business | Investor Daily
[35] We have been told there have been difficulties in the market in transferring clients from an existing provider to a new provider within a reasonable timeframe in a business-as-usual scenario. In that context delays can inhibit switching and weaken competitive pressure.

If material disruption were to affect an investment platform, wrap platform or fund administrator, transfer of services to alternative providers may be necessary. However, this process may be complex and subject to delay, particularly in a concentrated market, potentially amplifying the impact on investors.

Existing outsourcing controls – such as those assessed through FMCA licensing of market service providers and required under standard licence conditions – may not be sufficient to mitigate these risks where services are outsourced to large providers.

Question 14: Do concentration risks or regulatory gaps relating to platforms, wrap platforms, and fund administration warrant additional oversight or further consideration? How might these risks or regulatory gaps be mitigated or addressed?

Emerging issues

Technology and innovative financial products and services have outpaced aspects of the financial markets regulatory framework, including custody. Regulatory gaps create risks for consumers who are increasingly seeking access to new technology and innovative financial products and services. Regulatory uncertainty also acts as a barrier to entry for new products and services.

Through our feedback on our *Tokenisation in Financial Markets* consultation,[36] our regulatory sandbox for innovative products, services or business models, and ongoing market engagement, we have heard from parts of the financial services sector that clearer regulatory pathways for payment service providers (**PSPs**) and virtual assets would better support innovation and deliver benefits for businesses, markets, and consumers.

Through this paper we are seeking feedback on custody-related risks; broader questions about the regulatory treatment of these products and services fall outside its scope.

Payment services

Payment services are emerging as an area of innovation, focusing on improving the way New Zealand consumers and businesses buy goods and services, pay bills and staff, and receive income.

PSPs typically provide the following types of services:

- **Payment facilitation**: Helping people and merchants make or receive payments, processing domestic or cross-border money transfers, or enabling a payment to be initiated from a customer's account through an app or API (application programming interface). This includes supporting services like currency conversion and payment gateways. Customer funds are not necessarily held for long periods.
- **Stored value facilities**: Providing a way for customers to hold money for future payments (e.g. paying merchants or currency conversions), such as through a digital wallet or e-money account, or through tokenised forms of value like stablecoins.

[36] Submissions report: Tokenisation in financial markets | | Financial Markets Authority

Unlike some comparable overseas jurisdictions[37], New Zealand does not have a dedicated payment services regulatory regime. As a result, the default settings of the FMCA may not provide suitable protections for custody of assets that are related to payments rather than investments.[38]

MBIE published a consultation on payment services regulation in May 2026[39]. We provided advice and support in the preparation of that document and, once submissions close, will work closely with MBIE on next steps. This discussion paper does not seek to duplicate MBIE's payment services policy work. We are interested only in custody or safeguarding issues that may arise where payment service providers hold, control, or arrange for the holding of customer funds. If you have provided feedback on MBIE's payment services regulation paper, you do not need to raise the same points in response to this paper; we will incorporate all relevant feedback from MBIE's consultation into our consideration of custody settings.

Question 15: What custody-specific risks and safeguards should be considered where payment service providers hold, control, or arrange for the holding of customer funds or other customer assets, and should regulatory protections apply?

Virtual assets, financial services and financial products

Virtual assets and blockchain technology are increasingly changing the global financial markets landscape, including how certain products and services can be offered, traded, exchanged, and held in custody. These developments are blurring traditional boundaries between financial products and non-financial assets, and between intermediated and disintermediated market structures.

For example:

- Exposure to virtual assets (such as Bitcoin) is increasing offered by financial products such as exchange traded funds or managed funds, which rely on safe and secure custody of those underlying virtual assets (which are not financial instruments). Overseas, this type of custodial service is commonly provided by major custodial businesses.
- Some traditionally issued financial instruments, such as bonds or money market funds, are being bundled in tokenised wrappers, while others are being issued natively on-chain.[40] This allows trading on-chain and exchange for other virtual settlement assets (such as stablecoins).
- Digital payment tokens, particularly those that are asset-backed and redeemable for a fixed value, are raising similar governance challenges to deposit and managed fund products, including in relation to custody, liquidity, and operational resilience.

There are also regulatory gaps for both businesses and consumers in terms of how the exchange of virtual assets is treated. Virtual asset platform models range from those that resemble a centralised exchange, to

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[37] For example, in the UK PSPs must be authorised or registered with the Financial Conduct Authority under the Payment Services Regulations 2017 (and the Electronic Money Regulations 2011 where relevant), and comply with conduct, safeguarding, security, and financial crime rules. In Australia, proposed reforms, if enacted, will modernise the regulation of PSPs through a technology-neutral, activity-based licensing framework, with new rules applying to businesses that facilitate money transfers, operate stored value facilities or provide digital wallets.

[38] There are other legal obligations, such as under the Trusts Act 2019, Fair Trading Act 1986 (where applicable), and the terms of any deed and contract relating to the product or service that apply.

[39] Discussion document on payment services regulation (May 2026) | Ministry of Business, Innovation & Employment

[40] For example, Circle Internet Group offers a fully on-chain tokenised money market fund that delivers yield-bearing collateral with near-instant redemption in USDC (a stablecoin).

broker/dealers, to decentralised finance. Alongside these are a variety of self-custody and third-party custody solutions, which the current law does not contemplate.

Providers holding these assets can often fall outside the scope of core custody rules, as many types of virtual assets are not 'financial advice products' under the CMPS regime.[41] This is an emerging area; whether virtual assets are captured as 'financial advice products' under current regulation, and consequently how custody frameworks apply, is not always clear.

However, where a particular virtual asset is not a financial advice product there are no statutory obligations under financial markets law to hold the asset or client money on trust or to segregate them from other assets or money of the platform or custodial service.

There are unique custody risks associated with virtual assets that may not be addressed through current requirements – for example, risks associated with losing private keys (and consequently the virtual asset) permanently, particularly in the event of a platform or wallet provider's insolvency, make recovery much more difficult.

Other risks are associated with tokenised assets, where there can be on-chain custody risk (how the token is held) and off-chain custody risk (how the underlying asset is held). Differences in how these assets are held and dealt with can lead to reconciliation challenges, particularly if linkages between the on-chain and off-chain assets are weak.

The pace of change in New Zealand is slower compared to some overseas jurisdictions, in part because current regulatory settings are not fit for purpose for this new technology, but also due to the size, scale, and depth of our markets. However, as noted earlier in this paper there have been some significant virtual assets custody failures in New Zealand (see page 16).

The need for reform of custody of virtual assets has been raised previously in New Zealand. In 2021 the Finance and Expenditure Committee launched an inquiry into the current and future nature, impact, and risks of cryptocurrencies. Recommendation 5 of the report provided:

> *We recommend that the Government direct the Ministry of Business, Innovation and Employment (MBIE), in consultation with the FMA and the industry, to use its regulation-making powers to add a defined class of digital assets which are used for investment purposes as a new category of "financial advice product" (but not, to be clear, a new "financial product") to bring them into the regulated financial advice and client money–client property services regimes*"[42].

Question 16: What specific custody risks arise from tokenisation and other virtual assets, and what baseline safeguards would be most effective and proportionate in New Zealand?

[41] See full definition of 'financial advice product' in FMCA, s6(1). This term includes financial products as well as consumer credit contracts and contracts of insurance.
[42] August 2023 Report of the Finance and Expenditure Committee on Inquiry into the current and future nature, impact, and risks of cryptocurrencies

Final comments

We have identified potential risks in the current regime and are seeking feedback on whether these are present in practice and which sectors or activities are affected. We are not proposing solutions at this stage, but invite views on how any issues might be addressed. We also recognise that any reform has costs and comes with trade-offs. The questions below invite your feedback on anything not covered by the previous questions, including any potential consequences of reform generally or specific reforms.

Question 17: Do you have any feedback on any consequences or other relevant information or matters that should be considered in relation to any reform of custody regulation?

Question 18: Do you have other feedback?

Overview of early feedback

Since mid-2025 we have engaged with several firms, industry bodies and individuals (with some providing written feedback) to get their views on custody law and practices. Most stakeholders we spoke to considered that baseline safekeeping rules in our regime (i.e. requirements to hold client assets on trust and separately from a custodian's own assets etc) are fundamentally sound. Most also considered that custody arrangements in the MIS and DIMS sectors generally operate effectively, supported by supervisors (for MIS), assurance engagements and established governance frameworks.

However, stakeholders noted ongoing risks relating to conflicts of interest, outsourcing and market concentration (including reliance on key platforms, registries and offshore sub-custodians), cyber security vulnerabilities and operational resilience. Many emphasised the need to clearly define the problem being addressed before settling on solutions and stressed the importance of recognising differences between market sectors.

Several stakeholders raised concerns in relation to requirements for retail client money or property services (**CMPS**) custody, where low barriers to entry, limited segregation of duties and independence, manual processes, weak systems and constrained resources were seen as increasing the risk of misconduct and fraud, particularly for smaller custodians.

Universal minimum standards (such as fit and proper requirements, baseline operational controls and resilience expectations) were generally supported by stakeholders, provided they are proportionate and risk-based.

Some stakeholders saw licensing as a useful tool to lift standards, address gaps, provide regulatory visibility and operate as a credible 'badge' internationally. Others questioned whether licensing alone would have prevented past misconduct, and emphasised supervision, assurance and enforcement as alternative or complementary levers.

Strong emphasis was placed by some on the quality, consistency and use of assurance engagements. There were some calls for greater clarity of roles and responsibilities across advisers, platforms and custodians – particularly around record-keeping, reporting, disclosures and accountability – to reduce duplication and uncertainty.

Finally, stakeholders noted the need to consider emerging asset classes, including crypto-assets and stablecoins, with some suggesting custody of these assets should be subject to the same basic control expectations as traditional assets.

Appendix – Regulatory settings

Managed investment scheme sector

The MIS sector consists of a range of scheme types, including managed funds (e.g. KiwiSaver), 'other MIS' (e.g. property or forestry schemes), and restricted schemes. When referring to MIS or funds, for simplicity this document only discusses settings for managed funds. However, similar rules apply for most other types of schemes[43].

Regulatory settings for MIS custody

- **Licensing**: Retail MIS[44] must register and generally have a licensed manager and an independent licensed supervisor. The FMA licenses managers under the FMCA and supervisors under the Financial Markets Supervisors Act 2011. Supervisors oversee the manager's compliance with its functions and issuer obligations, and general duties apply when carrying out their statutory functions.
- **Scheme property**: Supervisors are responsible for holding scheme property or ensuring it is held appropriately according to statutory requirements for the custodianship of scheme property in sections 156-159 of the FMCA.
- **Outsourcing***:* A supervisor can appoint an external custodian if the scheme governing document authorises this[45]. The person appointed must meet the external custodianship requirements. The external custodian, if authorised in writing by the supervisor, may in turn contract custody of scheme property to another person on the same basis.
- **External custodianship requirements***:* The supervisor (or external custodian) that is outsourcing custody must believe on reasonable grounds that the person they are contracting to hold the scheme property is appropriate to hold and safeguard the scheme property.[46] The person must be a body corporate and independent of the manager. The supervisor (or external custodian) must take all reasonable steps to ensure the person performs custody as if the supervisor (or external custodian) performed it directly, and to monitor the performance of the function. The supervisor (or external custodian) that is outsourcing is jointly and severally liable with the person for performance of the function.
- **Key duties and settings relating to custody of scheme property for a registered MIS**: Key duties and settings include:

[43] There are some differences due to governance settings (e.g. no supervisor for restricted schemes).
[44] FMCA, s127
[45] FMCA, s 156. The custodian may in turn contract out custody with the supervisor's agreement in writing. The same rules apply.
[46] FMCA, s 156(1). Any head custodian can also outsource on the same basis if the supervisor agrees in writing: see FMCA, s156 (3).

a. Holding property: Ensuring scheme property is held on trust and separately from the custodian's own property or that of any related party of the scheme[47] (e.g. the manager).

b. Records and reporting: Keeping appropriate records of scheme property, and reconciling the records with those kept by sub-custodians and third parties to ensure the records are accurate. Obtaining an annual external assurance report by a qualified FMC auditor on whether the custodian's processes, procedures and controls were suitably designed to meet stated control objectives and operated effectively throughout the year. Custodians also have reporting obligations to the supervisor (and in some cases the FMA) if a serious problem occurs in relation to a registered scheme. This includes if the custodian has contravened any of its obligations in a material respect.

Regulatory settings in the DIMS sector

- **Holding property**: Unless held by the investor, a DIMS licensee must ensure that investor money or investor property is held by a custodian that meets the requirements below:
  - a body corporate (not being the DIMS provider) that the DIMS licensee believes on reasonable grounds is appropriate to hold and safeguard the money or property[48]
  - may be an associated person of the DIMS licensee only if permitted by a condition of the DIMS licence.

  If the FMA decides to allow the custodian of investor money or property to be an associated person through a condition of the licence, this may include limits on when or how long such an arrangement is permitted, or requirements that must be followed to manage the risks arising[49].
- **Obligations for handling client money and client property**: The DIMS licensee and custodian must comply with the obligations for handling client money and client property under the FMCA Part 6 client money or client property services regime, including specific custodian obligations under the FMC Regulations[50]. These include paying client money into a separate trust account and holding it on trust, accounting for client money and client property, keeping records, and client reporting including obtaining an annual external assurance engagement with a qualified FMC auditor.
- **Liability**: The DIMS licensee is jointly and severally liable with the custodian they appoint for compliance with the above obligations[51].

[47] See definition of related party in FMCA, s172(2)
[48] FMCA, s 445
[49] FMC Reg, reg 200
[50] FMCA, s446
[51] FMCA, s 445(3)

Client money or property services sector

Regulatory settings in CMPS sector

- **Registration**: Providers of CMPS (including a custodial service) must be registered appropriately on the FSPR and, if providing services to retail clients, belong to an approved dispute resolution scheme. FMCA Part 2 fair dealing prohibitions apply.
- **General conduct obligations**[52]: CMPS providers including custodians must:
  - exercise care, diligence and skill; and
  - not receive client money if the offer contravenes the FMCA or FMC Regulations[53].
- **Obligations for handling client money and client property:** For retail clients[54] this includes obligations to:
  - hold client money and property on trust in a separate trust account;
  - properly account to the client for money and property held;
  - report on client money and client property;
  - maintain adequate records of the client money and property; and
  - not use or apply client money or property, except as expressly directed by the client[55].
- **Custodian obligations:** Specific obligations apply to a person who provides relevant custody services to a client. Broadly these include:
  - reporting to clients;
  - reconciling records; and
  - obtaining an annual external assurance engagement[56].
- **Eligibility and appointment:** There are no eligibility requirements or restrictions on appointment as a custodian in the CMPS regime. No independence requirement applies.
- **Outsourcing**: Under the CMPS regime, if a business outsources provision of custody services to another person, the business must ensure that person complies with the custodian obligations. The business is treated as having the obligations, and if the obligations are not complied with then the business will be liable under the FMCA[57].

[52] FMCA, 431ZA to 431ZB
[53] FMCA, s431ZA, 431ZB
[54] These obligations also apply to some wholesale clients, i.e. those relying on their investment activity status (e.g. eligible investors) – see the following section on wholesale custody.
[55] FMCA, 431ZC to 431ZH
[56] FMC Regulations 229P to 229V
[57] FMCA, s431ZI; FMC Regulations 229P

- **NZX participant rules**: Custodians that provide trading/execution services may also be subject to third-party arrangements, such as the participant rules of the financial product market,[58] which provide a degree of oversight or standard-setting.

Wholesale custody

In February 2026, there were 106 entity registrations on the FSPR for wholesale custodial services. We have little information about some of these entities (e.g. where they do not offer any other licensed services). There are minimal requirements for wholesale custody services. Wholesale custodians must register on the FSPR and comply with fair dealing obligations under Part 2 of the FMCA. They must also comply with some general conduct obligations under Part 6[59]:

- to exercise care, diligence and skill
- not to receive client money if the offer contravenes the FMCA or FMC Regulations.

Part 6 obligations for handling client money and client property apply only to services to wholesale clients relying on their investment activity status (e.g. eligible investors)[60] and not wholesale clients that are:

- investment businesses (for example, an entity whose main business is investing in financial products, a registered bank, or a financial adviser);
- 'large' investors (i.e. investors with net assets or turnover exceeding $5 million for the last two completed financial years);
- Government agencies; and
- entities under the control of one of the above[61].

[58] For example, the NZX's Participant Rules, which set out detailed client asset and client money rules, and capital adequacy and operational resilience requirements for certain firms, such as NZX Trading and Advising Firms.
[59] FMC Act, s431Z(1)
[60] For example, eligible investors or persons who are wholesale because they meet certain investment activity criteria in clause 38 of Schedule 1 of the FMCA.
[61] FMCA, s 431Z(2)(c); FMC Regulations 229W

Glossary of defined terms

Term	Meaning
AFS licence	Australian Financial Services licence
CASS	Client Assets Sourcebook in the United Kingdom
API	Application programming interface
CMPS	Client money or property services
CSA	Credit Support Annex
DIMS	Discretionary investment management service
FAP	Financial advice provider
FCA	Financial Conduct Authority in the United Kingdom
FMCA	Financial Markets Conduct Act 2013
FMC auditor	A qualified auditor able to perform assurance engagements required under the Financial Markets Conduct regime
FMC Regulations	Financial Markets Conduct Regulations 2014
FMA	Financial Markets Authority – Te Mana Tātai Hokohoko
FSP Act	Financial Service Providers (Registration and Dispute Resolution) Act 2008
FSPR	Financial Service Providers Register
IMF	International Monetary Fund
ISAE 3402 report	An assurance report on controls at a service organisation, commonly used to assess custody and related operational controls
ISDA Master Agreement	The International Swaps and Derivatives Association master agreement used for derivatives transactions
KiwiSaver	New Zealand's work-based retirement savings scheme
MBIE	Ministry of Business, Innovation and Employment

MIS	Managed investment scheme
NZX participant rules	Rules applying to NZX market participants, including some third-party arrangements relevant to custody and execution services
OIA	Official Information Act 1982
PSP	Payment service provider
SFO	Serious Fraud Office
UCITS/AIF depositary regimes	European regulatory regimes requiring depositaries for certain collective investment funds, including UCITS and alternative investment funds