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ARTICLE

Duty of Best Execution and Payment for Order Flow: A Review of Recent Civil Litigation

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Payment for order flow (where market makers pay brokers to route orders for execution) and the duty of best execution (which requires a broker to seek the most favorable terms reasonably available for a transaction) were frequent regulatory topics in 2021. The SEC announced it would review payment for order flow in 2022, and FINRA issued guidance in July 2021 on both the duty of best execution and payment for order flow. Payment for order flow and best execution have co-existed for years, and regulatory focus has been on instances where payment for order flow allegedly takes priority over, and undermines, a broker's duty of best execution. But outside the regulatory sphere, the interplay between these two concepts also played out prominently in civil litigation over the last year.

For example, last year investors brought class-action lawsuits against brokers claiming, among other things, that a broker's public statements about satisfying the duty of best execution, without adequately disclosing its payment for order flow arrangement, were misleading. And in another case, the investor alleged the broker violated the duty of best execution by routing orders to trading venues that paid the broker the highest for order flow, rather than to venues providing investors the "best outcome." In these recent cases, the brokers prevailed, in large part because courts have recognized that determining a violation of the duty of best execution often requires, for each trade, a comparison between the executed prices and the prices available through alternative venues—which is an unwieldy exercise in class action cases potentially involving hundreds of millions of trades.

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