

# 5310. Best Execution and Interpositioning

- The Rule
- Notices

(a)(1) In any transaction for or with a customer or a customer of another broker-dealer, a member and persons associated with a member shall use reasonable diligence to ascertain the best market for the subject security and buy or sell in such market so that the resultant price to the customer is as favorable as possible under prevailing market conditions. Among the factors that will be considered in determining whether a member has used "reasonable diligence" are:

- (A) the character of the market for the security (e.g., price, volatility, relative liquidity, and pressure on available communications);
- (B) the size and type of transaction;
- (C) the number of markets checked;
- (D) accessibility of the quotation; and
- (E) the terms and conditions of the order which result in the transaction, as communicated to the member and persons associated with the member.
- (2) In any transaction for or with a customer or a customer of another broker-dealer, no member or person associated with a member shall interject a third party between the member and the best market for the subject security in a manner inconsistent with paragraph (a)(1) of this Rule.
- (b) When a member cannot execute directly with a market but must employ a broker's broker or some other means in order to ensure an execution advantageous to the customer, the burden of showing the acceptable circumstances for doing so is on the member.
- (c) Failure to maintain or adequately staff an over-the-counter order room or other department assigned to execute customers' orders cannot be considered justification for executing away from the best available market; nor can channeling orders through a third party as described above as reciprocation for service or business operate to relieve a member of its obligations under this Rule.
- (d) A member through which an order is channeled and that knowingly is a party to an arrangement whereby the initiating member has not fulfilled its obligations under this Rule, will also be deemed to have violated this Rule.
- (e) The obligations described in paragraphs (a) through (d) above exist not only where the member acts as agent for the account of its customer but also where transactions are executed as principal. Such obligations are distinct from the reasonableness of commission rates, markups or markdowns, which are governed by Rule 2121 and its Supplementary Material.

• • • Supplementary Material: -----

- .01 Execution of Marketable Customer Orders.** A member must make every effort to execute a marketable customer order that it receives fully and promptly.
- .02 Definition of "Market."** For the purposes of Rule 5310 and the accompanying Supplementary Material, the term "market" or "markets" is to be construed broadly, and it encompasses a variety of different venues, including, but not limited to, market centers that are trading a particular security. This expansive interpretation is meant to both inform broker-dealers as to the breadth of the scope of venues that must be considered in the furtherance of their best execution obligations and to promote fair competition among broker-dealers, exchange markets, and markets other than exchange markets, as well as any other venue that may emerge, by not mandating that certain trading venues have less relevance than others in the course of determining a firm's best execution obligations.
- .03 Best Execution and Debt Securities.** Rule 5310(a)(1)(D) provides that one of the factors used to determine if a member has used reasonable diligence in exercising best execution is the "accessibility of the quotation." In the context of the debt market, this means that, when quotations are available, FINRA will consider the accessibility of such quotations when examining whether a member has used reasonable diligence. For purposes of debt securities, the term "quotation" refers to either dollar (or other currency) pricing or yield pricing. Accessibility is only one of the non-exhaustive reasonable diligence factors set out in Rule 5310(a)(1). In the absence of accessibility, members are not relieved from taking reasonable steps and employing their market expertise in achieving the best execution of customer orders.
- .04 Best Execution and Executing Brokers.** A member's duty to provide best execution in any transaction "for or with a customer of another broker-dealer" does not apply in instances when another broker-dealer is simply executing a customer order against the member's quote. The duty to provide best execution to customer orders received from other broker-dealers arises only when an order is routed from the broker-dealer to the member for the purpose of order handling and execution. This clarification is intended to draw a distinction between those situations in which the member is acting solely as the buyer or seller in connection with orders presented by a broker-dealer against the member's quote, as opposed to those circumstances in which the member is accepting order flow from another broker-dealer for the purpose of facilitating the handling and execution of such orders.
- .05 Use of a Broker's Broker.** Paragraph (b) of the Rule provides that when a member cannot execute directly with a market but must employ a broker's broker or some other means in order to ensure an execution advantageous to the customer, the burden of showing the acceptable circumstances for doing so is on the member. Examples of acceptable circumstances are where a customer's order is

VERSIONS

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SUMMARY TOPICS ⓘ

Business Unit (BU) (3)

Customer Type (CT) (2)

Firm Type (FT) (4)

Numerical Reference (NR) (1)

Obligations & Duties (OD) (11)

Regulatory Process (RP) (1)

Security Type (ST) (2)

DETAILED TOPICS ⓘ

Defined Terms within the Rule or Rule Series (DT) (2)

Related Laws, Rules & Regulations (RL) (2)

Terminology (TR) (131)

“crossed” with another firm that has a corresponding order on the other side, or where the identity of the firm, if known, would likely cause undue price movements adversely affecting the cost or proceeds to the customer.

**.06 Orders Involving Securities with Limited Quotations or Pricing Information.** Although the best execution requirements in Rule 5310 apply to orders in all securities, markets for securities differ dramatically. One of the areas in which a member must be especially diligent in ensuring that it has met its best execution obligations is with respect to customer orders involving securities for which there is limited pricing information or quotations available. Each member must have written policies and procedures in place that address how the member will determine the best inter-dealer market for such a security in the absence of pricing information or multiple quotations and must document its compliance with those policies and procedures. For example, a member should analyze pricing information based on other data, such as previous trades in the security, to determine whether the resultant price to the customer is as favorable as possible under prevailing market conditions. In these instances, a member should generally seek out other sources of pricing information or potential liquidity, which may include obtaining quotations from other sources (e.g., other firms that the member previously has traded with in the security).

**.07. Orders Involving Foreign Securities.** The obligation in Rule 5310(a) that a member use “reasonable diligence” in exercising best execution applies to customer orders in both domestic and foreign securities. However, Rule 5310(a) also recognizes that the markets for different securities can vary dramatically, and the standard of “reasonable diligence” must be assessed by examining specific factors, including “the character of the market for the security” and the “accessibility of the quotation.” Accordingly, the determination as to whether a member has satisfied its best execution obligations necessarily involves a “facts and circumstances” analysis.

The handling of customer orders in foreign securities that do not trade in the U.S. can differ substantially from the handling of orders in U.S.-traded securities. In particular, the character of the particular foreign market and the accessibility of quotations in certain foreign markets may vary significantly. Some foreign jurisdictions, for example, may not have similar best execution requirements as those imposed by Rule 5310, or may not have comparable access and pre-trade or post-trade transparency standards.

Even though a security does not trade in the U.S., members still have an obligation to seek best execution for customer orders involving any foreign security. Consequently, a member that handles customer orders involving foreign securities that do not trade in the U.S. must have specific written policies and procedures in place regarding its handling of customer orders for these securities that are reasonably designed to obtain the most favorable terms available for the customer, taking into account differences that may exist between U.S. markets and foreign markets. While best execution obligations take into account differing market structures, best execution obligations also must evolve as changes occur in the market that may give rise to improved executions, including opportunities to trade at more advantageous prices. As such, members also must regularly review these policies and procedures to assess the quality of executions received and update or revise the policies and procedures as necessary.

**.08 Customer Instructions Regarding Order Handling.** If a member receives an unsolicited instruction from a customer to route that customer's order to a particular market for execution, the member is not required to make a best execution determination beyond the customer's specific instruction. Members are, however, still required to process that customer's order promptly and in accordance with the terms of the order. Where a customer has directed that an order be routed to another specific broker-dealer that is also a FINRA member, the receiving broker-dealer to which the order was directed would be required to meet the requirements of Rule 5310 with respect to its handling of the order.

**.09 Regular and Rigorous Review of Execution Quality.**

(a) No member can transfer to another person its obligation to provide best execution to its customers' orders. A member that routes customer orders to other broker-dealers for execution on an automated, non-discretionary basis, as well as a member that internalizes customer order flow, must have procedures in place to ensure the member periodically conducts regular and rigorous reviews of the quality of the executions of its customers' orders if it does not conduct an order-by-order review. The review must be conducted on a security-by-security, type-of-order basis (e.g., limit order, market order, and market on open order). At a minimum, a member must conduct such reviews on a quarterly basis; however, members should consider, based on the firm's business, whether more frequent reviews are needed.

(b) In conducting its regular and rigorous review, a member must determine whether any material differences in execution quality exist among the markets trading the security and, if so, modify the member's routing arrangements or justify why it is not modifying its routing arrangements. To assure that order flow is directed to markets providing the most beneficial terms for their customers' orders, the member must compare, among other things, the quality of the executions the member is obtaining via current order routing and execution arrangements (including the internalization of order flow) to the quality of the executions that the member could obtain from competing markets. In reviewing and comparing the execution quality of its current order routing and execution arrangements to the execution quality of other markets, a member should consider the following factors:

- (1) price improvement opportunities (i.e., the difference between the execution price and the best quotes prevailing at the time the order is received by the market);
- (2) differences in price disimprovement (i.e., situations in which a customer receives a worse price at execution than the best quotes prevailing at the time the order is received by the market);
- (3) the likelihood of execution of limit orders;
- (4) the speed of execution;
- (5) the size of execution;
- (6) transaction costs;
- (7) customer needs and expectations; and
- (8) the existence of internalization or payment for order flow arrangements.

(c) A member that routes its order flow to another member that has agreed to handle that order flow as agent for the customer (e.g., a clearing firm or other executing broker-dealer) can rely on that member's regular and rigorous review as long as the statistical results and rationale of the review are fully disclosed to the member and the member periodically reviews how the review is conducted, as well as the results of the review.

Amended by SR-FINRA-2014-023 eff. May 9, 2014.  
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Amended by SR-FINRA-2007-024 eff. Sep. 8, 2009.  
Amended by SR-NASD-2004-130 eff. Sep. 28, 2007.  
Amended by SR-NASD-2004-026 eff. Nov. 8, 2006.  
Amended by SR-NASD-2005-087 eff. Aug. 1, 2006.  
Amended by SR-NASD-2000-20 eff. Nov. 24, 2000.  
Amended by SR-NASD-98-57 eff. March 26, 1999.  
Amended by SR-NASD-97-42 eff. Oct. 22, 1997.  
Amended by SR-NASD-87-55 eff. May 2, 1988.  
Interpretation adopted eff. May 1, 1968.

**Selected Notices:** 97-88, 99-16, 00-78, 06-58, 07-40, 09-58, 10-26, 10-42, 12-13, 15-46, 18-29.

◀ 5300. HANDLING OF CUSTOMER ORDERS

UP

5320. PROHIBITION AGAINST TRADING AHEAD OF CUSTOMER ORDERS ▶



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