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To: [Comments, Public](#)
Subject: The Eligibility Rule
Date: Friday, April 17, 2026 2:33:16 PM

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Ladies and Gentlemen:

The following are comments that I have made to FINRA in the past concerning the eligibility rule, repeated here in the most part together with some additional comments, pursuant to the notice entitled FINRA Requests Comment on Modernizing FINRA Arbitration Rules, Guidance and Processes.

At least a majority of the rulings of federal courts of appeals hold Rule 12206/Rule 13206 of the Code of Arbitration Procedure to be a rule of repose, not subject to tolling, although there are federal district court cases holding that Rule 12206 is akin to a statute of limitations subject to equitable tolling.

In 2002, the U.S. Supreme Court in *Howsam v. Dean Witter Reynolds, Inc.*, 537 U.S. 79 (2002), held that the issue of eligibility pursuant to NASD Rule 10304 (now Rule 12206) is a question of fact for the arbitrators, not the courts, to decide. The Arbitration Guide states that “arbitrators may find that there is a continuing occurrence or event giving rise to the dispute. For example, although a customer purchased stock 10 years ago, there are allegations of ongoing fraud starting with the purchase, but continuing to a date within six years of the date the claim was filed.”

But that position seems to have been brought into question by the 2017 Supreme Court decision in *CalPERS v. ANZ Securities, Inc.*, 582 U.S. 497 (2017). The case held that for claims of misrepresentation in connection with the issuance of securities under Section 11 of the 1933 Securities Act, Section 13 of the Act establishes two distinct deadlines: a one-year deadline running from the discovery of the untrue statement or omission or after such discovery should have been made by the exercise of reasonable diligence, but in no event shall any such action be brought to enforce a liability created under Section 11 more than three years after the security was bona fide offered to the public.

The court in *CalPERS* stated that “the pairing of a shorter statute of limitations and a longer statute of repose is a common feature of statutory time limits. The two periods work together: the discovery rule gives leeway to a plaintiff who has not yet learned of a violation, while the rule of repose protects the defendant from an interminable threat of liability.” It ruled that the three-year time bar in Section 13 of the Securities Act of 1933 is a statute of repose not subject to equitable tolling. Rule 12206 also provides for two different time limitations, the six-year time bar and the statute of limitations, Rule 12206 specifically stating that the rule does not extend applicable statutes of limitations.

The position in *CalPERS* is analogous to NASD's position with respect to former Rule 10304. In 1998, NASD proposed amendments to the rule and provided a historical backdrop for the reasons behind the rule since it was first adopted in 1968, primarily for consistency with the SEC's books and records rule. NASD stated that the rule is intended to establish that the six-year limitation is a bright line standard for eligibility determination and that it cannot be tolled even if the claimant alleges fraudulent concealment of facts at the time of the original transaction. If the claim is based on an act or occurrence other than the transaction the six-year period will run from the date of the act or occurrence. (63 *Federal Register* 588 (1998)).

In 2019, FINRA issued its Dispute Resolution Monthly Update, including a reference to the *Final Report and Recommendations of the FINRA Dispute Resolution Task Force*, dated December 16, 2015. The discussion of Rule 12206 on page 39 of that report indicates that considerable time was spent on whether the eligibility rule should be eliminated or deemed a rule of repose, but no consensus was reached. Justice is not well-served when an issue can't be resolved because consensus wasn't reached. Note that the Supreme Court decision in *CalPERS*, cited above, which I found persuasive, was decided in 2017, after the 2015 report was issued.

In a statement of claim filed in May 2019, claimant sought the expungement of a customer complaint from her Central Registration Depository record. Respondent Morgan Stanley did not oppose the requested relief. *In the Matter of the Arbitration Between Haider Sharifi, Claimant, v. Morgan Stanley, Respondent* (19-01252). The arbitrator raised the question of eligibility under Rule 13206 *sua sponte*. After the hearing, the request for expungement was denied. The arbitrator apparently relied on *Horst v. FINRA*, a 2018 Colorado District Court case, which denied the claimant's motion to vacate the expungement denial, holding that "FINRA Rule 13206 speaks for itself, as does the Rule on the Arbitrator's ability to apply all the Rules in FINRA's Code of Arbitration Procedure".

<http://brokeandbroker.com/PDF/HorstNev181029OrdDeny.pdf>

While some arbitrators hold Rule 12206/13206 to be a rule of repose, as I do, others hold it to be a statute of limitations subject to tolling. Likewise, some courts do the same. How the parties fare depends on which arbitrators are selected, the courts to which a party may appeal a Rule 12206/13206 determination, and finally the luck of the draw.

Evalyn Lipton Fishbein
Attorney at Law
One Charles Street South, Suite 506
Boston, Massachusetts 02116-5453

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