IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 92-2392
Summary Calendar

KEN A. BODENHAMER, ET AL.,

Plaintiffs-Appellants,

v.

SHEARSON LEHMAN HUTTON, INC., ET AL.,

Defendants-Appellees.

Appeal from the United States District Court
for the Southern District of Texas
CA H 89 3549

July 14, 1993

Before GARWOOD, JONES, and EMILIO GARZA, Circuit Judges.*

EDITH H. JONES, Circuit Judge:

Appellants Ken A. Bodenhamer and Energy Materials, Inc. (Bodenhamer), investors in six limited partnerships, appeal the granting of summary judgment in favor of Shearson Lehman Hutton, Inc., Terrill Bell, and Lex Ann Edmondson (collectively, Shearson). Because we agree that Bodenhamer's federal securities law claims were time barred under the applicable statute of limitations, we affirm.

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*Local Rule 47.5 provides: "The publication of opinions that have no precedential value and merely decide particular cases on the basis of well-settled principles of law imposes needless expense on the public and burdens on the legal profession." Pursuant to that Rule, the Court has determined that this opinion should not be published.

I.

In late 1983 Bodenhamer's new company, Energy Materials, Inc., received an unprecedented customer order that allowed the company to realize a profit of approximately $500,000 during 1984. The extraordinary nature of that profit prompted Bodenhamer to consult with Terrill Bell, a CPA, and later Lex Ann Edmondson, a broker at E.F. Hutton & Company, about investing the company's surplus profits. Bodenhamer alleges that he informed Edmondson and Bell that he sought conservative investments that would provide a steady stream of income. Despite these alleged instructions, Edmondson suggested that Bodenhamer invest in six oil and gas limited partnerships. Edmondson also allegedly represented that the limited partnership interests would (1) be safer than stocks, (2) retain their liquidity at all times so Bodenhamer could easily sell his interests, (3) provide substantial tax advantages, (4) generate sufficient income to cover the payments on promissory notes given to buy into the limited partnerships, and (5) provide a 100% return on his initial capital investment within five years. Bodenhamer asserts these alleged representations were material and false.

Later in 1984, Bodenhamer was given an offering prospectus for each of the investments. The prospectuses contained repeated warnings to investors concerning the "high degree of risk" involved with the investments. The prospectuses also warned that the investments lacked liquidity. The subscription agreements Bodenhamer eventually signed contained similar warnings.

Bodenhamer admits that he noticed these warnings in the prospectuses, but asserts that he was unable to comprehend the prospectuses because of their technical nature.[1]

Bodenhamer invested various sums in the six limited partnerships. His cash investment was relatively small, but he also signed subscription loans requiring him to make cash payments over time to complete his capital contributions to the limited partnerships.

By mid-1985, at least two of the partnerships had ceased making distributions and were raising questions in Bodenhamer's mind. To make matters worse, in early 1986 Energy Materials suffered a severe financial reversal and became unable to make payments on its subscription notes. Bodenhamer defaulted on his notes to the limited partnerships and was forced to sell several of them.

On October 19, 1989, Bodenhamer filed suit against Shearson, alleging that he had been induced to invest in the limited partnerships through material misrepresentations and omissions in violation of section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5. After some discovery, Shearson moved for summary judgment contending that Bodenhamer's claims were

[1] Bodenhamer's repeated suggestions that he fell prey to Edmondson and Shearson because he lacked sophistication and did not understand the risks associated with an investment in an oil and gas limited partnership are unavailing. He had a college degree in business and had spent ten years in the oil and gas industry. Moreover, at the time Bodenhamer invested in these limited partnerships, he certified that he and his wife were suitably sophisticated for such investments.

barred by the statute of limitations. There appeared to be some confusion concerning the applicable statute of limitations to be applied to Bodenhamer's claims, but the magistrate judge found that a reasonable investor knew or should have known of the factual basis of the claims by July 1985, and therefore, recommended that summary judgment be granted on all of Bodenhamer's claims. The district court adopted the magistrate judge's recommendation and granted summary judgment on all claims. The court later amended its judgment to dismiss Bodenhamer's state law claims without prejudice.

In December 1991, Congress enacted section 476 of the Federal Deposit Insurance Corporation Improvement Act of 1991.[2] Relying on section 476(b), Bodenhamer moved the court to reinstate the claims that it had dismissed. Shearson responded that Bodenhamer's claims could not be reinstated under section 476(b),

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[2] Section 476 provides in part:

> (b) Effect on Dismissed Causes of Action. Any private civil action implied under section 10(b) of this Act that was commenced on or before June 19, 1991--
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> (1) which was dismissed as time-barred subsequent to June 19, 1991, and
>
> (2) which would have been timely filed under the limitation period provided by the laws applicable in the jurisdiction, including principles of retroactivity, as such laws existed on June 19, 1991,
>
> shall be reinstated on motions by the plaintiff not later than 60 days after the date of enactment of this section.

15 U.S.C. § 78aa-1(b).

because those causes of action were barred even under the two-year and four-year limitations periods applied in this circuit prior to Lampf, Pleva, Lipkind, Prupis, & Petigrow v. Gilbertson, ____ U.S. ____, 111 S. Ct. 2773, 115 L.Ed.2d 321 (1991). The district court agreed and denied the motion to reinstate because Bodenhamer's claims were barred even under a four-year statute of limitations. Bodenhamer appeals.

II.

Review of the court's summary judgment is performed de novo, employing the same standard as the district court, i.e. to determine whether the facts and inferences, taken in the light most favorable to the non-moving party, present no genuine issue of material fact and require judgment for the movant as a matter of law. White v. Texas American Bank/Galleria, N.A., 958 F.2d 80, 82 (5th Cir. 1992).

The primary issue in this case is when the statute of limitations began to run. Although we borrow the applicable limitations period from state law, the determination of when that limitations period begins to run is governed by federal law. Jensen v. Snellings, 841 F.2d 600, 606 (5th Cir. 1988); Davis v. A.G. Edwards & Sons, Inc., 823 F.2d 105, 107 (5th Cir. 1987). According to federal law, the limitations period commences when "the aggrieved party has either knowledge of the violation or notice of facts which, in the exercise of due diligence, would have led to actual knowledge" of the violation. Davis, 823 F.2d at 107 (quoting Vigman v. Community National Bank & Trust Co., 635 F.2d

455, 459 (5th Cir. 1981)). The limitations period for fraud, including causes of action brought under section 10(b) or Rule 10b-5, does not begin to run until the plaintiff discovers, or in the exercise of reasonable diligence should discover, the alleged fraudulent conduct. Jensen, 841 F.2d at 606; Breen v. Centex Corp., 695 F.2d 907, 911 (5th Cir. 1983). Thus, as this court emphasized in Vigman, even if the plaintiff does not have knowledge of the existence of a cause of action, the limitations period will begin running if the plaintiff has knowledge of "the facts forming the basis of his cause of action." Vigman, 635 F.2d at 459 (emphasis in original) (quoting Azalea Meats, Inc. v. Muscat, 386 F.2d 5, 9 (5th Cir. 1967)).

A potential plaintiff has an affirmative duty to diligently investigate facts which might lead to discovery of the fraudulent conduct. If a reasonable person would inquire further, a plaintiff must proceed with a reasonable and diligent investigation of the facts the plaintiff has learned and is charged with the knowledge of all facts such an investigation would have disclosed. Jensen, 841 F.2d 607; see In re Beef Indus. Antitrust Litig., 600 F.2d 1148, 1171 (5th Cir. 1979), cert. denied, 449 U.S. 905, 101 S. Ct. 280, 66 L.Ed.2d 137 (1980); Armstrong v. McAlpin, 699 F.2d 79, 88 (2d Cir. 1983). "Investors are not free to ignore 'storm warnings' which would alert a reasonable investor to the possibility of fraudulent statements or omissions in his securities transaction." Jensen, 841 F.2d at 607 (quoting Cook v. Avien, Inc., 573 F.2d 685, 697-98 (1st Cir. 1978)).

Bodenhamer's section 10(b) claim, the only claim at issue, accused Shearson of making misrepresentations in connection with the sale of the limited partnership interests. Thus, the statute of limitations began to run against Bodenhamer when he learned facts that would have caused a reasonable person to initiate a reasonable and diligent investigation that would have uncovered the alleged fraudulent conduct.[3]

Bodenhamer, perhaps relying on this court's analysis in Jensen, asserts that he did not discover that the investments were not liquid until early 1986. He also asserts that it was 1986, or at least very late in 1985, before he realized that his limited partnership investments were going belly-up. If true, argues Bodenhamer, he was not on notice of fraud until very late in 1985, i.e., less than four years before he filed suit.

To the extent that Bodenhamer relies on Jensen, that reliance is misplaced. In Jensen, the plaintiffs' first indication of any fraudulent conduct came when they learned that the cattle-feeding program in which they had invested substantial amounts of money was suffering significant losses. Knowledge of these losses and other revelations about the cattle investment program served as "storm warnings" that triggered the duty of the Jensens to inquire

[3] Bodenhamer's allegations of fiduciary duties are insufficient to toll the running of the statute of limitations. See Jensen, 841 F.2d at 607-10. The existence of a fiduciary relationship may, however, affect the determination whether the plaintiff learned sufficient facts such that a reasonable person would inquire further. Id. at 607, 610 n.6.

further and started the running of the statute of limitations. Jensen, 841 F.2d at 607-08.

This case differs from Jensen in that Bodenhamer's discovery of the illiquidity of his investments and the substantial losses which they had incurred were not the first "storm warnings" that Bodenhamer received. Bodenhamer's own deposition testimony reveals that, as early as 1984, he was aware of the glaring inconsistencies between the representations made to him personally and those contained in the prospectuses of the investments. While Bodenhamer alleges that Shearson represented to him that the investments were conservative, low risk, and liquid, he was also aware that the prospectuses specifically warned that each of the investments involved "a high degree of risk." The prospectuses also warned that the investments lacked liquidity, in direct contradiction to the representations Bodenhamer alleges were made to him. The subscription agreements Bodenhamer signed also should have put him on notice of the speculative nature of his investment.

As this court stated in a similar case also involving oil and gas limited partnership units, "It certainly triggered a reason to exercise reasonable diligence. If plaintiffs subsequently were told something contrary to this agreement, that should have dyed the flag raised by the subscription agreement an even brighter shade of red." Topalian v. Ehrman, 954 F.2d 1125, 1134 (5th Cir.), cert. denied, ____ U.S. ____, 113 S. Ct. 82, 121 L.Ed.2d 46 (1992). In Topalian, because the subscription agreement directly contradicted alleged representations made to them about the degree of risk involved in the investment, this court held that the statute of limitations began to run on the date the plaintiffs signed the subscription agreements and consequently, the plaintiffs' claims were barred. Topalian, 954 F.2d at 1134-35; Kennedy v. Josephthal & Co., 814 F.2d 798, 802-03 (1st Cir. 1987) ("A reasonable investor would have at least inquired as to this glaring difference but instead appellants, according to their own version, relied upon the more favorable assessment. . . . Appellants were, therefore, on inquiry notice from the time they received the prospectus and spoke with the [broker]."). These claims were barred.[4]

CONCLUSION

For the reasons stated, the judgment of the district court is **AFFIRMED**.

[4] Shearson challenges the constitutionality of section 476, 15 U.S.C. § 78aa-1. Because Bodenhamer's claim would not have been timely filed under the limitation period provided by the laws of Texas as they existed on June 19, 1991, this section is not implicated, and we have no occasion to consider its constitutionality. We note, however, that several circuits have upheld the section. See, e.g., Cooperativa De Ahorro y Credito Aguada v. Kidder, Peabody & Co., ____ F.2d ____, 1993 WL 156464 (1st Cir. May 19, 1993); Berning v. United States, 990 F.2d 272 (7th Cir. 1993); Grey v. First Winthrop Corp., 989 F.2d 1564 (9th Cir. 1993); Anixter v. Home-Stake Production Co., 977 F.2d 1533 (10th Cir. 1992), cert. denied, ____ U.S. ____, 113 S. Ct. 1841, 123 L.Ed.2d 467 (1993); Henderson v. Scientific-Atlanta, Inc., 971 F.2d 1567 (11th Cir. 1992).