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# Avoiding the Next Enron

By Catherine Reese  
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(FORTUNE Magazine) – Enron shareholders may not have been able to prevent their company from imploding, but there's a chance they could have detected the number fudging sooner--and gotten out in time--if they'd exercised their inspection rights.

These little-known statutes allow stockholders to police corporate books, giving them access to everything from minutes of board meetings to expense reports to even internal e-mails. Let's say that in reading through the annual report you notice several mentions in the footnotes of "related-party transactions." These aren't necessarily indicators of foul play but can occasionally lead to the juicy stuff. And we're not just talking about Enron.

Consider what happened when a stockholder in former global food giant TLC Beatrice International (now trading as a pink-sheet stock) demanded inspection of corporate accounts because of concern over related-party deals there. After looking over the records, the shareholder sued on behalf of the company--he was an owner, after all--to recover assets diverted by senior managers for their own benefit and to halt future diversions. The case was eventually settled in 1997, with the managers repaying millions of dollars to the company.

So why have so few investors heard of these potentially revelatory rights--and fewer still exercised them? Well, for one, companies don't exactly publicize them. And second, using them can get a little complicated.

Here's how they work. First, you need to find out where the company in question is incorporated. The laws of that state govern--and in the vast majority of cases that means Delaware. Then, write a letter, signed before a notary, to corporate headquarters detailing the records you want to review and why. It's that simple. No lawyer required.

If the corporation refuses or ignores the demand for five business days, under Delaware's statute you can petition the Chancery Court for a "summary" order requiring the company to comply. This proceeding is fast, focused, and inexpensive. Inspection rights were created to permit shareholders to keep an eye on their investment. As one court recently said, when a manager hides "misdeeds from the passive investors by imposing an information blackout, the right to seek court-ordered access to the books and records may be the passive investor's only recourse." If you have concerns that one of your investments may be the next Enron, you may want to exercise your inspection rights before it's too late.

--Catherine Reese

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