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Would You Hire a Wife-Beating Kleptomaniac? No?

Then you'd better play it safe and hire a private investigator.

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Last summer, Deb Kramer, chairman of the board of Lightdog.com, a Minneapolis-based Internet service provider, raised $18 million to acquire a competing startup ISP. The day before the deal was to close, Kramer says, she got a "bad gut feeling" about the firm's chief executive and called **California Business Intelligence** of Camarillo, Calif., to run a background check. Her gut was right. CBI unearthed bankruptcies and an FTC injunction for fraud against the executive's former company. Kramer passed on the investment, and less than a year later, the startup went out of business.

CBI is one of a growing number of corporate private investigation firms, which for $350 and up will carry out background checks by poking around in databases, unearthing courthouse documents, and paying visits to former friends, employers, and business acquaintances. For premium fees, as we've seen in Larry Ellison's recent digging for dirt on Microsoft's monopolistic practices, some sleuths will even root through trash to look for revelations.

It wasn't many years ago that firms like CBI were far off the radar screens of startup technology companies. Early-stage tech investing and hiring used to be a regional, clubby affair conducted within a well-connected network of venture capitalists, angel investors, and entrepreneurs with business or engineering pedigrees. The technology boom, however, has changed all of that. Venture capitalists are placing bets worth hundreds of millions of dollars. And startups not only are far more numerous than in the past but also are growing far faster. As a result, VCs, managers, and headhunters are working the crowd outside their clubs -- and that raises the risks.

"Most of the time, you've only met the management team recently," says Talbott Simonds of Trident Capital, a Palo Alto investment firm that works with early-stage companies. "And we're investing a lot of money in these folks." Trident Capital routinely hires New York-based Corporate Resolutions and Bishops Investigative Services to check out the management of companies it is looking to fund. "They always turn up something," Simonds says. "Ninety-nine times out of a hundred, it's not a deal-breaker, but knowing it ahead of time gives you peace of mind."

And peace of mind counts for a lot when SEC scrutiny is around the corner. Take the case of Phillip C. Radlick, founder and chief executive of Cardima, a medical instrument maker with venture backing from the likes of Goldman Sachs and Kleiner Perkins. Unbeknownst to at least some of Cardima's investors, Radlick had been convicted in 1976 of conspiracy to manufacture a controlled substance, a felony. During the preparations for Cardima's June 1997 IPO, due diligence by the underwriters, Bear Stearns and Dain Bosworth, revealed the conviction. A paragraph about the felony appeared in the registration document Cardima filed with the SEC. The venture capitalists who found out at the eleventh hour were red-faced. Regardless of whether Radlick's past is to blame, the company's stock dropped 17 percent on its first day of trading and never recovered. Initially priced at $7 a share, it now languishes at around $1. Radlick is still CEO and chairman.

At least one of Cardima's backers, VC firm New Enterprise Associates, now regularly uses investigators when considering new investments. Chip Linehan, a partner at NEA, says he prefers to check out executives using his own industry sources. However, if something looks fishy -- an unexplained gap in employment history, for example -- he'll turn to a professional investigator.

Kenneth Springer, a retired FBI agent, started Corporate Resolutions, a New York City business investigation outfit, in 1991. Springer and his 11-person team boast numerous success stories; they've busted a CFO skimming from the company till and nailed a shakedown racket that resulted in the arrest of three government inspectors. About 10 percent of the time, Springer says, his firms' investigations lead clients to reconsider potential deals. "Years ago, people thought doing integrity investigations was underhanded. Now it's just the real prudent thing to do&. Companies come to us because they don't want to get embarrassed."

For companies looking to hire an investigative firm, there's a range of options. On the low end, for $350, California Business Intelligence will conduct an initial background check that includes sifting through public and private databases such as CDB Infotech/Choicepoint, Lexis-Nexis, and other subscription databases. CBI charges $75 an hour for additional digging. Basic checks take a day or two to complete. On the high end, Corporate Resolutionscharges $3,000 to $5,000 for much deeper snooping that can take weeks. Its investigators interview subjects in person and travel to out-of-the-way document depositories for hands-on research.

How far will PIs probe into someone's background? Pretty far. CBI owner Michael Adams says failure to pay child support, for example, is easily found in public records and is fair game. Corporate Resolutions's Springer says an executive's past indiscretions or patterns of behavior like drug abuse or spousal abuse could hurt a company's reputation and wreck its chances for a successful IPO, so his clients often need to know that sort of thing. Adams says he won't delve into nonpublic records, but adds that there are less scrupulous investigators who will go much further for a price, digging up things like bank account balances, phone records, and credit reports. "There's nothing you can't find out," says Adams, "with enough money."

Are there ethical or legal limits to what you can probe? "It's hard to say anything's off-limits," says Laura Hartman, associate professor of ethics at DePaul University. "The boundaries are blurred because the person's judgment is what you're looking into." Hartman draws the line at investigating someone's preadult behavior.

Now that investors are more anxious, thanks to the dotcom slide, CBI's Adams expects to see a surge in business. "Because of the [market] correction, you will start seeing more and more due diligence requirements for investing in dotcom companies, more looking into the people running the startups," he says.

Before you rush right out and hire a PI, keep in mind that while he may prevent you from investing with or hiring a bad apple, he can't protect you from your own ineptitude or from a turbulent business climate. Remember Deb Kramer's company, Lightdog.com? It has just filed for bankruptcy.