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For-Profit Schools, Tested Again

By GRETCHEN MORGENSON

LAST week was challenging for the Apollo Group, the big for-profit education company that runs the University of Phoenix, Western International University and other institutions. One reason is that the Obama administration instituted new rules barring pay-for-enrollment deals among student recruiters at for-profit colleges — a development that is likely to cause significantly lower enrollment levels at Apollo and its peers.

But last week also brought a disclosure from Apollo that the Securities and Exchange Commission had requested information about the company's insider trading policies relating to stock sales made by some of its top officials in 2009. The sales the S.E.C. is focusing on occurred around the time that the Department of Education was asking questions about the University of Phoenix's policies relating to money it receives under the federal government's Title IV financial aid programs.

An Apollo spokesman declined to comment on the S.E.C.'s request. The S.E.C., as is its custom, would not discuss its inquiry into the company.

Apollo's facilities offer flexible-degree programs for people ("working learners," it calls them) who have jobs or other obligations that keep them from attending school full-time. The University of Phoenix, by far the largest of the company's institutions, offers both online and on-campus classes. It operates in 39 states.

A majority of Apollo's revenue comes from federal student aid. The University of Phoenix, which accounted for 91 percent of Apollo's net revenue this year, gets the bulk of its own revenue from Title IV programs. Just 1 percent of cash revenue at the University of Phoenix comes from student loans that aren't channeled through the federal government.

Top for-profit colleges like Apollo's received $26.5 billion in government-funded student aid in 2009, the Department of Education says. Because taxpayers are on the hook if these loans go bad, it is high time that regulators increased their scrutiny of practices at Apollo and other for-profit education companies.

WITH the government taking a closer look at Apollo and its brethren, shareholders have been fleeing. An index of 13 for-profit education companies has lost 32 percent of its value this year. Apollo's stock closed on Friday at $37.48, down 37 percent for the year to date.

But back in 2009, the period the S.E.C. is focusing on in its inquiry, Apollo and others in its industry were highfliers. Apollo's shares peaked that year on Jan. 16, at almost $90. By year-end they had fallen to $60.58.

Insider sales of Apollo shares spiked twice in 2009 — once in January and again in July. What the S.E.C. may want to determine is whether these sales were related to communications from the Department of Education about problems it had identified at the University of Phoenix.

The first batch of sales took place between Jan. 15 and Jan. 23. John G. Sperling, the company's chairman and founder, and Peter V. Sperling, his son and the company's vice chairman, sold almost 1.1 million shares during that period, S.E.C. filings show. Most of the shares were sold for prices ranging between $87 and $89.

Internal Apollo e-mails provide an interesting backdrop to these sales. They were obtained through the Freedom of Information Act by Robert S. MacArthur, president of Alternative Research Services Inc., a firm in Ridgefield, Conn. Mr. MacArthur conducts research for investors known as short sellers who are interested in making negative bets on companies. He doesn't take positions in stocks he covers.

On Jan. 13, a Department of Education official sent an e-mail to Apollo asking about three student complaints it had received relating to the University of Phoenix's loan disbursement practices. It also noted that the department had received a copy of a class-action lawsuit against Apollo filed by students encountering problems with reimbursements from the company.

The government raised a series of questions about Apollo's practices. On Feb. 9, about three weeks after the Department of Education sent the e-mail, federal education officials advised Apollo that the government would be conducting an in-depth program review of the company's financial aid practices.

The federal inquiry was to begin on Feb. 23 and examine Apollo's procedures going back to 2006.

Apollo didn't publicly disclose the federal review until March 31, 2009, when it announced

its quarterly earnings after the stock market had closed. The next day, Apollo's shares dropped 15 percent, to $66 from around $78.

Federal reviews typically take a long time to produce. Department of Education officials analyze the information they've gleaned from their examination and then produce an initial report that they share with the company.

Mr. MacArthur, the researcher, has studied government disclosures about the time frame of such reviews and believes that the Department of Education's initial report would probably have been produced and provided to Apollo no later than the end of May 2009 — after which Apollo would have several months to respond.

It was during this period — in July 2009 — that the second spurt of insider selling took place at Apollo. John and Peter Sperling sold 2.1 million shares at between $65 and $70 per share.

The Department of Education made public its report on the University of Phoenix in June this year. And it found several problematic practices at the school. For example, it determined that the University of Phoenix was late in returning federal grant money that it was not entitled to keep because some students had dropped out of its programs.

The University of Phoenix paid the Department of Education $661,000 to resolve the problems and had to post a $125 million letter of credit to cover future payment problems.

A year before the report's conclusions saw the light of day, Apollo insiders were selling stock.

"It is clear that the S.E.C. has serious concerns about the timing and size of the insider sales made by board members in July 2009," Mr. MacArthur said. "Given the fact that a negative program review could cause the Department of Education to revoke Apollo's Title IV participation, it seems unlikely that board members would be unaware of the serious findings" in the report.

Insider trading cases are notoriously difficult to make, of course. And although the Sperlings sold a total of more than three million shares, they represented a small portion of the stock held by both men. At the end of October 2009, according to company filings, John Sperling held 16.8 million shares and Peter Sperling held 7.9 million.

Asked about these transactions, Ryan Rauzon, an Apollo spokesman, declined to comment

and declined to make the Sperlings available for an interview. But he said the company was cooperating with the S.E.C. and that it looked forward to an open and fair process. He also pointed out that in the fall of 2008, Apollo had alerted investors that a program review by the Department of Education was likely to occur in the coming year.

MR. MacARTHUR has researched the for-profit education sector since 1997, starting with a company called Computer Learning Centers, which closed its doors after the Department of Education identified illegal recruiting practices at the firm.

And he thinks something is amiss at Apollo.

“Given the chairman and his son sold roughly two million shares in July of 2009 during a program review that was raising questions around the proper refund calculations, it should come as no surprise the S.E.C. is asking questions,” he said.

Stay tuned.