Concordia Portland—Closed

What does HotChalk's $302M Lawsuit against Synod and Others Mean?

by James D. Runzheimer, Attorney

(As published in the *Lutheran Clarion,* November 2021)

Introduction

The 2019 LCMS Convention considered three wide-ranging resolutions related to the structure and governance of the Concordia University System (CUS). This attention is overdue and critical to the future of both the CUS and the Synod. Three Concordia universities have closed in less than four years. It is not hyperbolic to suggest that we face a crisis. Litigation resulting from the closing of Concordia University Portland (CUP) bears particular risks for the Synod, Lutheran Church Extension Fund (LCEF), and CUS.

Closing of CUP and Resulting Lawsuit

CUP announced on February 10, 2020, that it would permanently "close at the end of the spring semester as a result of plummeting enrollment and high debt [1] . . .". Interim President Dr. Thomas Ries was quoted as stating that the financial condition of the university led to the decision." [2] CUP was the largest private university in Oregon.

CUP's closure was a shocking change of status from only six years earlier in 2014 when its revenue was a record $173 million, and the excess of its revenues over expenses was $10 million. The enrollment had climbed to 7,435, a 37 percent increase in a single year. [3]

The *Portland Business Journal* stated that a "lot of the enrollment and revenue growth resulted from the University's controversial partnership with California-based HotChalk, which partners with universities to create online degree programs, including Concordia's online graduate programs in education." [4] By 2014, Concordia had become the leading provider of online degrees in teaching.

The closing of CUP resulted in HotChalk, CUP's online program management (OPM) partner, suing Synod, LCEF, CUS, and CUP and numerous other defendants on April 17, 2020. [5] These defendants include The Lutheran Church—Missouri Synod (Synod); Lutheran Church Extension Fund (LCEF), Concordia University System (CUS); Concordia University, St. Paul; CUP; CUP Foundation; members of the Board of Regents of CUP; and several CUP administrators.

The three key targeted defendants are Synod, LCEF, and CUS. The causes of action against these three include fraud, fraudulent transfer, breach of duty of good faith and fair dealing, alter ego and corporate veil piercing, and interference with contractual relations. The largest damage amount that HotChalk is claiming is $302,105,410, jointly and severally, against Synod, LCEF, and CUS. HotChalk has calculated the $302,105,410 as a combination of a "termination fee" and "recoupable advance" derived from an Administrative Services Agreement, (ASA) that HotChalk and CUP signed in February 2018. This was only two years before the announcement of CUP's closure. Incredibly, this ASA had a 20 year term in which CUP had agreed to pay HotChalk a revenue share over the term of the ASA of 60% of CUP's tuition revenue. CUP would only retain 40%. The Regents of CUP approved the ASA and Dr. Charles Schlimpert, president of CUP for 35 years until his resignation in July 2018, signed it.

Relationship Between CUP and HotChalk

The relationship between CUP and HotChalk began in 2009. The current Amended Complaint of HotChalk in the Oregon litigation describes the 12 year history from the perspective of HotChalk as follows:

> Beginning in 2009, HotChalk and Concordia worked together to become leaders in online education, especially for teachers and other education professionals seeking masters and doctoral degrees in

> education. In exchange for a share of Concordia's tuition revenue, HotChalk provided a variety of services to help develop, implement, and support nonacademic aspects of Concordia's online graduate education program. HotChalk and Concordia established the online education business model to support working people wanting to further their professional education. Under most school-district contracts, teachers who wanted pay raises needed to complete additional graduate-level coursework. As a result, many of Concordia's students—working as both teachers and graduate students—preferred the flexibility afforded by online classes.
>
> HotChalk and Concordia's online program experienced immediate success and was hailed as a model for online education. This rapid growth was occurring as "brick and mortar" campuses, including Concordia, faced significant challenges, including declining enrollment, increasing expenses, and reduced revenue.
>
> The success of the parties' business plans made Concordia a model for other struggling small universities. In approximately 2013, in connection with a *qui tam* lawsuit brought by former employees, the Department of Justice began reviewing whether HotChalk and Concordia complied with certain U.S. Department of Education regulatory requirements related to incentive compensation and outsourcing limitations. Despite a series of court rulings in HotChalk and Concordia's favor in the underlying case that prompted the government inquiry, HotChalk and Concordia chose to settle with the United States and the plaintiffs, admitting no wrongdoing. [6] After the settlement and consistent with the related agreement, HotChalk and Concordia worked on restructuring their arrangement and entered into a new, 20-year agreement that was active at the time of the Concordia closure.
>
> HotChalk and Concordia entered into this new, 20-year agreement, the Administrative Services Agreement ("Agreement"), on February 14, 2018. . . . This new Agreement was structured to address U.S. Department of Education concerns.
>
> Under the Agreement, HotChalk received weekly "revenue-share" payments, also called the "Bundled Services Fee," which were calculated as a portion of the tuition payments made by Concordia's students. Concordia owed HotChalk, payable on a weekly basis (with certain amounts deferred, as discussed below), 60% of Concordia's tuition revenue; and HotChalk was responsible for a proportional amount of operational expenses. In exchange for the weekly revenue-share payments, HotChalk provided, among other things, services related to supporting Concordia's marketing, recruiting, enrollment, student support services, and information technology, all supervised and controlled by Concordia.

HotChalk's Amended Petition quoted above refers to the 2013 *qui tam* lawsuit brought by former employees of HotChalk. [7] That lawsuit is enlightening as it describes the conduct of both HotChalk and CUP related to HotChalk's recruitment of students, and provision of enrollment activities, educational curriculum, faculty, and classes for CUP's online degree programs. The enrollment specialists at HotChalk worked out of a Phoenix call center and had authority to enroll students for CUP, ignore CUP's standard admission policies, and increase enrollment numbers to increase HotChalk's compensation.

The result of this 12 year relationship was a disaster for CUP. Multiple Oregon print media publications provide an eye-opening financial and educational perspective. Writer Molly Young of *The Oregonian/OregonLive* analyzed this relationship as early as October 21, 2016. [8] Young's observations as to CUP included the following:

> The Northeast Portland college now bestows more Master of Education degrees than any other public or private nonprofit school in the country, thanks to a popular online teaching program that helped quadruple the college's revenues in five years.
>
> The meteoric growth came at a price to Concordia. The small Christian school has paid more than

> $160 million to a private contractor hired to handle aspects of the online graduate degree program. Students know little about the Silicon Valley company or its outsized role.
>
> Concordia and HotChalk Inc. drew rebuke last year after the U.S. Education Department concluded a two-year investigation into their relationship. A federal prosecutor said the arrangement appeared to violate laws that keep colleges from paying incentives for recruitment, or from outsourcing more than half an educational program to an unaccredited party.
>
> "HotChalk would recruit students, cover all enrollment activities and provide the educational curriculum, faculty, and classes" for at least some of Concordia online degree programs, said a July 2015 letter that summarized the government's findings.
>
> Concordia and HotChalk soon signed a $1 million settlement that admitted no wrongdoing in the case, started as a whistleblower suit by former HotChalk employees.
>
> . . .
>
> Concordia denied all of the allegations in the federal lawsuit, and HotChalk said it is not possible to draw accurate conclusions from the case.
>
> Concordia spokeswoman Madeline Turnock said in a written statement that HotChalk has no role in enrollment, admission or financial aid decisions at Concordia, and the college provides "100 percent" of its academic programs.
>
> An in-depth analysis by The Oregonian/OregonLive, drawing on publicly available documents and cached versions of the university's web pages, uncovered an unusual degree of interdependence between Concordia and its contractor. Together, the two transformed the university.
>
> . . .
>
> Federal student loans heavily financed the growth. Concordia students in 2014-2015 received more from the government's leading graduate loan program than students at any Ivy League school but Columbia.
>
> Between the tax years that began in July 2009 and in July 2014, Concordia's annual revenues grew fourfold to $173 million, and its year-end surplus went from $1 million to $10 million, ...
>
> . . .
>
> Concordia's growth strategy was not without risks.
>
> A dramatic enrollment increase, a shift toward teaching most students online and heavy spending on marketing are all warning flags identified by the National Consumer Law Center, a nonprofit consumer advocacy group, in a 2014 report about online education.
>
> . . .
>
> The degree of Concordia's financial connection to HotChalk appears to be unusual, based on a review of IRS filings.

Now, the post mortems of CUP's collapse are brutal. Derek Newton of *Forbes*, relying in part on reporting by *The Oregonian*, stated in "A New Normal, A College Undone By Greed": [9]

> . . . the school was eaten alive, devoured from the inside by a for-profit company it hired to run its online programs.
>
> . . . School leaders "bet the college's future" on a deal with a company called HotChalk. In the deal, HotChalk would manage many, even most, of the details of the college's online programs, specifically their graduate programs in education. Things such as marketing, recruitment, enrollment, course design and delivery would all be handled by the outside company. In exchange, HotChalk would get a cut of the tuition revenue.
>
> . . .

> . . . The school paid the company $62 million in 2014, representing "nearly half of all tuition and other revenue" the school took in, according to the paper.
>
> . . .
>
> . . . Even many public schools are sharing revenue with, and shoveling hundreds of millions of dollars to, private, for-profit companies to "manage" their online programs. Some of those agreements call for the private company to take 50%, 60% even 80% of student tuition.
>
> . . .
>
> At HotChalk, for example, three of the six "senior leaders" listed on its website previously worked for Apollo Education, owner of the infamous for-profit, largely online, University of Phoenix. . . . Most of the non-Apollo leaders have close ties to Bertelsmann, which invested $230 million in the company in 2015.
>
> . . .
>
> . . . Much of the heartburn over the closure there has been focused on the decision by school leaders to move ahead with a local fundraiser when they knew the school may close, to wait until after the "drop" deadline to tell students, to have handsomely paid administrators while the school cratered, and to have signed such a bad deal with HotChalk in the first place.
>
> . . . What was bad was signing a revenue-sharing deal with a for-profit company in the first place.

Synod's Pending CUS Governance Model Proposal

Synod, at its 2019 convention, passed several resolutions directed to university education.[10] These included 7-01A To Amend Bylaws Related to Structure and Governance of the Concordia University System, 7-02 To Nurture Our Lutheran System of Higher Education, 7-03 To Direct a Collaborative Process to Propose a New Governance Plan, and 7-04A To Advance the Prior Review Process for CUS Institution Presidential Candidates.

This process has proceeded with the "Official Notice: CUS governance model proposal and request for comment" that Synod posted on March 12, 2021. Synod's Board of Directors had approved dissemination of an initial governance model that had been developed by the 2019 Res. 7-03 Committee to "Strengthen all CUS institutions' connection to the Synod" and "to strengthen [their] confessional Lutheran identity." The objective of this effort is to obtain comments from members, officers, boards, commissioners, and other agencies of Synod, resulting in the submission of a final proposed governance model as an overture to the 2023 Synodical Convention.

Where Are We Now?

Synod is asking us to consider Resolution 7-03 and provide comment and feedback in preparation for the 2023 Convention. This request has to be considered in relation to the pending HotChalk litigation. HotChalk is claiming that Synod, LCEF, and CUS caused the failure of CUP as legal alter egos of CUP by interfering in CUP's process of choosing a new president of CUP, and refusing to provide financing to CUP until CUP closed its "Gender and Sexuality Resource Center." When CUP failed to do so, HotChalk claims that Synod and LCEF forced CUP to close by starving CUP of operating funds.

Apart from the dubious factual merit of HotChalk's claims, the pending case will not go to a jury trial until April or May 2023. That jury trial will likely take one month. In the meantime, the trial judge will be making rulings on motions to dismiss by Synod, LCEF, and CUS. In December 2021, the trial judge will consider motions by Synod, LCEF, and CUS to dismiss HotChalk's claims, in part, based on First Amendment grounds. One should also add that the cost of attorney's fees in defending against HotChalk will be enormous.

Final Observations

Much of the attention given to CUP over the years has been directed at the pro-LGBTQ stance of CUP and the Gender and Sexuality Resource Center. The concerns that so many have expressed are legitimate and Biblical.

What is missing from these discussions and debates is the reality that CUP's delegation of its admission process to HotChalk made it inevitable that CUP would accept significant numbers of students who were neither Christian nor committed to standards of Biblical conduct and character.

What is also missing is that CUP's ASA with HotChalk, as it was in effect at least as early as 2013, and renewed in February 2018, doomed CUP to financial failure. The U.S. Department of Education's regulatory action against CUP and HotChalk should have been sufficient for CUP to terminate its relationship with HotChalk prior to 2018. These two issues of HotChalk's failure to comply with federal law in compensating its enrollment specialists and the one-sided ASA in HotChalk's favor in being paid 60% of CUP's tuition receipts, should have been warning signs to Synod, LCEF, and CUS as early as 2016 that CUP was pursuing a vision that would inevitably result in its disintegration.

Conclusion

Quite simply, CUP should have applied the wisdom of Proverbs 6:27. "Can a man take fire into his lap without getting his clothes burned?"[11] Instead, CUP took fire into its educational, religious, and financial bosom when it contracted with HotChalk. The "burning" of its clothes was inevitable.

Disclaimer

The opinions the author has expressed are solely his own. The content is based primarily on public information. The primary sources of this information include the filed pleadings and court decisions in HotChalk, Inc. v. Lutheran Church - Missouri Synod, *et al*., Case No. 20cv15620, Circuit Court, State of Oregon, Multnomah County. The author listened to a lengthy public hearing in this case on September 17, 2021. Other sources include the extensive coverage of CUP in numerous Oregon print media outlets going back to 2016, as indicated in the footnotes. The author is not privy to any confidential information related to the pending HotChalk case described in detail above. The author has not talked with any attorney or known witness involved in the pending HotChalk case.

The author has made numerous references to the pending case and the 2013 case in the U.S. District Court, Arizona. Pleadings in those two cases provide valuable factual and legal background. But pleadings are not evidence.

James D. Runzheimer, Attorney
Arlington, TX

---

1 https://www.bizjournals.com/portland/news/2020/02/10/concordia-university-to-close-at-end-of-semester.html by Mathew Kish.

2 *Ibid*.

3 *Ibid*.

4 *Ibid*.

5 HotChalk, Inc. v. Lutheran Church - Missouri Synod, Case No. 20cv15620, Oregon Circuit Court, Multnomah County.

6 HotChalk's Amended Petition fails to disclose that the two entities were assessed a penalty of $1 million. HotChalk paid the entire amount.

7 Regina Calisesi, et al., v. HotChalk, Inc., Concordia University, *et al*.; Case 2:13-cv-01150-NVW; U.S. District Court, Arizona.

8 https://www.oregonlive.com/portland/2016/10/concordia_gained_thousands_of_new_students_--_and_a_federal_inquiry.html

9 https://www.forbes.com/sites/dereknewton/2020/03/01/a-new-normal-a-college-undone-by-greed/

10 Proceedings of the 2019 (67th) LCMS Convention, Resolutions, pages 165-174.

11 AAT, William F. Beck, Leader Publishing Company, New Haven, Missouri. Copyright 1976, Mrs. William F. Beck.