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Career Education Corporation: As CEO, Todd Nelson Brings Growth in Enrollments and Drop in Quality Metrics; Closer Look at FTC Settlement

"As soon as Todd Nelson came in and brought in John Kline, everything just went to a sales environment," says one former American InterContinental University (AIU) student advisor in Illinois who left in 2018 because of what she says was an unhealthy work environment. Kline is President of AIU.

School quality data, interviews with former employees and interviews with higher education experts suggest that since Nelson took the over as CEO of Career Education Corporation (CECO) in 2015, CEC-owned schools American InterContinental University and Colorado Technical University (CTU) have enjoyed an uptick in growth but have declined in quality metrics—spending on instruction, number of dropouts and bad debt all worsened, sometimes dramatically so.

The Todd Nelson playbook at Career Education Corporation is reminiscent of the strategies that Nelson implemented as CEO of University of Phoenix and, after that, as CEO of Education Management Corporation (EDMC). University of Phoenix was plagued by government investigations and litigation shortly after Nelson resigned as CEO in 2006.

EDMC ended up in bankruptcy following Nelson's tenure as CEO from 2007 to 2013. EDMC, like University of Phoenix, was plagued by government investigations and litigation following Nelson's departure as CEO.

On August 27, Career Education Corporation settled with the FTC for $30m related to illegal misrepresentations made by CEC and companies it worked with in the lead generation industry. CEC said in a recent 8k that it did not expect the settlement to change its business outlook.

In an interview, an FTC staff attorney said that CEC had to "substantially change its compliance structure" to meet the terms of the settlement. The settlement is enforceable following a court order which is expected to happen within the next few weeks.

For this article, *The Capitol Forum* interviewed 5 former CEC employees, an FTC staff attorney, and several education policy experts.

CEC did not respond to multiple requests for comment sent to their press and investor relations teams.

CEC By the Numbers

Since Nelson took over as CEO at Career Education Corporation, total enrollment has jumped by about 2,000 students, using data from SEC filings for Q2 2015 and Q2 2019.

However, that growth has come at a cost. To get the 2,000 student increase in total enrollment, CEC has seen the number of students dropping out or graduating grow by 4,300, from 35,320 a year (from 3Q 2014-2Q 2015) to 39,680 a year (from 3Q 2018-2Q 2019).

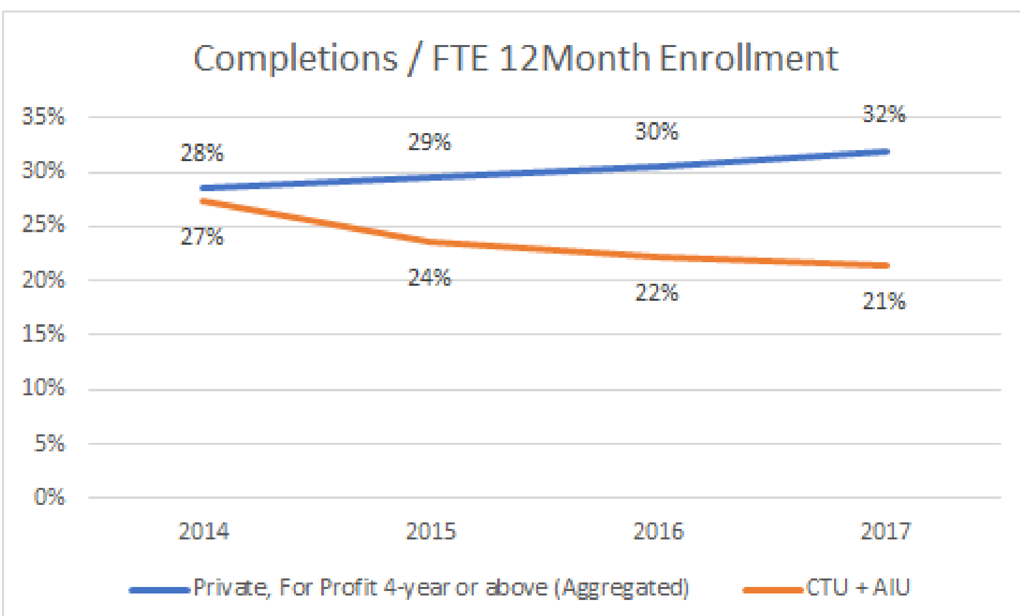
Higher education experts look to metrics like spending on instruction, retention, and student defaults to assess the quality of a school's outcomes. Career Education Corporation also reports a bad debt number in its quarterly filings that likely is an indicator of student outcomes, with higher bad debt likely being associated with worse student outcomes.

Below *The Capitol Forum* provides snapshots of CEC's quality metrics before and after Nelson's arrival as CEO.

Completion Rate

Ben Miller, a student loan expert and former Department of Education official who now works for the progressive think tank The Center for American Progress, says one of the best ways to measure retention is to take the number of degrees/certificates awarded and divide that by the number of FTE students.

Here are those completion calculations for CTU and AIU online based on Miller's recommendation from 2014-2017 compared to the average of all private, for-profit four-year schools:



Source: IPEDS, The Capitol Forum

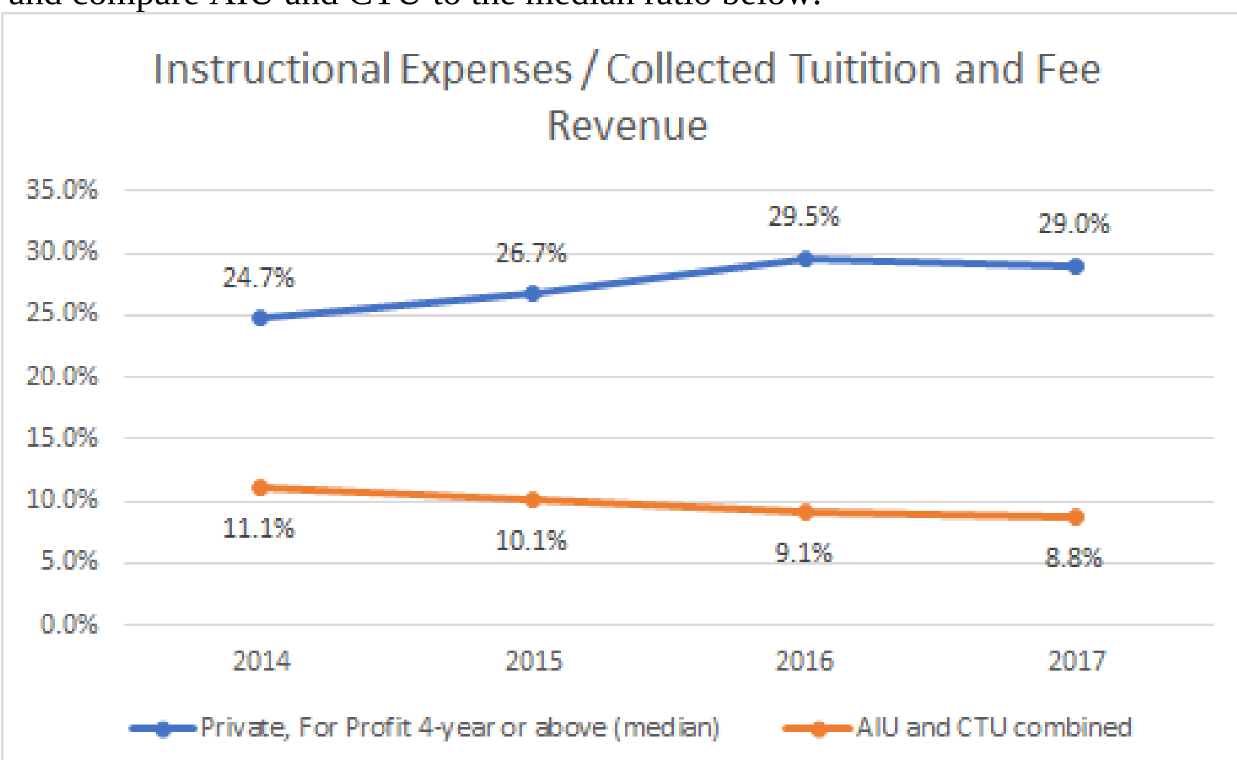
Completion rate low compared to other for-profits. In 2014, CEC's completion rate is roughly in line with the average four-year for-profit school, but by 2017, CEC's completion rate is significantly lower at 21 percent versus the four-year for-profit school average of 32 percent.

<u>Instructional Spending</u>

The Century Foundation issued a report earlier this year titled "Examining Instructional Spending for Accountability and Consumer Information Purposes." The Century Foundation looked at data from the Department of Education's Integrated Postsecondary Education Data System (IPEDS) to assess school quality by looking at instructional spending as a proportion of tuition and fee revenue.

The Century Foundation used the ratio of Instructional Expenditure to "collected tuition and fee revenue" to analyse the share of funds collect for instruction that actually go towards instructions expenses.

Using the Century Foundation's methodology, we calculated those ratios for all four-year for-profit schools and compare AIU and CTU to the median ratio below.



Source: IPEDS, The Capitol Forum

Instructional spending lower than average four-year for-profit schools. While CEC's instructional spending ratio for AIU and CTU in 2014 starts off low at 11.1 percent versus the median across four-year for-profits of 24.7 percent, the gap widens over the following three years, with AIU and CTU in 2017 combining for an 8.8 percent instructional spend ratio versus the median across four-year for-profit schools of 29 percent.

Bad Debt (Quarterly From 1Q 2014-2Q 2019)

Fiscal Year	Bad Debt Expense Quarterly ($000)
2019 Q2	11,432
2019 Q1	11,709
2018 Q4	10,361
2018 Q3	7,900
2018 Q2	6,697
2018 Q1	6,982
2017 Q4	5,920
2017 Q3	6,404
2017 Q2	6,888
2017 Q1	8,224
2016 Q4	8,684
2016 Q3	8,432
2016 Q2	5,217
2016 Q1	9,552
2015 Q4	6,454
2015 Q3	6,388
2015 Q2	4,863
2015 Q1	4,275
2014 Q4	-4,266
2014 Q3	6,698
2014 Q2	6,557
2014 Q1	5,852

Source: SEC Filings, The Capitol Forum

Bad debt increases after 2015. According to SEC filings, CEC's bad debt has steadily increased following Nelson's arrival in 2015. It has grown from roughly $6.4m in 3Q 2015 to $11.4m in 2Q 2019.

According to [Brad Safalow](), founder of PAA Research, bad debt at for-profit colleges can be related to the amount that a student owes beyond what is covered by student aid.

Key upcoming quality metric: FY2016 Cohort Default Rate. Cohort Default Rate (CDR) measures the defaults for any given cohort of students that either drop out or graduate in a fiscal year, with the FY2015 CDRs measuring defaults for students graduating or dropping out during the 2014-2015 school year. Since Nelson arrived in 2015, the FY2016 cohort default rates (expected to be released in September) will be the first CDRs that reflect the students that Nelson's strategy has brought to the school.

Here are the Cohort Default Rates for FY2013, 2014 and 2015:

	FY2013	FY2014	FY2015
CTU	14%	15.70%	19.50%
AIU	14.70%	16.20%	19.70%

Source: Department of Education, The Capitol Forum

The average for-profit cohort default rate for those years was 15 percent, 15.5 percent, and 15.6 percent, respectively.

Nelson's Arrival

Overall, the data analyzed by *The Capitol Forum* shows higher growth at the expense of certain quality metrics. According to former employees, the business culture at AIU changed following Nelson's arrival more than the numbers tell.

"We did a huge hiring push after Todd Nelson came on," said the former AIU student advisor in Illinois. "We opened up a whole new campus outside of Phoenix, Arizona, because that's where Todd and John Kline lived." She added that roughly 100 new admissions advisors were brought in at the new campus, but that they didn't bring in new hires to focus on retention.

Sales culture leads to retention decline. A former AIU admissions advisor who worked in the enrollment center in Chandler, Arizona called it a "turn and burn organization." He says he was terminated recently for answering a prospective student's question about student loans.

"People looking for work see a banner ad on their computer or mobile phone that says, 'Need a job?'" explained the admission advisor. Those ads are posted by lead generation companies that contact the respondents. According to the admission advisor, the lead generator would get a hot lead on the phone and forward the call to AIU where it was his job to persuade the caller to get interested in going to school and get them enrolled using a persuasive script.

"The script is very influential and coercing," said the admissions advisor. "I would keep questioning. It puts prospective student's back up against the wall. That's how a lot of enrollments take place."

“It’s really a shitty place. Get them enrolled and funded. Most of these people have no business getting loans,” he added. “Many of my enrollees—I estimate over 50 percent—dropped out during the very first class which is an introductory class.”

The AIU student advisor in Illinois said it was hard to keep retention high in a sales-driven environment.

The specialist explained that while salespeople could be incentivized specifically to meet quotas, “they could be fired for not meeting admissions goals, and they were.” She added, “People were fearful of their jobs and enrolling anyone they could enroll.”

She said that her job was to be responsible for retention, and that a sales-driven environment meant that there was no commitment to ensuring that students who enrolled could succeed in the school. “When there was no quality of students that really understood what they were going to be doing, it was very hard to get the retention piece right.”

She said she thought the student attrition was a reflection of the poor lead quality, aggressive sales practices and pushing students to enroll who weren’t committed.

According to a second former AIU academic advisor who worked in 2017 and 2018, “Most of the admissions advisors had come over from other CEC school's like Le Cordon Bleu or other schools that had been closed like Everest and ITT.”

According to the second former AIU academic advisor, “retention was horrible.”

“I’d follow on average 30 to 40 students each quarter and I tracked them on a spreadsheet I was keeping on my own,” the advisor told us. The best outcome the advisor had under his watch was seven students still hanging on after four consecutive quarters.

“That was one of the moments when I realized this isn’t right,” the advisor said. “They are pushing way too hard on the front end.”

When asked what was behind the student attrition, the second former AIU academic advisor said that most students just disappeared after they enrolled. He would call and email but get no response.

When he could find out why students failed, their explanations were sobering. Some students had lost their phone or internet connections. Some had become homeless. Some just couldn’t handle the switch from managing the workload of one class at a time to two classes contemporaneously.

A former student success coach for CTU said that some enrolled students were "woefully unprepared" to attend school, especially in an all online environment. He explained that there were students without devices and students without "resources or basic tech knowledge," and even some homeless students. He said that he would personally work with students who did not have the tools or resources to be successful in their program to make sure they withdrew before there was a financial or academic penalty.

Lead generation at AIU. "John Kline was of the opinion that it shouldn't matter what kind of lead it is," said the former AIU student advisor in Illinois. She explained that AIU uses a lead score, with A and B scores yielding very good conversion rates (approximately 30 percent to 50 percent), and D to E scores leading to conversion rates somewhere in the range of 2 percent to 3 percent.

"Most of the leads, 80 percent or so, that come in for admissions advisors are in the D through E category, which is a very, very low category," she said.

"John Kline's mentality is that he hates lead scores and that it shouldn't matter at all when it comes down to enrolling because if you get a student on the phone, you should be able to convince them to go to school, start, and graduate," said the former AIU student advisor in Illinois.

In the opinion of the former AIU student advisor in Illinois, however, "that's just not the reality of the world—a lot of these students have no idea what they're getting themselves into." She concluded, "They're falling for the dream."

Highlights from August 27 FTC Complaint, Settlement, and Interview with FTC Official

In an August 1 8-K, Career Education Corporation previewed an upcoming settlement with the FTC over the company's lead generation practices. The company concluded that "The Company does not expect the Agreement [with the FTC] to negatively impact its previously provided 2019 adjusted operating income outlook."

Given the importance of lead generation to the sales push implemented in 2015, it is hard to piece together how significant compliance changes wouldn't affect CEC's business outlook. Further, as mentioned previously, FTC staff attorney Quinn Martin explained that CEC had to "substantially change its compliance structure" to meet the terms of the settlement.

CEC dragged its feet in making changes. In its complaint, the FTC explains that CEC did not change its business practices even after it was notified that the company and its lead gen partners were potentially engaged in illegal practices.

Specifically, the complaint said, "CEC does not review its lead generators' marketing materials, including telephone scripts and websites, before hiring them to generate leads on its behalf. It has not changed this practice even after it has been on notice that its lead generators are engaging in illegal conduct to procure leads for CEC."

In an interview with *The Capitol Forum*, Martin explained that CEC did not change its practices after it received a CID from the FTC in 2015 and also did not change its practices after the FTC and DOJ brought enforcement actions against three CEC lead generators.

However, Martin added that it is not unusual for companies to continue with practices if the companies believe those practices do not constitute illegal conduct.

Landmark case. Martin said that this enforcement action is a landmark case because it is the first time the FTC is holding an education company liable for the conduct of a lead generator. He said that this case puts companies in the lead generation ecosystem on notice and that companies' "days of putting their head in the sand are over" when it comes to not knowing the type of conduct their lead generators are engaged in.

The consent agreement lays out extensive reporting and compliance criteria that Martin said required CEC to substantially change its compliance structure. Among other things, the consent agreement prohibits CEC from using leads that make any misrepresentations and compels the company to perform exhaustive record-keeping related to its lead generation practices.

Martin explained that CEC has assured the FTC that its new compliance system is already in place.

Complaint. Allegations made in the complaint match up with concerns expressed by the former employees interviewed by *The Capitol Forum*.

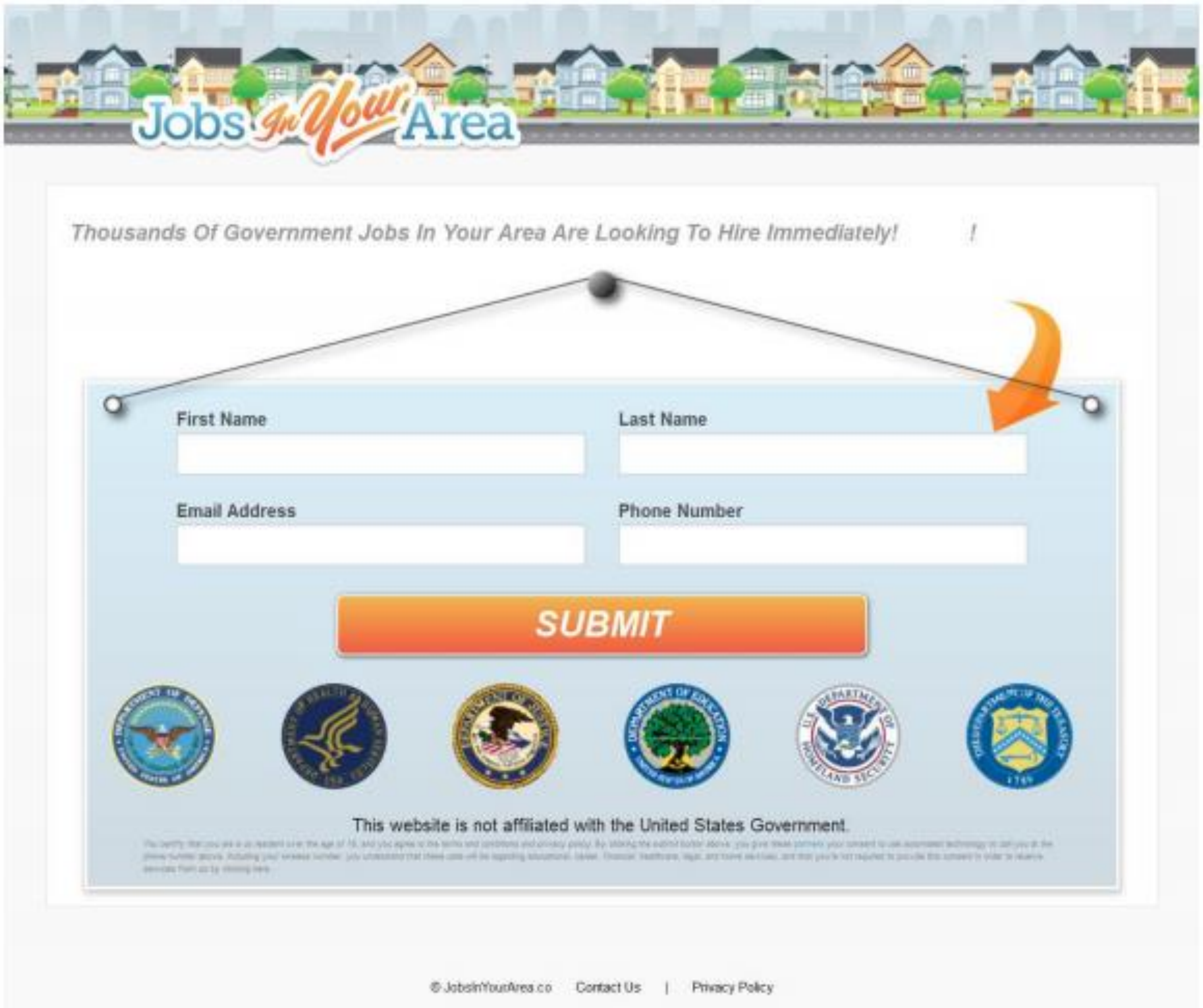
The FTC's allegations against CEC focused on how CEC worked with unscrupulous lead generation companies and then CEC continued to engage in deceptive practices when contacting those leads.

According to the complaint, one of CEC's lead generator partners, SKFM, deceived customers by "operating numerous websites that posed as official recruiting websites, including army.com, armyreserves.com, air-force.com, armyenlist.com, airforceenlist.com, marinesenlist.com, nationalguardenlist.com, and navyenlist.com." When customers looking to enlist went on the site, their information was collected and sent to CEC and other postsecondary schools so they could be targeted as a prospective student.

Source: FTC Complaint

According to the complaint, CEC worked with another lead generator, Expand, which “targeted consumers looking for jobs and lured them into submitting personal information by misrepresenting that it could assist them in applying for jobs, claiming that it pre-screened consumers on behalf of specific prospective employers.”

CEC also worked with a lead generator called Edutrek, a company that “generated leads originated from websites that claim to help consumers apply for jobs, health insurance, unemployment benefits, Medicaid coverage, or other forms of public assistance.”



Source: FTC Complaint

Will buying Trident University help CEC address quality issues? In March, CEC announced that it was buying Trident University for between $35 and 44 million.

In an April 2019 investor day slideshow accompanying a presentation by Nelson, CEC acknowledged that one of the strategic reasons for acquiring Trident University, a school with 4,000 students that focuses on graduate-level degrees for military-affiliated students, is that Trident has "Expertise in organic lead generation" and has the "ability to share best practices" with CEC in that area.

During the presentation, Nelson also explained that Trident "is regionally accredited through WSCUC and, obviously, have some of the lowest CDRs in the industry."

Following the most recent FTC settlement, whether the Trident acquisition leads to improvements in lead generation and quality across CEC schools, or whether Nelson's leadership causes an increase in enrollment and a decrease in quality for Trident programs is likely to be a topic of interest for policymakers and law enforcers going forward.