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HURN - Q2 2012 Huron Consulting Group Inc. Earnings Conference Call

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PRESENTATION

Operator

Good afternoon ladies and gentlemen, and welcome to Huron Consulting Group's webcast to discuss financial results for the second quarter 2012. At this time all conference call lines are on a listen-only mode. (Operator Instructions). As a reminder, this conference call is being recorded.

Before we begin, I would like to point all of you to the disclosure at the end of the Company's news release for information about any forward-looking statements that may be made or discussed on this call. The news release is posted on Huron's website. Please review that information along with the filings with the SEC for a disclosure of factors that may impact subjects discussed in this afternoon's webcast. The Company will be discussing one or more non-GAAP financial measures. Please look at the earnings release, and on Huron's website for all of the disclosures required by the SEC, including reconciliation to the most comparable GAAP measures.

Now I would like to turn it call over to Jim Roth, Chief Executive Officer and President of Huron Consulting Group. Mr. Roth please go ahead.

Jim Roth *- Huron Consulting Group - CEO, President*

Good afternoon, and welcome to Huron Consulting Group's second quarter 2012 earnings call. With me today are Mark Hussey, our Chief Financial Officer, and Patty Olsen, our Corporate Vice President of Human Resources. Jim Rojas, Chief Operating Officer will not joining us today due to a prior commitment. I will spend a few minutes talking about our Q2 performance and our outlook for the rest of the year, and then turn it over to Mark for a more detailed discussion of the financials. As anticipated, our second quarter performance was impacted by several large engagements in our healthcare practice for which performance based fees will not be recognized until later in the year. All of our segments with the exception of financial consulting, are performing at a pace consistent with our expectations. I recognize the challenge for our investors stemming from the ebb and flow of healthcare revenue.

So I am going to go straight into a discussion of our segment performance in order to provide color on our results. Revenue in the health and education consulting segment was $9.6 million lower in the second quarter this year as compared to the second quarter 2011. The primarily factor driving the lower revenue was the fact that we had $34 million in performance based fees in the second quarter last year, compared to only $14 million in the second quarter this year, a decline of $20 million.

Let me pause here briefly to talk about performance based revenue in the healthcare practice. Every month we perform a detailed review of every project that is expected to generate performance based fees. During that review, we evaluate the extent to which our efforts remain on target to generate performance based fees, along with the timing and magnitude of those fees. Our most recent internal forecasting review continues to indicate that we are on track to generate performance based fees for the year consistent with our internal estimates.

There are other factors that we look at within this segment, that provide us with additional comfort that we are on pace to achieve our planned results. Those factors include the size of our revenue backlog, and the extent to which that backlog continues to build. The utilization rate of our personnel, and the level of new assessments that we are performing for prospective clients. All of these factors, backlog, utilization, and new assessment are projecting positive trends for the practice consistent with our guidance.

The leaders of our healthcare business meet quarterly with many of our clients and I participate in some of those meetings with our largest healthcare clients. Our recent meetings indicate that our efforts are on track to achieve expected results, and that the clients are comfortable with result to date. From a market perspective demand for our services continue to be strong.

Some of the hospital we serve are facing severe financial challenges. While those that are generating healthy margins are facing increasingly difficult regulatory and competitive challenges that are creating the need to reduce costs and improve revenue. Combined with the rapidly evolving transition and provider business models from fee for service, to value based billing we expect the trends for our healthcare practice to continue to remain positive for Huron.

Our Higher Education and Life Sciences practice had a solid second quarter highlighted by its largest revenue quarter ever. Universities are undergoing a rapidly evolving business environment. The drivers of the change include declining public funding, the onset of new and very expenses online courses, flat to declining federal research funding, and pressure to limit tuition increases. Collectively these pressures are forcing all universities to evaluate their strategy and operations, actions that are at the core of our service offerings in the higher education practice. There was nothing that gives us any reason to believe that these pressure will abate in the near or intermediate term, and we are confident that this practice will finish the year strongly.

Our Legal Consulting segment finished another strong quarter. Within ediscovery services growth was driven by some of our financial service clients that continue to generate strong demand, and we continue to expand the number of global clients within our portfolio. The recent acquisition of AdamsGrayson will enhance our ability to serve the DC marketplace where many large regulatory disputes and investigations are centered. And we expect the acquisition to be accretive to revenue and earnings.

Our Advisory Practice within the Legal Consulting segment had another strong performance during the second quarter. The Advisory Practice has improved its revenue for the fifth quarter in a row, and we are pleased with the way it is positioned for continued growth. Finally, our financial consulting segment had a challenging quarter, while the restructuring and turnaround business and many of our competitors have been similarly challenged, we will continue to monitor this practice closely and are taking the necessary steps to get it back on pace to acceptable growth and profitability levels.

We have narrowed our annual revenue guidance to $620 million to $640 million before taking into account the AdamsGrayson acquisition. Although still within the range of our initial annual guidance, we feel more comfortable at the lower end of the range given anticipated shortfalls in financial consulting, and the potential for some healthcare revenue to be deferred until the first quarter of the next year. We do not provide performance based fee guidance, but we expect our performance based revenues in the second half of the year to be significantly higher than the first half. Similar to what we experience in 2011 following the first quarter we expect a sizable pickup in the performance based revenues during the balance of the year, as we realize the benefits of the current productive hours being spent on engagements.

Finally we remain on pace to achieve our recruiting goals for 2012. Our attrition rates, which typically have been lower than industry norms, had actually been lower than we expected further reinforcing our confidence that our employee are very engaged, and support the achievement of revenue and earnings goals for the year. Now let me turn it over to Mark to discuss our second quarter results.

Mark Hussey - *Huron Consulting Group - CFO*

Thank you, Jim. Good afternoon everyone. Let me begin by discussing a few housekeeping items. Consistent with our past practice I will be discussing our financial results, primarily in the context of continuing operations. I will also be discussing non-GAAP financial measures, such as EBITDA, adjusted EBITDA, adjusted net income, and adjusted EPS. Our press release, website, and 10-Q each have reconciliations of these non-GAAP measures to the most comparable GAAP measures, as well as a discussion of why management uses these non-GAAP measures.

I will now walk you through some key financial results for the quarter. Revenues for the second quarter of 2012 were $144.7 million compared to $153.1 million in the same quarter of last year. Sequentially second quarter revenues increased about 4% from $138.6 million in the first quarter. Last year's second quarter included a record $33.9 million in performance based fees, and in this year's quarter performance based fees were $13.8 million.

Second quarter 2012 EBITDA was $19.9 million, or 13.8% of revenues, compared to $28.0 million, or 18.3% of revenues in the comparable quarter last year. The decline in margin reflects the lower level of performance based fees coupled with a 13.3% increase in our average full time billable headcount. These resources were relatively productive as measured by our utilization levels. For Q2 2012 utilization was 74.5% compared with 71.9% a year ago. However due to the lower level of performance based fees in Q2 2012, our average billing rate declined to $210 per hour, from $270 per hour in the same quarter last year. I will provide some additional color when I discuss the operating segments in a few moments. Adjusted EBITDA came in at $21.5 million in Q2 2012 for 14.9% of revenues compared to $30.8 million in Q2 2011, for 20.1% of revenues. Adjusted EBITDA excludes a number of items which are listed in our press release. Sequentially adjusted EBITDA increased 83% over Q1, while adjusted EBITDA margin increased 640 basis points.

Operating income was $14.7 million, or 10.2% of revenues in Q2 2012, compared to $22.3 million, or 14.6% of revenues in Q2 of 2011. Net income from continuing operations was $6.3 million, or $0.28 per diluted share in the second quarter 2012, compared to $9.2 million, or $0.43 per diluted share in the same period of 2011. Adjusted Non-GAAP net income from continuing operations was $8.2 million, or $0.37 per diluted share in the second quarter 2012, compared to $12.1 million, or $0.56 per diluted share in the same period of 2011.

Our effective income tax rate decreased to 49.7% in the second quarter of 2012from 51% in the second quarter 2011. The effective rates for both periods were higher than the statutory rate, inclusive of state income taxes, due mainly to the impact of foreign losses with no tax benefit, and certain non deductible expenses.

Now let's look at how each of our business segments performed in the quarter. The health and education consulting segment generated 65% of total Company revenue during the second quarter of 2012. This segment posted quarterly revenue of $94.5 million for the second quarter of this year, compared to $104.1 million for the second quarter of 2011, a decline of $9.6 million including a decrease of performance based revenues of $20 million. The operating income margin for health and education consulting was 30.2% for Q2 2012 compared to 35.4% for the comparable quarter in 2011. The decrease in margin reflects the lower level of performance based fees and higher compensation expense associated with an increase of average full-time billable consultants of 16.7%. The timing of performance based fees impacted most of the financial measures in the segment, and we expect a significant pickup in these revenues in the second half of 2012.

As Jim said, the healthcare practice in particular is experiencing solid marketplace demand, utilization for this segment increased from 73.6% thin second quarter 2011 to 76.6% in the second quarter 2012.

Our Legal Consulting segment generated 32% of total Company revenue during the second quarter of 2012. This segment posted revenue of $45.9 million in the second quarter of 2012, up 14.8% from $40 million in the comparable quarter in 2011. The momentum that we experienced during the first quarter in our advisory business continued into the second quarter. Our document review and electronic discovery business also experienced solid growth.

Our full-time billable consultant utilization rate in this segment increased to 68.7% during Q2 2012, from 54.9% a year ago, reflecting increased demand in the Advisory business. The operating income margin for our Legal Consulting segment came in at 27.2%, compared to 24.1% in last year's second quarter, reflecting lower contractor expense, partially offset by higher compensation in technology expense as a percentage of revenues.

During the second quarter of 2012 our financial consulting segment generated 3% of total Company revenues. This segment posted revenues of $4.3 million in Q2 2012, compared to $9 million in the same quarter of last year. The operating income margin for financial consulting declined to a negative 7.9% in Q2 2012, from a positive 30.8% in the same quarter of 2011, primarily due to higher salaries and related expenses as a percentage of revenues.

As Jim discussed the financial consulting segment had several initiatives under way to improve the segments financial performance and broaden its service offerings. We believe the professionals and service offerings remain relevant to the market place, and we expect performance to improve in the second half of this year and into 2013.

Now turning to the balance sheet and cash flows. We are pleased with several measures including DSO for the second quarter which came in at 62 days or about 9 days better than Q1. Cash flows from operation for the first half of 2012 were $28.5 million, and particularly strong in the second quarter at $41 million. For the full year we expect cash flows from operations to be about $80 million to $90 million. As Jim mentioned, we have narrowed the ranges of our previous full year guidance based on our current best estimates.

For full year 2012 we anticipate revenues before reimbursable expenses at a range of $630 million to $650 million this amount includes the AdamsGrayson acquisition that closed on July 2nd. We anticipate EBITDA in a range of $107 million to $112.5 million, and adjusted EBITDA in a range of $116 million to $121.5 million. We expect GAAP diluted earnings per share in a range of $1.90 to $2.05, and non-GAAP adjusted diluted earnings per share in a range of $2.30 to $2.45. Weighted average diluted shares for 2012 are estimated to be approximately 22.4 million and our guidance on the effective tax rate remains at 45% for the full year.

Let me conclude with a couple of final notes, last week we reached a settlement with the SEC resolving its investigation into the Company's 2009 financial restatement. The settlement imposed a fine of $1 million. We had previously accrued for this amount in 2011 consequently it will not have any impact on our 2012 earnings. Separately during the second quarter of 2012 we had conducted preliminary settlement discussions with respect to the pending qui tam case, although no settlement was reached as result of the discussion we accrued $1.2 million of litigation settlement expense, our second quarter 10-Q will have further details. This charge is unrelated to the SEC settlement that I previously mentioned.

Thanks everyone. I will now turn it over to the operator for questions. Operator?

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). Your first question comes from the line of Tim McHugh with William Blair. Please proceed.

Tim McHugh - *William Blair & Co. - Analyst*

Mark or Jim can you give us given the new guidance, what type of growth rates for the different segments are you assuming now in that updated guidance?

Mark Hussey - *Huron Consulting Group - CFO*

I will take that one Tim. If you look at the overall guidance the color that we had given you when we originally gave you the guidance was for health and education consulting up between 5% and 10%, and if you kind of back into what the new guidance implies within that segment obviously we just told you that education had a record quarter and is doing particularly well. So a portion of that decline is going to be related to the healthcare business. The Legal Consulting segment of course we just added the $10 million of added AdamsGrayson which we called out for you, and originally we had expected this to be flat to up 5% roughly, and at this point we continue to be confident in that guidance and maybe a little bit more optimistic just based on what we have seen year-to-date. Financial consulting is clearly struggling with where they are right now, although we are very optimistic that for the second half the run rate will improve, will be attributable for a portion of that decline.

Tim McHugh - *William Blair & Co. - Analyst*

Okay. So just on the healthcare or the health and education segment overall, would you be expecting a lower growth rate now, or is it relatively unchanged?

Mark Hussey - *Huron Consulting Group - CFO*

It would be a little lower than we had in our original guidance because we have gone to the lower half of the range.

Tim McHugh - *William Blair & Co. - Analyst*

Okay, I just didn't know how much of that was financials. Okay. Given that, what are you seeing out there as you look at the complexity of the case, Jim you gave us some color about the process you go through and looking at the contingent fees, but are you seeing anything in the complexity of the cases, or the length of time to earn the fees that makes you think they could slip, or more likely to possibly slip in 2013, or is that just trying to be conservative given what has happened so far in the year?

Jim Roth - *Huron Consulting Group - CEO, President*

Tim, this is Jim. Some of the projects that we are working on right now certainly are complex, I think particularly in some of the academic medical centers, the complexity of getting to where you need to go is complex, and we kind of anticipated that. The point we were trying to make in the comments was that when we look back at what it is we need to achieve we are very comfortable that we are going to be hitting on our metrics, for us the question is going to be when and we understand that is an important question to ask. One of the reasons we reduced, put the guidance toward the lower end was to reflect the fact that it is possible that some of the revenues that we originally thought would fall in 2012, may in fact fall into the first quarter of 2013 our current guidance reflects those possibilities.

Tim McHugh - *William Blair & Co. - Analyst*

Okay. Have you seen any signs as you moved from Q2 to Q3 that fees are starting to come in, and any commentary, Mark, you might give between Q3 and Q4 are they particularly Q4 weighted?

Jim Roth - *Huron Consulting Group - CEO, President*

This is Jim again. It is going to be hard for us, Tim, to gauge whether it is going to be Q3 or Q4, when we go out and we have monthly or sometimes quarterly discussions with the clients, it is really is about making sure. When we go out to a particular client it is not as though there is just one contingent task that is going to be the focus of contingent revenue, there are actually multiple tasks that come through, you may have one for labor, you may have one for non labor, you may have one for the revenue cycle, so there is independent pathways towards the contingent revenues and the performance fees on any given project, and each one of them has its own set of complexities and timing and opportunities.

When we have these reviews with the clients, we are going back on a task by task basis, and try to figure out where do we stand, is the client satisfied with the pace at which things are going, are we on pace to get the results that we were looking for, and that collectively gives us some comfort as to where we are going. Even though some of the projects are a little bit more complex, and some of them may in fact be taking a little bit more time than we thought, our sense of our ability to get to where we need to go and what we have committed to the client hasn't changed, and that is part I really want to reinforce because it is an important part of us providing the guidance that we have right now, and the comfort around it.

Mark Hussey - *Huron Consulting Group - CFO*

Tim, in terms of the timing again while we are not specific in terms of which quarter because we don't give quarterly guidance we certainly expect Q3 will be much better than Q2, and we think Q4 will be better than Q3. So I would not characterize this as completely weighted in the very last quarter of the year waiting for everything to happen, there is expectation that Q3 will be better than Q2.

Tim McHugh - *William Blair & Co. - Analyst*

Okay. Thank you.

Jim Roth - *Huron Consulting Group - CEO, President*

Just to be fair on this I think in every one of those work streams that we see for every one of our clients, I mean there were opportunities for things to be missed, we don't do it often but it occurs. There is also opportunities for us to receive more performance fees than we anticipated, that happens as well. And so we have got all of these complexities of timing and amount that kind of have to factor into this, that is why we go through such a detailed assessment on a month by month basis.

Tim McHugh - *William Blair & Co. - Analyst*

Okay great, thank you.

Operator

Our next question comes from the line of Dan Leben with Robert W. Baird. Please proceed.

Dan Leben - *Robert W. Baird & Co. - Analyst*

Great, thank you. Just looking at the bill rate in health and ed outside of contingencies, those numbers are still down a little bit year-over-year, can you talk about any mix issues in terms of more contingent engagements of mix towards education, anything that is impacting that, or is it just a competitive market?

Mark Hussey - *Huron Consulting Group - CFO*

Dan this is Mark. There are a lot of things that affect the bill rate as you can imagine. One of the things is assessments which we normally do at close to a breakeven level, so while it is not a material impact in terms of the bill rate certainly we have indicated a stronger level of assessments year-on-year, but also and probably the more important factor is just the mix of the engagements and what percentage of that comes in the form of fixed fee at the beginning versus contingent at the end. As you look at that we have had some larger engagements that we talked about earlier in the year that were a little bit more toward the higher end of that range, and so that has more impact even if you strip out the contingent fees.

Dan Leben - *Robert W. Baird & Co. - Analyst*

Great. Any changes to activity in the pipeline following the Supreme Court decision, have you seen any flow-through positive or negative to the business?

Jim Roth - *Huron Consulting Group - CEO, President*

Dan this is Jim. It is too early to really sense that. We said upfront that we didn't think we would be impacted that much because the issues that the marketplace issues are having such a big impact on our clients right now, on their performance and the challenges they are up against. I think even if there was a change I think it is frankly it is too early for us to tell.

The nature of the work that we are seeing right now, and frankly I think that this is true in higher ed and healthcare, but it is also true in higher education and that is, the stresses on those industries are really significant right now, I think what happens is the nature of the projects that we are being asked to look at or consider or actually do are probably more invasive than they have been before. They are certainly going to be more challenging and more complex, and so to some extent it takes a little bit more time for the projects to ramp up, but when they ramp up I think for the large part we are seeing projects that are going to be continue to be large and complex and probably last for a period of time. Maybe that is a long way of saying that I am not sure that we have seen anything yet that we can directly contribute to the Supreme Court ruling, but at the same token the marketplace is very vibrant throughout the entire segment right now.

Dan Leben - *Robert W. Baird & Co. - Analyst*

Great. And then on the Legal Segment, the average revenue per FTE ticked up nicely back to the levels you were at in 2010, can you talk about the drivers behind that, is it simply a good set of big cases where you have got a lot of leverage, or help us understand the dynamic?

Mark Hussey - *Huron Consulting Group - CFO*

I think you described it well. I think we have some larger cases that we mentioned in Jim's remarks relative to some of our financial services clients, and as those revenues have grown in the quarter it is reflected in the average that you are seeing.

Dan Leben - *Robert W. Baird & Co. - Analyst*

Okay. Last one for me, just on AdamsGrayson you mentioned the impact to revenue what about adjusted EBITDA and EPS?

Mark Hussey - *Huron Consulting Group - CFO*

We didn't break that out separately at this point, we are going to integrate that into the practice, and so we don't tend to manage it and track this business separately, because it is inherently an ediscovery part of the business, but what I can tell you is that we have actually had a couple of early wins already on a couple of larger clients and we are very excited about it. I think in terms of the service offerings they were primarily review, they didn't do a lot on the processing side so that is clearly an incremental opportunity for us in terms of additional services within their existing base. And then finally as we have talked a little bit about before is the model that they use includes the ability to have onsite customer review, customer managed review, and as a result of that it gives us a new opportunity to get into cases and situations that we might not otherwise have gotten into with the former model we were using.

Dan Leben - *Robert W. Baird & Co. - Analyst*

Great. Thanks guys.

Operator

Our next question comes from the line of Jim Janesky with Avondale. Please proceed.

Jim Janesky - *Avondale Partners - Analyst*

When you look at the operating margin within health and education it was up pretty dramatically sequentially despite revenue only up a couple of million sequentially and therefore so was the absolute dollars of operating income, can you share with us why?

Mark Hussey - *Huron Consulting Group - CFO*

Yes Jim, it is Mark. And again the key driver was each quarter as we adjust our bonus expectations, which is done towards the midpoint of guidance, and with a narrowed range would have reversed some of the bonus expense and contributed to margin.

Jim Janesky - *Avondale Partners - Analyst*

Okay. Did you reverse, and that is because of the slippage into 2013, the potential slippage into 2013 of success fees?

Mark Hussey - *Huron Consulting Group - CFO*

As it relates to the overall new guidance range, yes.

Jim Janesky - *Avondale Partners - Analyst*

Okay. But the core there is no change in the core businesses operating income metrics, right? This was just bonus related?

Mark Hussey - *Huron Consulting Group - CFO*

Yes. Principally bonus related and again we have said this in the past, our process is very well laid out and non discretionary in nature, because we don't have the ability to vary our bonus expense to achieve the margin within the quarter, we are looking to what a full year number is expected to be, so really in the context of that is and as you look at our guidance as well based on first half numbers our bonus expense now will again be at a run rate on a fixed basis here in Q3 and Q4, given that if people are on pace to achieve those numbers and as result of that we should see an improvement in margin as a result of the fixed bonus expense on higher revenue to the extent that we hit the guidance numbers.

Jim Janesky - *Avondale Partners - Analyst*

Okay. Jim, can you help us understand what the difference is year-over-year in the sequential realization of success fees? So last year they started off at about the same level as they were at this year and then jumped up significantly in the June quarter and then backed off in the September and December quarter only by a little bit. What changed the pace of recognition so significantly year-over-year in your mind?

Jim Roth - *Huron Consulting Group - CEO, President*

Jim this is Jim. I wish there was some pattern we could point to in the activities that are going to be generating revenue for us, this is the challenge for us, our first task is to go out and try to generate the projects that are going to be doing the work, once we do that we do our best to try to begin to project. We certainly have a higher complement of projects today that are performance based than we have had in the recent past. It so happens to be that tends to be dominated by probably three, maybe four pretty good sized jobs, all of which for reasons that are not systemic, it just happens to be the way they are, they have performance fees that are going to be paying out more towards the end of these cycles. It is not always the case that way. Each client a different design a different metric in terms of how and when performance fees are measured, or the performances are measured, and therefore the performance fees are paid out. We end up really doing our best to try to gauge the progress through which we are going to be generating the work and hitting the performance targets. We try to judge the complexity of the opportunities.

As we have said before, there could be times where if we spend additional effort on the project and therefore more time, we actually may end up getting more revenue, so we make those decisions as well. Every task on every job has this whole unique set of patterns, we are in a pattern right now, where the biggest projects tend to be pushing revenues out towards the second half of the year. I think it could be next year has a very different pattern, we just don't know. That is best we can tell this is just the cards that we have got right now. As I said as challenging as it is for everyone to try to make sense to where it is going, and what is going to happen. We take a lot of comfort in fact the work that we are doing today, is in fact going very well and that we seem to be on target to hit the performance metrics that we set.

Mark Hussey - *Huron Consulting Group - CFO*

Let me just add to what Jim said that is driven by the mix of engagements all of that said, at any point in time our healthcare practice is incented to hit an annual planned number in terms of EBITDA, and so to the extent that they have to deal with the marketplace mix, they are trying to navigate through all of those challenges to achieve the annual targets that they have out in front of them. Even though the mix has changed over time what they are trying to do is still achieve the overall plan for the year.

Jim Janesky - *Avondale Partners - Analyst*

So when you talk about the guidance range of 5% to 10% growth in health and education possibly being slanted towards the lower end, is that purely because you have success fee timing, or is there a fundamental change in the market?

Jim Roth - *Huron Consulting Group - CEO, President*

There is no fundamental change in the market that we have seen, as strong as it was through last year, it is even stronger this year so there is no change in the market from our perspective, it is really question about timing about some of our biggest jobs.

Jim Janesky - *Avondale Partners - Analyst*

Got it thank you.

Jim Roth - *Huron Consulting Group - CEO, President*

We feel very good about where the market is at and we feel equally good about our ability to competitively serve the market today.

Operator

Our next question comes from line of Paul Ginocchio with Deutsche Bank. Please proceed.

Paul Ginocchio - *Deutsche Bank - Analyst*

Thanks, sorry if I missed this, but you said earlier I think on a previous call you thought performance fees would grow in line with revenue in the healthcare and higher ed division, is that still true? Can you talk about margins in the HEC division headcount up 18% year-on-year? Revenues are sort of down in the first half of the year. What is the outlook for margins? Finally, in ediscovery you talked about mainly financial service projects, can you talk about if you are working on any LIBOR projects, or within financial services what is driving ediscovery? Thanks.

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Mark Hussey - *Huron Consulting Group - CFO*

With respect to margins I am going to take this from the standpoint of pricing and the healthcare environment as Jim mentioned, we haven't really seen a change in the market, that has been true really from our expectations from a profitability standpoint, as we look at the opportunities, in other words we have not really changed our margin expectation over time and that incorporates the assumed staffing levels to achieve the numbers. So over time we believe that we have stable margins within that side of practice, and really on the higher ed side, that particular practice as well is fairly stable and can have a different mix depending on what is going on at any given time, but we believe that if you look historically, our expectation would be that margin performance is going to be generally in line. Jim if you have anything to add?

Jim Roth - *Huron Consulting Group - CEO, President*

That is exactly right I would agree with that. Maybe I will answer that piece about ediscovery Paul. Our preference is typically not to talk about, we certainly don't talk about clients unless they have already been made public, and I think that sometimes it gets a little bit misleading, if we talk about particular events because we could say that we are doing LIBOR matter with one of the banks, and what you don't really get out of that is how big it is.

I think our preference is to say, you are this group, this is the last group I need to tell about all of the complexities that are challenging financial service industries right now. I think we have a pretty good array of clients across the various issues that are affecting them right now. I would rather leave it at that. It is probably our largest industry that we are serving right now. We do a lot in energy we do a lot in pharmaceutical as well, we are doing a lot in telecom and tech. So all the current stuff for the most part, we are doing some of it. I think I would rather leave it at that.

Paul Ginocchio - *Deutsche Bank - Analyst*

Understood. Is it still your outlook that performance fees grow in line with HEC revenue, or have you toned that down a little bit?

Mark Hussey - *Huron Consulting Group - CFO*

No. You know what Paul, back to what Jim said originally about the mix of engagements going on at any point in time, so we have seen an increase in several clients that have taken us a little bit towards the higher end of the range. If you look historically we are really not outside of the range of what we have seen. If you look at how much revenue is going to come from performance based fees versus fixed fees. So that has a barrier in terms of what the future effect on revenue will be. To the extent that we have new engagements that are going to be a little bit higher in that mix, that may end up depending on what period of time you are looking, push it into a future period of time. Over time if you looked at it, it would be higher just because of the mix, but in any given quarter based on the recognition it can vary a little bit.

Paul Ginocchio - *Deutsche Bank - Analyst*

Thank you.

Operator

Our next question comes from the line of Tobey Summer with SunTrust. Please proceed.

Frank Atkins - *SunTrust Robinson Humphrey - Analyst*

This is Frank in for Tobey. I wanted to ask about the Life Sciences business, how has demand and pricing been on the pharma medical device side.

Jim Roth - *Huron Consulting Group - CEO, President*

Frank, Life Sciences has actually been doing very well. It continues to grow, it has had a nice growth rate for us. I think they are broadening the level of services they are providing, and we are pretty pleased with the growth rate in that group as well. It is indicative really of collectively across the board, all of the various practice within higher education and life sciences business have been doing very well. And as we indicated, we had a record quarter in the second quarter for that group, so life science was certainly a part of that.

Frank Atkins - *SunTrust Robinson Humphrey - Analyst*

If I could dig into legal a little bit more pricing environment there, and any areas of either strength or weakness by either practice or geography?

Jim Roth - *Huron Consulting Group - CEO, President*

I don't know that we are seeing, there has always been this discussion of pricing pressures, and certainly it is not a case of where it is still a very competitive market make no question about it. I think for us right now even though pricing is always going to be an issue, I think what is really driving the collective business and the segment, is the fact that the needs across the board are pretty acute, so even if there is some pricing pressure, I think some of the improved margins that we have seen are really the result of the fact that we are getting high volume in the various services that contribute to that volume, we are learning to manage the business a little bit better. I think we have been making progress over the last several quarters, and we hope to continue to do that.

Frank Atkins - *SunTrust Robinson Humphrey - Analyst*

Great. What was consulting turnover in the quarter?

Mark Hussey - *Huron Consulting Group - CFO*

On a year-to-date basis it is running, I am not going to talk to the quarter, but on an annualized basis it is running probably about 15% to 16%.

Frank Atkins - *SunTrust Robinson Humphrey - Analyst*

Okay. Great. You talked about a sequential pickup in the financial segment in the second half of the year, what maybe if you could talk about some things that would drive that, or what gives you some comfort that things could kind of turn up there?

Jim Roth - *Huron Consulting Group - CEO, President*

It obviously has been a challenging at least last couple of quarters and we had hoped to see more improvement in the second quarter, and we didn't it went the other direction. There are a couple of things that give us some comfort the most important one would be that we have got some pretty good people in the practice, and they are in the market quite a bit, and I think we need to just have a few things fall our way. Either through a transaction, we are broadening some of the services there. Again I think we have got some really competent people that are in the market, we are not losing tons of work, I think we just have to have more times at bat. I think that will come in the third quarter so that is what we are pushing for right now. We have broadened the services that we provide, and we are just extremely, extremely focused on trying to generate revenue by getting out and talking to people. And I think hopefully events will fall our way in the third quarter and beyond.

Frank Atkins - *SunTrust Robinson Humphrey - Analyst*

Great, thank you very much.

Operator

Our next question comes from the line of Joseph Foresi, Janney Montgomery Scott. Please proceed.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

My first question here is just, as we think and talk a lot about the success fees, has the visibility on the timing of these fees improved at all as we have gone through the year? Is there any color or metrics you can give us around backlog or give us a little more comfort numerically about the direction of the business?

Mark Hussey - *Huron Consulting Group - CFO*

I would say the fundamental visibility is better only because we have a shorter runway ahead of us. So as you have more visibility shorter in, we get a little bit more comfortable in terms of our numbers, and that is one of the reasons why we just narrowed our range, because we do have more comfort.

With respect to quantifying the numbers we have looked at this and actually have contemplated whether or not to publish a number, but as we report our numbers we have a higher in health and education segment so really the fundamental pipelines are very different for education versus how it works within healthcare. What I can tell you is that we have certainly seen improvement in the pipeline and we feel that based on the level, those hard backlog as well as the assessment activity within that, that we are at a level that gives us confidence behind our statement that we have very solid prospects looking ahead.

Jim Roth - *Huron Consulting Group - CEO, President*

I would agree with that, I think we do, as Mark indicated we have thought about whether there are other things we can give more color, and we would like to if we could, but it just gets to be a little bit more complicated because of the varied patterns between higher ed, and then life sciences and healthcare.

The backlog has been growing. Assessments are very strong right now. All of the things that we look at internally to figure out how things are going are just fine. To a large extent we already have much of the activity that we are doing today particularly on assessments are all really going to generate 2013 revenue. If we are doing an assessment today, it is likely going to be impacting 2013 and so our job is certainly to close out the year as strong as we can. Our job is also that we hit the road running on January 1st 2013, because we know that growth expectation is there as well. I think collectively when we look at all of the different factors that we talked about, the kinds of work that we are getting, the kinds of opportunities that are being serviced to us. The growth of the backlog, the number of assessments, all of those factors give us comfort that we are going in the right direction.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

Okay. Maybe instead of quantitative. I know that you have given some qualitative numbers. How does the backlog and assessments look compared to historical levels, are they at all-time highs, are they trending upwards, maybe you could just provide color in that format?

Jim Roth - *Huron Consulting Group - CEO, President*

The backlog, Mark will talk about the backlog and assessments in a second, but the assessments as we have kind of said in the past, it is a little bit hard to judge because I can tell you that we have got the highest level of assessments, but they could be relatively small opportunities, or I could say that they are lower than in the past, but they could be higher. Unfortunately the number of assessments doesn't say much. We are doing a very healthy number of assessments right now, that give us comfort that we are in the right spot and that they are likely to generate very decent future revenue. In terms of the backlog.

Mark Hussey - *Huron Consulting Group - CFO*

In terms of the backlog, there is also complexity looking at it, so if we sell a multi-year engagement with one large client and over time that is going to inflate a prior period comparison to look at. So you really have to break it down you can't generalize without really having an understanding. What I can tell you is that from a quantitative and qualitative perspective as Jim indicated it has been growing and it is a robust profile right now, relative to remaining fees and contracts that we have actually signed, and have expectations in place. With respect to both fixed fee and contingent. Jim.

Jim Roth - *Huron Consulting Group - CEO, President*

Yes, and the other thing I think I would talk about a little bit. We certainly are pleased with the continued growth of our performance improvement type of work and our revenue cycle work that we have historically done.

We have mentioned before and I want to mention right now, because it is really an important part of where we expect the future growth to be, and our clinical solutions is really the kind of work we are being asked to do and the kinds of opportunities that are being presented to us are exactly reflective of the kind of work that we think is going to be of very high demand in the future. There remains a tremendous amount of change as we have said before in the fundamental business models of these hospitals, and we are positioning ourselves in the clinical solutions area to be very well positioned to help our clients deal with that, and I wish you could the kind of work that we are being asked to look at or do right now, it is very exciting and it is exactly the kind of work I know will be the foundation for us for solid growth for the future, over and above the core bread and butter things that we have historically done so well in this practice.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

On the topic of the assessments of backlog being I guess characterized as healthy. Maybe you could remind us what you think the long term growth rate of the health and education practice is, and based on what you are seeing this year and the fact that it is back end loaded, would you expect an acceleration in that growth rate heading into 2013, or at the end of 2013 just based on what you guys are seeing in the pipeline?

Mark Hussey - *Huron Consulting Group - CFO*

This is Mark. I think fundamentally we have always talked about the long term, by long term I am saying the next five years. We think healthcare if you look at the broader economics and the percentage of GDP that is going to continue to be actually getting a higher percentage, there is going to be continued spending and demand in this marketplace, and as you can see from our hiring over time we continue to hire north of 10% and over time as clinical develops into a larger solution we are going to have plenty of opportunities we think to be at a minimum of 10% growth within the health and education segment. Frankly, all of my statements about healthcare hold equally true on the education side of the house as well.

Jim Roth - *Huron Consulting Group - CEO, President*

I would agree with that. I mean we will see as we put together our plans for future years, I would be disappointed if we dropped below 10%, I think that there is just so much activity that is taking place, and we happen to be very well positioned to do that. I would consider 10% to be a very attainable growth rate. And I would certainly do everything that we can to try to get above that.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

Last one from me. Any way to quantify the impact on margins from the success fees? In other words does $1 million in success fees equal 1 basis points on margins I imagine most of it is going to start to trickle down to EPS coming into guidance and implies that, is there any metric that you can give us on that front? Thanks.

Mark Hussey - *Huron Consulting Group - CFO*

The success fees largely drop to the bottom line because there is such a discrepancy in terms of the current efforts versus when the revenue recognition happens. So if you think about fees that we recognize in the current quarter, these efforts happened last year, or perhaps in Q1 but to a very large degree, the efforts would not have come in the current period. It generally has been true that these fees just generally drop to bottom line in the period that they are recognized. Not to say that you don't have other things going on at the base, where you have hours being spent that may not have these recognized. But if you look specifically at the ones that are recognized against the efforts in the current period, they have largely dropped to the bottom line.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

Okay. Thank you.

Operator

(Operator Instructions). Our next question comes from the line of Brendan Matthews with Northland Securities. Please proceed.

Brendan Matthews - *Northland Securities - Analyst*

I am just filling in for Bill today. A couple of quick questions for you guys. Do you have any especially large engagements that you are expecting to end during the third quarter?

Mark Hussey - *Huron Consulting Group - CFO*

I am sorry I think you cut out right when you asked the question. Could you repeat that please?

Brendan Matthews - *Northland Securities - Analyst*

Yes. I am sorry about that, do you have any especially large engagements you are expecting to end during the third quarter?

Mark Hussey - *Huron Consulting Group - CFO*

To end?

Jim Roth - *Huron Consulting Group - CEO, President*

To end, right. Not that I am aware of. Just trying to think off of the top of my head. Not really. I'm thinking off the top of my head I don't think anything in the health and education segment that I am aware of. We have got some that will be rolling off, nothing that is going to be so big. In the Legal Consulting business you always have an option, something could end very quickly, but you also have the same possibility that one could startup very quickly. There is nothing that we are doing today of very sizable magnitude that I think will have different patterns in the third quarter.

Brendan Matthews - *Northland Securities - Analyst*

Okay. Last question from me, I know that you touched on this earlier, but should we be still looking for flat to 5% revenue growth in the financial consulting segment for the full year 2012?

Mark Hussey - *Huron Consulting Group - CFO*

No. At this point just based on where we see the run rate right now, we are not expecting it to be flat to up 5%. It will likely have some decline, although the run rate in the second half of the year we are looking to improve substantially based on some of the initiatives and activities that we have going on.

Brendan Matthews - *Northland Securities - Analyst*

Okay. Thank you very much.

Operator

Our next question comes from the line of Dan Mazur with Harvest Capital. Please proceed.

Dan Mazur - *Harvest Capital - Analyst*

Good afternoon guys. Thanks for taking my question, just have a quick one on adjusted EBITDA to follow-up on Joe's question. You have had in the past some individual quarters where you have had some large outsized performance fees, and it has driven margins higher in the quarter kind of more in that 20% to 21% adjusted EBITDA margin range, and I think your guidance in the second half implies a lot higher margin range, just what is different in the second half than just maybe some of those individual quarters where you did high-20s or mid-30s performance fees?

Mark Hussey - *Huron Consulting Group - CFO*

Hi Dan it is Mark. It really is driven largely by the success fees in the second half, and really the underlying business otherwise you have headcount, headcount growth, so really on a second half basis compared to the first half, assuming that our guidance in the second half is a substantial increase, that we have a disproportionate profitability and bring the adjusted EBITDA margin really out of line on a long term basis. Plus at the same time you get the advantage of having the bonus being at a fixed level against higher revenue.

Dan Mazur - *Harvest Capital - Analyst*

So it is last year on just doing the last three quarters at substantial levels you just had the comps spread out more, it still just looks like it is a really big jump on what is flowing through in the second half, and it just comes down to how comps come through?

Mark Hussey - *Huron Consulting Group - CFO*

Yes I think that is exactly how it is.

Dan Mazur - *Harvest Capital - Analyst*

Okay. Acquisitions remain the top priority for capital at this point as you digest in the second half. If you could just talk about the capital allocations?

Mark Hussey - *Huron Consulting Group - CFO*

Sure. Jim, with respect to acquisitions maybe you want to talk about our positive outlook.

Jim Roth - *Huron Consulting Group - CEO, President*

I think in all of our practices we have got, as we have always done, we have always looked at a variety of things, and so I do think that I would expect there to be some potential acquisitions over the next period of time. We are certainly looking at each of our segments, probably more so in our two largest segments.

Mark Hussey - *Huron Consulting Group - CFO*

Really from a return perspective, we think in the interest of shareholders if we can go out in the marketplace and find investments that are going to generate those attractive returns on a risk adjusted basis. It is our highest and best use of capital, so that is going to continue to be prioritized.

Operator

Our next question is a follow-up with Tim McHugh with William Blair. Please proceed.

Tim McHugh - *William Blair & Co. - Analyst*

Just one more to sneak in there. Can you talk about the headcount growth plans for the health and education business and probably I guess, I know you didn't want to give a backlog number , but can we take that as a rough proxy for the pace of the backlog growth that you are seeing? I am assuming you are hiring commensurate with the pace of that growth rate and the demand that you seeing?

Jim Roth - *Huron Consulting Group - CEO, President*

I think that, Tim, is probably a pretty good surrogate. The one thing as we have mentioned before in the higher ed part of healthcare we still have a little bit of an anomaly where we are kind of hiring into people that have historically have been contractors, and we are hiring people in there now, so that puts the growth rate and FTEs slightly higher than the growth rate, but I think that is a reasonable surrogate.

Jim Rojas - *Huron Consulting Group - COO*

And then it is really both across the health and the education side of the practice, we have seen really strong headcount growth and hiring needs on both sides, and that is probably not surprising consistent with the comments that we made earlier about not only demand on the healthcare backlog, but also just back to the demand on the education side of the business.

Tim McHugh - *William Blair & Co. - Analyst*

Is there any plan to slow that down what is the expectation for the second half of the year?

Jim Rojas - *Huron Consulting Group - COO*

We will slow it down a little bit. We will probably slow it down a little bit. Fortunately because our attrition rate is less than we anticipated, so we have got a little bit more flexibility in terms of how we recruit and staff in the engagements. The other thing is in some of our service lines really across Legal Consulting and the health and education segment, we have got some new services as well that we are beginning to ramp up, and sometimes those services require different skills that we actually don't have right now, so that too accounts for some of the hiring that we are doing right now in anticipation of further growth in those businesses.

Jim Roth - *Huron Consulting Group - CEO, President*

In general I think Tim to answer your question, it is decent surrogate although it will slow down a little bit.

Mark Hussey - *Huron Consulting Group - CFO*

And Tim, just one last color comment, it is just really sometimes it is tied to the campus recruiting that we do for analysts will effect a little bit of the timing of when they come in, when they are available, so we tend to see a little bit more hiring between May and September, and then towards the other quarters it just naturally starts to go down anyway.

Tim McHugh - *William Blair & Co. - Analyst*

Okay. Great thanks.

Operator

Ladies and gentlemen since there are no further questions in queue, I would now like to turn the call over to Mr. Roth for closing remarks.

Jim Roth - *Huron Consulting Group - CEO, President*

I want to thank everybody for spending time with us this afternoon on the call. I look forward to speaking to you again in October when we announce our third quarter results. Have a good evening.

Operator

Ladies and gentlemen that concludes today's conference. Thank you for your participation. You may now disconnect. Have a wonderful day.
