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HURN - Q3 2014 Huron Consulting Group Inc Earnings 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 third quarter 2014.

(Operator Instructions)

As a reminder of 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 on Huron's website for all of the disclosures required by the SEC, including reconciliation to the most comparable GAAP numbers. And now I would like to turn the call over to Jim Roth, Chief Executive Officer and President of Huron Consulting Group. Mr. Roth, please go ahead sir.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Thank you. Good afternoon and welcome to Huron Consulting Group's third-quarter 2014 earnings call. With me today is Mark Hussey, our Chief Operating Officer and Chief Financial Officer.

I'm pleased to report strong third-quarter results for Huron Consulting Group. As discussed in previous calls, given some of the sizable performance-based fees we received in the first two quarters, we fully expected that the second half of the year would yield a growth rate lower than the 25.5% revenue growth we saw in the first half. Our results for the third quarter were consistent with our expectations, and have put us in a position where we are able to raise the midpoint of our revenue guidance for the year.

Before I turn to a discussion of the market demands for our services, I want to highlight some of the key attributes of our performance through the third quarter. First, our Company-wide organic revenue growth rate for the first nine months of 2014 was 12.6%, exceeding our initial expectations set forth earlier in the year. In 2015 we expect that our organic revenue growth rate will continue at our previously communicated mid- to upper-single digit range. Demand for our services remains strong and we are excited about our ongoing efforts to expand the portfolio of services we offer within our existing segments and the geographic reach of each of our practices.

Second, as Mark will discuss in a few minutes, our revised revenue and earnings guidance for the remainder of the year puts us net of acquisitions ahead of our initial 2014 guidance targets. Over the course of the year we have raised the low end of our revenue guidance by $30 million exclusive of Vonlay, reflecting our strong market presence and our ability to help clients navigate some complex strategic and operational environments. Our bonus accruals in the third quarter are consistent with the increased midpoint of our guidance range and expectations for continued strong performance in the fourth quarter.

Finally, and perhaps more importantly, we are well-positioned in each of our practice areas to achieve solid growth in 2015. We are in the process of planning for next year, and while I'm excited about the prospects for our future, I'm even more excited about the fundamental market conditions that are driving each of our businesses.

It's no secret that the drivers of demand in our core businesses are expanding and we are fortunate that our people have put us in a position where we have a strong reputation in markets that remain vibrant and responsive to our capabilities. There were several factors that had a slightly negative impact on our performance in the third quarter.

Most notably, our healthcare and enterprise performance management practices each held practice-wide meetings during the third quarter. While these events were contemplated in our forecast and guidance, they tend to have a several hundred basis point impact on utilization in the quarter. In addition, we remained busy on the M&A front, incurring some deal-related expenses as we continue to see numerous opportunities for acquisitions that will help drive future growth in excess of our organic targets.

Let me now provide some commentary on each segment before turning the discussion over to Mark. Huron Healthcare turned in another solid quarter, with strong revenue growth resulting from ongoing changes in the healthcare provider market. As I have mentioned in recent quarters, the quarterly revenues in this segment are impacted by the timing and nature of some of the larger engagements we have underway.

In recent years we have seen strong second-half performance. Consistent with my comments made on the last earnings call due to the timing of projects that we have underway, we anticipated our highest run rate and performance-based fees would fall into the first half of the year, in contrast to what we've seen in recent past where the third and fourth quarters had the highest revenue.

This year we have seen a shift to strong first-half performance due to the timing of the start and completion of engagements that commenced in late 2012 and early 2013. These timing characteristics are more reflective of the date of initiation for our larger projects than they are reflective of any seasonal patterns. We manage our Healthcare business based on annual forecasts, and we believe that our year-end results in this practice will again exceed our expectations.

I'm not going to repeat commentary that we have provided in prior quarters regarding the strength and direction of demand in the healthcare space. Suffice it to say that the cost and quality pressures remain significant for our hospital clients. The transition toward population health is evolving slowly but it is evolving.

In this interim period, which we expect to play out over the next five to seven years, hospitals will be in the challenging position of having to manage two very distinct business models simultaneously, creating new opportunities for Huron to help them with his transition. Furthermore, the ongoing trend of consolidation in the industry has opened new areas of focus for Huron, helping hospital clients address the operational and clinical efficiencies that need to arise in order to achieve the goals of consolidation.

We have recently won several sizable and competitive projects where the client's goal is to implement meaningful clinical integration and cost efficiency across a recently consolidated group of hospitals. These are complex projects that were often long in duration and we expect engagements of this nature to arise more frequently in the coming years. Finally, our recent acquisition of Vonlay, which provides healthcare IT consulting, has provided us with new competencies in areas that are strategic to our growth, and we are excited about our ability to increase the array of healthcare IT offerings available to our hospital clients.

Turning now to our Huron Legal segment, the third quarter resulted in solid performance year over year, but the third quarter was softer than the second quarter of 2014. The decline in revenue from Q2 to Q3 was driven by an anticipated partial wind down of a large engagement within the financial services industry, and the absence of a large second-request engagement. Our strategy of focusing on the office of the general counsel among large multinational corporations remains at the forefront of our efforts, and we believe that the strategy will enable us to achieve solid growth in the future as the amount and complexity of data continues to grow.

Consistent with comments that we've made on prior calls, the criticality of having highly secure technical platforms from which to manage the data that we receive has enabled Huron to continue to distance itself from some competitors that have struggled to achieve the security infrastructure required by our large clients.

The Education and Life Sciences segment, also known as ELS, grew 5% in the third quarter of 2014 over the same period last year. While revenue declined about 5% on an organic basis, the percentage decrease was reduced to about half the level experienced during the first half of the year as performance has begun to solidify.

The technology practice within ELS continues to produce solid results. Our technology solutions to the higher education market continue to expand and we have recently begun to enhance our historical focus of providing enterprise system solutions in the higher education markets to the hospital market.

With a few key wins during the recent quarter and a solid pipeline, we expect this practice will continue to perform well throughout the rest of the year and into 2015. In our Life Sciences practice, we've seen an increase in demand for both our compliance-focused services as well as a strategy services, which we acquired in January through the Frankel Group acquisition.

The Life Sciences group has seen an uptick in utilization and recently won several sizable projects which we believe will pave the way for improved utilization and margins in the fourth quarter. The integration of the Frankel Group continues to go well, as that team has strong market relevancy in areas that are core to the growth of this business.

The strategy and operations practice within the ELS segment showed improvement during the quarter. The practice closed on more wins during the third quarter than in recent quarters, which drove an increase in utilization. We also saw an increase in our pipeline activity during the third quarter, which confirms our expectation that the market will continue to be more active in the last quarter of the year.

As I have mentioned on prior calls, the higher education market is going through a dramatic change that I believe is even more significant than the healthcare market. And we believe that we will remain the primary source of value-added consulting to our college and university clients as this industry continues to evolve.

Finally, our business advisory segment had a strong quarter with solid contributions from our legacy business advisory practice and the enterprise performance management, or EPM practice. Our legacy business advisory practice had another good quarter; compared to Q3 of last year on an organic basis, this business grew 30%, helped by the addition of Huron transaction advisory, our limited purpose broker dealer.

We're seeing an increased interest in our new offerings associated with broker-dealer license, and we are encouraged by the success we've had to date that the broker dealer will continue to be a platform for growth. The legacy business advisory practice has continued to play a preeminent advisory role among many middle-market clients, and we are pleased with the ongoing participation of our people in this part of the market.

The third quarter culminated with the one-year anniversary of the Blue Stone acquisition, the foundation of our EPM practice. Over the past year our EPM practice has seen consistent revenue, EBITDA, and headcount growth. They have also built new service lines, organically and inorganically, and a news sales organization that we expect will continue to position the practice for solid growth in the future.

Over the first year since we acquired the business the practice has grown nearly 30% compared to the 12 month period prior to the acquisition. We're excited to have recently announced our acquisition of Threshold Consulting. Threshold has enabled us to strengthen our data warehousing and business intelligence capabilities while also introducing us to the salesforce.com market. We are pleased with the talent that came to Huron from Threshold, and we believe that the analytic skills provided by Threshold will help us to better assist our clients to use data as a strategic asset to improve business performance.

Turning to our view of Huron for the rest of the year, we are increasing the low end of our revenue guidance by $10 million. We now expect annual revenues to be in the $815 million to $825 million range for 2014. We've also increased our adjusted EPS guidance, which Mark will provide more detail on shortly. We are maintaining our annual performance-based revenue guidance in the Healthcare segment at $85 million to $95 million.

The midpoint of our newly revised guidance implies a strong end to the year, which is consistent with the level of market activity across all of our practices. Each day and every week I am reminded of how fortunate we are to have assembled such a talented group of people focused on markets that are essential in today's economy. We are excited about our future prospects and we're looking forward to a strong finish to 2014 and a solid start for the new year.

Now let me turn it over to Mark for a more detailed discussion of our third-quarter results. Mark?

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Think you Jim and good afternoon everyone. Before I begin please note that I will 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, along with the discussion of why Management uses these non-GAAP measures.

Also we recently announced our acquisition of Threshold Consulting which will deepen our capabilities in data warehousing and business intelligence solutions. The transaction closed effective October 1, so our Q3 financial results do not include Threshold. Their results, which are not material, will be included within our Huron business advisory segment beginning in the fourth quarter.

Now I will walk through some of the key financial results for the quarter. Revenues for the third quarter of 2014 were $198 million, up over 13% from $174.7 million in the same quarter of 2013. Revenues for the third quarter of 2014 reflect our acquisitions of Blue Stone, the Frankel Group, and Vonlay, which in the aggregate generated $18.8 million of revenues. On an organic basis revenue was up 2.5% in the quarter, while acquisitions added 10.8% to total revenue for Q3.

Operating income decreased $9.8 million or 31.6% to $21.3 million in Q3 2014, from $31.1 million in Q3 of 2013. Operating margin was 10.7% in Q3 2014, compared to 17.8% in Q3 of 2013. The decrease in operating margin in Q3 of 2014 was primarily attributable to an increase in salaries, bonus, and related expenses as a percentage of revenues. Also we recognized a $5.3 million litigation settlement gain in Q3 of 2013 which favorably impacted the margin in the year-ago period. Bonus expense accounted for approximately $6 million of the decrease in operating income compared to the prior year.

Adjusted EBITDA was $28.9 million in Q3 2014 or 14.6% of revenues, compared to $31.5 million in Q3 of 2013 or 18% of revenues. The decrease was due primarily to an increase in salaries and related expenses as a percentage of revenues, as well as higher bonus accruals. As many of you know, in the interim quarters we report bonus expense corresponding to the midpoint of our annual guidance range.

Net income for continuing operations was $12.2 million or $0.54 per diluted share in the third quarter of 2014, compared to $17.2 million or $0.75 per diluted share in the same quarter last year. Adjusted non-GAAP net income from continuing operations was $14.2 million or $0.62 per diluted share in the third quarter of 2014, compared to $14.8 million or $0.65 per diluted share in the same period of 2013.

Our effective income tax rate in the third quarter of 2014 was 36.8%, compared to 42.2% a year ago. The effective tax rate for Q3 of this year was lower than the statutory rate inclusive of state income taxes, due primarily to the favorable settlement of IRS audits for years 2009, 2010, and 2011.

The effective tax rate for Q3 last year was higher than the statutory rate inclusive of state income taxes, due primarily to the impact of foreign losses with no tax benefit and certain non-deductible business expenses. On a full-year basis, we anticipate our 2014 effective tax rate to be approximately 31%, inclusive of the one-time tax benefit resulting from the check-the-box election. On a normalized basis, that is excluding the non-recurring tax benefit, we expect our effective tax rate to be approximately 40.5%.

Now let's look at how each of our operating segments performed during the quarter. The Huron Healthcare segment posted revenues of $97.8 million for the third quarter of 2014, up $10.9 million or 12.5% over the third quarter of 2013. Revenues for the third quarter of 2014 included $7.6 million from our recent acquisition of Vonlay. Excluding Vonlay, organic revenue increased 3.8% in the quarter.

Performance-based fees in Q3 of 2014 were $19 million, compared to $22.5 million in the same quarter last year. Excluding performance-based fees for both years, organic revenue increased over 10%. While Huron Healthcare had a strong first half of 2014, as we had mentioned during our last call, we expected some moderation in the third quarter of 2014 and expect this to continue into the fourth quarter. Utilization trended downward in Q3 compared to Q1 and Q2, due to the timing and nature of the projects we have underway along with the impact of the annual practice meeting.

Also as we've said on many occasions, the timing of performance-based fees can vary significantly. They are not driven by a seasonable pattern, but rather the mix of engagements at any point in time.

The operating income margin for Huron Healthcare was 28.3% for Q3 2014, compared to 35.4% for the same quarter in 2013. The decrease in margin was due primarily to higher salaries, bonus, and related expenses as a percentage of revenues, and an increase in intangible assets and amortization resulting from our acquisition of Vonlay. Sequentially, the decline in margin was primarily driven by the increased bonus accrual, along with the planned cost of the annual practice meeting and lower utilization. Utilization has picked up in Q4, and we expect to be back in the upper 70% range for the quarter.

Our Huron Legal segment posted revenues of $46.1 million in Q3 of 2014, compared to $45.3 million in Q3 2013. The increase in revenue was attributable to slightly higher utilization in both our discovery centers and in our consulting practice.

The operating income margin for our Huron Legal segment was 23.7% in the third quarter of 2014, compared to 33.4% in the same quarter of 2013. The decrease in this segment's margin was primarily due to higher contractor expenses related to an increased portion of work coming from review as a percentage of revenues. In addition, bonus expense was higher than the prior year.

The Huron Education and Life Sciences segment posted revenues of $36.5 million for the third quarter of 2014, and includes $3.5 million from the Frankel Group which was acquired at the beginning of 2014. Revenues for the third quarter of 2013 were $34.8 million.

The operating income margin for Huron Education and Life Sciences was 25.9% for Q3 2014, compared to 22.3% for the same quarter in 2013. The increase in margin was primarily due to lower contractor and practice meeting expenses, partially offset by higher bonus expense. Utilization continued in line with the improved level we saw in Q2 and is well ahead of the level in Q3 2013.

The Huron business advisory segment posted revenues of $17.1 million for the third quarter of 2014, and includes $7.7 million from our EPM practice which we acquired in Q4 of last year. Excluding EPM, revenues for the third quarter of 2014 were $9.4 million, compared to $7.2 million for the same period last year. On an organic basis, revenue increased 30%, largely attributable to performance-based fees associated with the limited purpose broker dealer we established in April of this year.

The operating income margins for the Huron business advisory segment was 25.7% for Q3 2014, compared to 9.2% for the same quarter in 2013. The increase in this segment's operating margin is primarily due to the performance-based fee revenue and lower bonus accruals for the legacy business advisory practice. This favorability was partially offset by the combination of our EPM business, which has a lower margin profile, into the Huron business advisory segment. As Jim mentioned, the EPM practice has grown rapidly since the acquisition continues to have significant growth opportunities both organic and inorganic.

Other corporate expenses not allocated at the segment level were $24.3 million in Q3 2014, compared to $18 million in Q3 2013. Corporate expenses in Q3 of the prior year were reduced by a $5.3 million litigation settlement gain.

Now turning to the balance sheet and cash flows. Cash flow from operations for the third quarter was $79.9 million, with DSO coming in at 78 days. Cash flow was particularly strong as we funded $35.6 million of share repurchases, $18.5 million for convertible hedging transactions, $12.5 million for our investment in Shorelight Education, and $5 million for a deferred acquisition payment, all of which in the aggregate totaled over $71 million. Despite this spending, we ended the quarter with our net debt position increasing only $4.5 million over the end of the second quarter.

Let me clarify our net debt calculation since our balance sheet reports the bifurcated values of the $250 million of convertible debt in both debt and equity. As of the end of Q3, Huron's net debt includes the face value of the convertible notes of $250 million plus, our term loan of $150 million, less cash of $226 million for net debt of $174 million. This represents 1.1 times leverage at the midpoint of our guidance range for the adjusted EBITDA for 2014.

We've now completed the $50 million share repurchase program that was authorized in Q1. Over the course of the program we repurchased over 805,000 shares, including 568,000 shares in Q3. The Board also approved a new open market share repurchase program of $50 million as mentioned in today's earnings release. We are very happy with the strength of our cash flows and balance sheet, and believe we are well positioned to pursue investment opportunities that will drive future growth.

Turning to guidance, with only one quarter remaining, we are narrowing our guidance range as follows. For the full year 2014, we now anticipate revenues before reimbursable expenses in a range of $815 million to $825 million; embedded in our guidance range are expected performance-based fees in Healthcare in the range of $85 million to $95 million, adjusted EBITDA in a range of $154 million to $158.5 million, net income in a range of $77 million to $79.5 million, and adjusted non-GAAP net income in a range of $76.8 million to $79.3 million.

GAAP EPS between $3.35 and $3.45 per share. And adjusted non-GAAP EPS also in a range of $3.35 to $3.45 per share. This represents an increase at the high end of the range of $0.05 per share primarily related to the lower share base due to the share repurchase program. And finally, with respect to taxes, you should assume an effective tax rate of approximately 31% for the full year 2014, or approximately 40.5% excluding the one-time tax benefit.

With respect to adjusted EBITDA, adjusted net income, and adjusted EPS, there are several items that you'll need to consider when reconciling these non-GAAP measures to comparable GAAP measures, and the reconciliation schedules that we included in our press release will help walk you through these reconciliations. And now I would like to open up the call to questions. Operator.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions)

Our first question comes from Timothy McHugh with William Blair. Please proceed.

Timothy McHugh - *William Blair & Company - Analyst*

Yes, thanks. I guess just to start on Healthcare. Mark you made a comment about the trends you saw in the quarter continuing into the fourth quarter, but then you also said you expected utilization to trend or has already trended back up into the upper 70%s. Could you clarify that?

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Let me clarify that Tim, yes sure. If you look at the first half of the year on a run rate basis, our growth rate if you looked at as an example the total Healthcare revenue excluding performance-based fees or kind of the run rate revenue it was at 25%-type run rate, and what I'm saying is that that will moderate a little bit. We saw it moderate in Q3, it will probably be a little bit below that in Q4, but certainly still positive in the mid-single digit range or maybe a little bit better. And utilization again will come back as well.

And so total revenue in Q4 in Healthcare is likely to be better than that we have seen in Q3.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

And just be clear Mark, the run rate, the percentage you're talking about, that's exclusive of performance-based fees--

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Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Exactly.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Just to be clear on that.

Timothy McHugh - *William Blair & Company - Analyst*

Okay. And so obviously I think probably I think the number in Q3 was a little less than people thought, and then utilization came down and then you had a competitor here in town had somewhat weak results and kind of talked about seeing some change in even the demand environment for performance-improvement type of opportunities.

Can you talk about what you are seeing? And is there anything that has I guess at a high level you said nothing's changed in terms of your enthusiasm, but I guess just in response to those kind of other data points.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Tim, this is Jim. We're seeing no change at all in terms of the demand for the Healthcare services that we are providing. Particularly the performance improvement for us continues to be very strong. We knew and we signaled that we would have just because of the nature of our projects, as you know we probably have 30 or 40 at a given time. We probably knew in December of last year 2013, that we knew that the second half was going to be less than the first. And it was really because it just as we said it was just the adjustment of timing.

There are several factors, none of which are at all long term, that caused the utilization to go down a little bit in the third quarter. As we indicated, one of them was the performance-wide or the practice-wide meeting that had some impact. We also just had a transition, we had some very large practices that were beginning to transition out. We have a large number of assessments that are going on right now, which we know are going to bode well for future performance.

And so there's really nothing at all in our look at the market that tells us there's any weakness coming up. In fact, one of the things I mentioned in my script, Tim, was that one of the things that's actually enhancing and we've typically been going along on the performance improvement revenue cycle clinical services route and that will continue. Those are all performing well and we expect them to perform well for the future.

What we are beginning to see now as we've had a couple of -- recently we've had a couple of very large competitive projects that we've won and they have to do with this consolidation in certain markets. So when hospitals go through consolidation, they are trying to address the cost and quality pressures that they are seeing within their geographic region.

To get a hospital system to be operating efficiently, to basically be using the collective capacity within the system to address the outcomes, to address the cost and quality issues, is a huge undertaking. These are going to be projects that I think are going to be larger than the ones that we've seen historically. Historically, we've said that many of our projects will tend to go 9 to 18 months, or 12 to 18 months.

I think some of these are likely to go 18 to 30 months. And there will be fewer of them but when they come, they are very complex. They require full integration of our collective healthcare services, including performance improvement, and I think that they are going to be an important part of our growth for the future.

So the long way of saying we really not seeing any weakness at all in the markets, and we anticipate the kinds of growth rates that we've been anticipating and talking about for a long time.

Timothy McHugh - *William Blair & Company - Analyst*

And then you commented on I guess two things impacting the margin this quarter. One was bonuses and the other deal expenses. On the bonuses, the $6 million I think you said versus the year-ago period. I guess what is the comparison for that? I guess I would assume just given the growth of the business that you might -- bonuses would be higher this year than last year.

And I guess can you help us I guess understand relative -- or how to put that number in perspective. Then also I thought your historical practice is usually when you increased guidance is when the bonus accruals changed, and I would have thought that would have been last quarter.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Yes, Tim, let me take those. So first of all really when you compare say Healthcare year on year, there are two main factors that are really driving the reduction in margin. Probably the bigger impact is just the fact that there were $3.5 million less in contingent fees versus last year. And then in addition, we had a higher -- within Healthcare we had a higher bonus accruals than we did as of last year, so that's just wherever we were in the business, as reported, those are the numbers.

And just to clarify how we do account for it then sequentially, it is also when we adjust our guidance ranges, it's done at the practice level. So each individual business we look at in terms of what the expectations are. So consistent with our expectation that full year is going to likely exceed our expectations, as we adjusted our guidance range this year, you saw a pickup in the bonus accrual in Q3. You also saw one a little bit in Q2 as well.

Timothy McHugh - *William Blair & Company - Analyst*

Okay. Can you quantify the deal-related cost that you might have seen in the quarter?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

The deal-related really go back to the corporate SG&A. And so it was perhaps a lesser impact overall. And so those again -- those having stayed at the corporate SG&A, you could take that out year on year, we're up maybe 4%. So there is various puts and takes associated with that. So that one is a little bit less impactful in the quarter, but sequentially we had a little bit more in Q3 than we did in Q2.

Timothy McHugh - *William Blair & Company - Analyst*

Okay, thank you.

Operator

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

Paul Ginocchio - *Deutsche Bank - Analyst*

Thanks. I just have two questions. First, as we look into -- maybe it's too early to look into 2015, but just wanted to clarify and make sure the performance fees as you look into next year probably be within the normal range of performance fees. Is there any reason or any way it would be higher or lower? Or is it too early to tell? If you could give us any color, that would be great.

Then second, with the additional $50 million buyback, should we read anything into that? Or are you still looking to spend most of the convert on acquisitions? Thanks.

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Jim, you want to take the first one and I'll take the second?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Yes, in terms of the performance fess for 2015, it is too early to tell. We're certainly tracking those right now. We're beginning to map them out. But as you heard us say 1,000 times, it's really hard to tell where they are going to fall. So we will obviously know a lot more when we release fourth quarter, but at this point, it's too early to tell.

And I don't think we're going to see anything unusual next year, but again, there could be things that end up in Q4 of 2015, there could be some things that push over into first quarter of 2016. At this point, it's just too early to tell.

Paul Ginocchio - *Deutsche Bank - Analyst*

Jim, there's nothing that's telling you or there's no reason to assume it's going to be below the normal range that you've seen in the past, right?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

No. I don't think it will be below the normal range.

Paul Ginocchio - *Deutsche Bank - Analyst*

Thank you.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Let me clarify that. I don't know what the normal range is. I don't think it will be below it this year, I guess would be another way of saying that. The normal range as you know has swung wildly, but I think we will see -- I don't expect it to be lower than this year, where we stand right now.

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

I agree, I don't think there's anything structural that would suggest that, so it really comes down to how the year shapes up from a timing perspective.

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Jim Roth - *Huron Consulting Group Inc - CEO and President*

And I think Paul, I think obviously what others are trying to get at is we are just not seeing any type of weakness in the market for our Healthcare services. And I realize that others may have been talking about that within some of our competitors. It's just something we are not seeing.

We run this entire business on an annual basis, and we had predicted a slightly weaker second half is coming just as we are, but in fact, our results for the fourth quarter -- for the year are likely to exceed our original estimates in Healthcare anyway. So we're just not seeing any type of secular weakness within the Healthcare segment at all.

Paul Ginocchio - *Deutsche Bank - Analyst*

Perfect.

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

And Paul to your question on the buyback and reading into it. I would not read into it that our priorities have changed. Our number-one priority continues to be deploying capital in acquisitions, and so the share buyback let me just comment on that briefly.

So the $50 million we did, half of that came through the convert transaction, and the other half is really open market share repurchases. And our view of share repurchase in general is one that basically tries to offset dilution from equity programs, but really not trying to manage to an EPS. I would just say it's very opportunistic to have it out there and approved should we had those right conditions, but the primary goal is to deploy capital into acquisitions.

Paul Ginocchio - *Deutsche Bank - Analyst*

Thank you.

Operator

Our next question comes from the line of Jerry Herman with Stifel Nicolas. Please proceed.

Jerry Herman - *Stifel Nicolaus - Analyst*

Hi guys. Good afternoon everybody. Just wanted to ask a couple of high level questions if I could. In particular if you look at the third quarter P&L and look at the direct cost relative to the revenue increase, it just doesn't look like there's any leverage at all. I mean there is a pass through essentially on all the revenue increase and its direct cost. And a realize I can think of some of the key components of that, but help us think through that including the performance fees and the bonus comp, but help us reconcile that lack of leverage.

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

I guess if you are looking Jerry at the total Company level, the easiest answer is that the utilization was lower and that just means those headcounts did not generate as much top-line revenue. And so that's first and foremost the biggest impact from, if you're looking at that. And then also perhaps to a little bit lesser extent, the Legal segment basically had more contractor fees associated with it.

But overall there's really nothing that's changed in terms of leverage of the business other than timing around the utilization. Our view of leverage models remains exactly what it's been in the past.

Jerry Herman - *Stifel Nicolaus - Analyst*

And nothing -- no other timing issues other than the obvious one you just referenced, but any other timing issues on cost and currents in the third quarter?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

No.

Jerry Herman - *Stifel Nicolaus - Analyst*

Okay. And then with regard to your fourth-quarter guidance, the midpoint actually implies a down revenue quarter, by my calculation only gets to $202 million versus $211 million. I realize you did $45 million in performance fees last year. In light of a rather large increase in headcount at the end of the quarter, help us think about that expected revenue decline in the fourth quarter.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Yes, Jerry let me put this framework around it. You are absolutely right. $45 million in Q4 last year sets us up for a pretty tough comparison. If you take our guidance range for Healthcare performance-based fees for the full year versus what we recorded to date, it would suggest at the high end that we are looking for about $25 million of performance-based fees at the high end. So you've got a net decrease year on year just from performance-based fees of approximately $20 million.

If you look at what the implied number is, again, we'll just use the high end for convenience, it's certainly not going to be anywhere, not down near that magnitude. Organically, that's probably going to be the biggest contributor to why we're going to have a tough comparison though is the performance-based fees.

And again, just to remind everybody too, the year-ago performance-based fees we had come into the end of Q3 with our range at $80 million to $90 million, we had indicated on the Q3 call last year we thought the performance-based fees would be toward the upper of the range of $90 million, and they ended up at $105 million. So this was somewhat of a windfall that we were not otherwise expecting in the year.

All of that said, we still think the Healthcare growth for the year is still going to be toward the upper end of the mid-upper single digit range that we talked about in the past.

Jerry Herman - *Stifel Nicolaus - Analyst*

Great. And with regard, Jim, you could help with 2015, you did indicate mid- to high-single digit organic growth. Should we likewise expect some margin movement as we look into 2015?

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

So Jerry, I think the three things that I would comment on about 2015 at this point, again, we haven't finished our budget cycle so some of this is really still very much work in progress, and we are pretty early on, quite honestly. The three things I would say every time we talk about margin coming into the next year, what happens in our budget cycle is we look at the areas of investment that we have to balance in terms of competitive returns to shareholders. So those investments to the extent that they need to take a form of expense or things we expect that we will do, we take them into consideration every single year and really evaluate them as part of the process.

I think the other areas -- so that would suggest that there are potentially some investments that we are looking to make. But I do think that likely the fact that the share base is lower than we think we would've expected coming into next year as well as potentially a little bit lower tax rate, I think there's some compensating factors there.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Yes, Jerry, this is Jim. The only thing I would add to that would be when we look at some of these investments, we have a pretty strict discipline around the investments. And the investments that we're going to be making in the practices are being done because we have for a long time, for since I've been in this position, we've had a very strong inclination towards organic growth. And so if we see an opportunity, we are very strong in the markets that we serve, and if we see an opportunity to grow or expand new competencies or new capabilities, our inclination is to try to do that organically.

So that's -- when Mark talks about the investments, those are ideas and services that are surfacing from the practices that are typically coming up, and we're putting the discipline around them, because we internally expect there to be return on those investments. Hence we watch those very carefully.

But when we do talk about those things, it's probably going to be in some cases that would be in lieu of otherwise having to go out and acquire that. And we feel very comfortable with our ability to grow organically. And I'm sure that's going to be a part of our philosophy for the future as well. Doesn't mean we won't do acquisitions because I'm certain we'll do acquisitions, but we also feel very comfortable on the organic side.

Jerry Herman - *Stifel Nicolaus - Analyst*

If I could sneak one more in regard to acquisitions obviously you have a significant amount of dry powder here. Since you got sort of a public venue here, could you talk about your acquisition criteria, and in particular in the past you've talked about only accretive acquisitions. Can you sort of reframe that discussion or revisit that discussion?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Sure Jerry. So let me frame -- we really look at it from a number of different perspectives, but primarily a return on capital. With us now having locked in a very low positive capital for the convertible debt and then even when you look under the bank line, what our underlying interest rate costs are, it's hard to imagine that on an adjusted EPS basis, so meaning we take intangible amortization out of that expectation, so on a cash EPS basis, we believe that any acquisition is likely to be highly accretive that we would look at.

From that standpoint, when you get back to the acquisition criteria from a return on capital standpoint, we've talked in the past about looking at things in the marketplace that are likely in the 17% to 20% range. We think that if you are looking higher than that you may be too optimistic on your assumptions. We think strategically to the extent that there's something to gain, we would potential look at something lower than that. But again, overall looking at somewhere in that kind of mid-teen type ROI type range.

Jerry Herman - *Stifel Nicolaus - Analyst*

That's great. Thanks guys. Appreciate it.

Operator

You next question comes from the line of Tobey Sommer with SunTrust. Please proceed.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Thanks. Have a question for you on the Legal practice. Year to date there's been a decent amount of a pickup in M&A activity. I think you referenced absence of a second request. Would it be your expectation that based on the deals that have been announced year to date that the next several quarter should be better for the Legal consulting business?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Toby, this is Jim. You know what? I think this is the hardest practice for us to predict where things are going to be going, and I think if I was guessing one way or the other on that comment or that question, it would be pure speculation. We just have very little visibility in this business, and I know that when acquisitions, when M&A activity comes around, I know that we are generally considered very high for those types of things. We won a pretty decent share of them so far, and there's no reason for me to believe that we won't continue to win more than our fair share.

Having said that, the predictability of the stops and starts of those, and frankly even the predictability within a quarter of what portion of them we're going to get is just too much.

So we were a little surprised at the downturn in the third quarter, but we don't view it as any type of weakness that we want to continue to project in the future. We're doing well. We have got a very good track record over the past 18 months in this business. This was just a little bit less than we expected. But we don't expect that to continue.

How and when that picks up remains to be seen. But there is nothing that we are worried about from a strategic perspective about our position in the marketplace that causes us any worry.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Okay. I was wondering on the higher education business, I was wondering if you could compare and contrast your competitive position there versus your competitive position in Healthcare.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

It's an interesting question Toby. Hard to think how to respond to it.

First of all, one of the biggest differences is that the markets -- the buyers, hospitals in one case and universities in the other case, buy services differently, not just from us, but from our competitors as well. In healthcare there tends to be a relatively small number of fairly large projects and in higher education there tends to be a relatively large number of smaller projects. Not to say that some don't get to be bigger, but the average size in the higher education business, average engagement size is significantly less than it is in healthcare.

In terms of our competitive position, I believe we have probably in both practices we have by far and away the largest combined management consulting services, that is mostly operations and strategy. I think combined we probably of the [boast] -- we feel really good about it, but we've got a different set of competitors in the higher education space, we've got a larger number of competitors, some that are very large from a company perspective, firm perspective, but don't do that much work in higher education, but still become very formidable competitors because of a more nationally brand recognition.

In Healthcare, there's probably fewer competitors, but the intensity of the competition is probably more significant. So they are just very different markets for all those reasons, and so there are hard to compare.

Having said that, as I indicated in my script, and I'll repeat this; because I work regularly in both healthcare and education, I think the nature of the turmoil that's taking place in higher education within the market higher education is actually more significant than we are seeing in healthcare. It's just the buyers are buying our services differently, and it will play out.

But I think we're on a very good trajectory for the higher education practice, and I feel very good about the way 2015 is looking.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

And Mark, just one numbers question. Do have an estimate for cash flow for the year and/or the fourth quarter?

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Toby, full-year I think we've been working on about $105 million of cash flow.

Tobey Sommer - *SunTrust Robinson Humphrey - Analyst*

Thank you very much.

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Yes.

Operator

Your next question comes from the line of Randle Reece with Avondale Partners. Please proceed.

Randy Reece - *Avondale Partners - Analyst*

Good afternoon. I'm glad I don't have to make the legal forecast for you. It's wild. In the healthcare arena I want to talk a little bit more about mix and get a little more detail what you can give me in terms of the kind of differences in growth that you are seeing in different practice areas. However you want to define them.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Randy, within just healthcare, is that what you're talking about?

Randy Reece - *Avondale Partners - Analyst*

Yes.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Let's start by saying that the revenue cycle part of our Healthcare practice remains the largest component. I would say next is performance improvement, and then clinical is third.

And I think in terms of growth rate, I think if we were to look back here in December 31 of this coming year, my guess is the growth rate in clinical would probably be growing at a faster rate but it's coming off a smaller base. I think we're still -- we're just seeing continued strength across the services, and we are seeing a very significant increase in the demand for what we call, internally we call our integrated solutions, which is basically institutions that are looking for the collective set when there is revenue, expense, and clinical issues that need to be addressed. And those are the ones where we, I think our experience and our capabilities are capable of adding the most value.

We often go to market individually with revenue cycle performance improvement in clinical, but as I mentioned when we have some of these issues like we're seeing right now where there's some very large projects, and they are really meet the need of the collective set of integrated solutions, that is when we really are at our best I think, and it's great to see how all the teams come together.

So I think you're going to continue to see growth rates within the practices within healthcare that are probably going to be reasonable consistent with what we've seen. There's nothing that tells me about the market right now that would indicate that there's going to be a push for one or the other. Clinical solutions continues to be the smallest but I think its growth rate is going to continue to be the biggest over time. I don't know if that is answering your question, but that's the way we're looking at it.

Randy Reece - *Avondale Partners - Analyst*

Thank you. You have made a number of acquisitions of IT implementers, and how are they performing versus your expectations? And how well do they integrate with your consulting pipeline? How much business do you hand off to them?

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Let me take that one Randy. So let's go back to the Blue Stone acquisition a year ago. I think we mentioned on the call versus the year period prior to acquisition, up almost 30%, and it's gone well. There was some transition where some people did not end up remaining with the company, but it was an expected percentage. In the meantime we hired a tremendous amount of people and continue to have really strong demand, and quite honestly it's not just domestic demand as well. They also have a nice presence in the Canadian market and some overseas markets as well.

So that's gone very well. Truthfully, they really worked very well across our practice because as we have vertical opportunities where we have strength within as an example, within higher education or healthcare, they interface very well with the existing teams and bring capabilities into those particular areas.

Vonlay we are very pleased with. Although we are very early on in that acquisition, while it's only been four or five months now, so we still have more room to go. But we have been pleased with some of the things that we have been able to do in the marketplace. We have more opportunities still to pursue, but so far we've been delighted with the Vonlay team as well.

And then the most recent one, which is a pretty small deal, as I mentioned the results wouldn't be material, Threshold Consulting. But again it really is the capabilities that they have a very differentiated, and really strengthen the offering that we have and have immediate revenue type opportunities as well bringing them into the Company.

I think you will continue to see IT be a theme, but it's not the only theme. We have other things that we certainly like within the businesses. Just happens that these most recent ones have been in technology.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

And one thing Randy, I will point out. We've talked about one of the differences about Huron is being our collaboration. That's something that we stress a lot. I know that a lot of places can talk about it. I think, I'm extremely pleased with the way our practices collaborate, not just over a quarter or a year, but really it's ingrained in our entire culture. And it really shows up.

Use Blue Stone as an example. Mark just walked through some of that. Had they come in and had they not integrated, they would've done whatever their sales efforts would have allowed them to do, they would've pursued their own client base. They would have pursued their own sales channels, and they would've done whatever they did, which we would have assumed to be okay.

But in fact because of the highly collaborative nature of our business, they are working very closely with people in our Healthcare practice, our business advisory area, our Education and Life Sciences, they are working very closely, they have sold work in each of those segments. So a company like that comes in and then it cannot only do what they were planning on doing on their own, but they actually have immediate access to channels that they didn't have before where we happen to have a very strong position.

And so it really enhances their ability to grow organically. It's one of the reasons why we think we can take acquisitions and get a very solid results out of them.

Randy Reece - *Avondale Partners - Analyst*

I just have one last question. When you have contracts that are mostly fixed price but might have some sort of incentive at the end, is all of that revenue accounted in your contingent fee revenue total? I've seen a couple of contracts that had to be publicly filed by your publicly government managed clients where there was several million on the back end of the contract, but it was largely set up as a fixed fee contract.

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Randy, this is Mark. Those contracts are for us are actually fairly clear. The performance-based criteria are really well set out. And the reason that is the case is the client has got to agree with the models after the assessment phase, and then there's a portion that's really truly fixed fees as well, and whatever that allocation is, they are really accounted for separately and very clearly. So for us, there is no intermingling of those contractual arrangements at all.

Randy Reece - *Avondale Partners - Analyst*

Great. Thank you very much.

Operator

(Operator Instructions)

Your next question comes from Joseph Foresi with Janney Montgomery Scott.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

Hi. I'm wondering if you could talk a little bit about just the general pipeline as you head into 2015 versus the pipeline last year. And if there's any changes in deal sizes or projects.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

This is Jim. I'm trying to figure how to respond to that, that's obviously a different answer for each of our practices. Maybe I'll start with the one on Legal, which is probably the easiest, and I'm not sure it's different, but still very unknown without much of visibility. I would say in Healthcare and Education and Life Sciences and business advisory, it's probably stronger than it was at this time of year last year.

We've got as always within Healthcare, they've got a small a number of projects that tend to be much larger, so we'll get into the timing of some of those when we start going through the 2015 planning and look to see how they're going to evolve. But at this point in terms of marketplace demand, I think we're probably as strong if not stronger as we were at this point in time last year.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

Okay. So if I think about that commentary versus your standard for lack of a better term guidance on 2015 of what you're expecting for growth in Healthcare, is there anything to read into it? Are conversion rates any different, or is there just an element of conservatism given the fact that you still haven't gone through all the budgeting process?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

We've said for awhile, you call it our standard guidance but we would maybe use a different term, but I know where you're coming from. We feel in general, when we go back, and having been in this business for a long time, you can look at the demand and you can get really, really excited about what demand would be and you can project all kinds of wonderful things that are going to occur, and sometimes they do and sometimes they don't.

We feel, and we've said this now for multiple years that we feel really good about our ability to maintain the quality of our services and to maintain the efficiency and effectiveness of our businesses by growing organically in the mid- to upper-single digit range. And the reality is I think at least Company-wide we probably exceeded that for the recent past, and we certainly would have hopes to do that again next year.

But we're not going to get over our skis at this point in time. I think for a while you're going to continue to see us talk about that kind of growth rate because that is the position that we feel comfortable about managing our business with. Because we have served that many markets.

We're very cognizant of the quality aspects of the work that we do, and it's the quality of the work that we actually do that enables us to have low turnover and have -- be very competitive in the marketplace. I think we are as competitively, we are as strong as we've ever been. The market demands are very high. And we're just not going to get -- predicting all kinds of wild amounts. We're going to talk about mid- to upper-single digit growth, and hope to beat that, and we're going to have incentives internally that will kick into place if we do beat that. But that I suspect is what you're going to hear from us for some time to come.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

Got it. Okay, two other quick ones for me. It sounds like you are a little bit more excited about Education next year. Is that a fair assessment? Is that based on pipeline, and should we be thinking about maybe an improvement versus sort of what we're seeing right now?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

I would be disappointed if there was not an improvement next year. We went through -- the market changed over the past couple of years, or 18 months to couple of years, in some cases we may been a little bit slow to respond to that. I think we've taken a number of important steps to respond to where I think the market demand is going to be coming from. We've already seen the fruits of some of that labor already. I would expect 2015 to be a better year than 2014 for the segment.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

Got it. Last one from me. Your performance business -- are you taking market share in that business? We had obviously a competitor maybe you don't see them directly discuss the changing outlook in that business and finding it a little bit more difficult. It sounds like you are not seeing the same challenges. I'm wondering if you can comment on what you are seeing from a competitive advantage, from a competitive standpoint.

Mark Hussey - *Huron Consulting Group Inc - COO and CFO*

Joe, the market is really big. It's one that we think is really not just limited to certain sizes of hospitals. We are seeing good demand across mid market, across AMCs, across integrated systems.

We think that there is enough business out there that it's hard for us to tell if we're gaining share or not, quite honestly. We are pleased with the number of wins that we've had, but and we don't really see anything changing in the demand profile for those services.

Joseph Foresi - *Janney Montgomery Scott - Analyst*

Okay great. Thank you.

Operator

Your next question comes from Kevin Steinke with Barrington Research.

Kevin Steinke - *Barrington Research Associates, Inc. - Analyst*

Hi, good afternoon. Just wondering on the large projects related to healthcare consolidation that you've recently closed, has it been determined whether those are going to be fixed fee or performance-based fee?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

No. We are in the early stages -- we're in the middle of the late stages I guess of some of the assessment basis, so no, that has not been determined yet.

Kevin Steinke - *Barrington Research Associates, Inc. - Analyst*

Okay. And if you do win those, are those the type of projects where you might have to ramp up hiring from current levels to meet the demands of those larger, longer-tailed projects?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Probably yes. A lot will depend upon as the assessment goes through -- one of the interesting things about these kinds of projects is that you are not working in one hospital, you may be working in 10 or 20 or 30, and depending upon the size of the system. And so you can't just kind of go in and start doing your work. It has got to be sequenced. And so as you go through the assessment phase, you learn among other things, you learn how you're going to sequence the projects and which part of the integrated solutions you're going to be focusing on first.

So that's the kind of reason you go through the assessment to figure out where things are at. And then they'll make those decisions shortly. And that will probably drive some of our hiring patterns in that practice area.

I do think that once these things begin to start, and my guess is they'll probably start in the first quarter or so give or take a little bit, that you are going -- some of these things could go into 2016, and in some cases, maybe even 2017 revenue. So they are good size. They are longer engagements. And they are very complicated. So I think that's one of the reasons why they look to us. And these have been fairly competitively bid, and we have had a very good track record on these large types of engagements because of the depth of our practice.

Kevin Steinke - *Barrington Research Associates, Inc. - Analyst*

Great. Would you expect to get your normal levels of profitability on those larger contracts?

Jim Roth - *Huron Consulting Group Inc - CEO and President*

I don't see any difference in terms of the margins we've been getting. That's correct.

Kevin Steinke - *Barrington Research Associates, Inc. - Analyst*

All right. Thanks for taking my questions.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Thank you.

Operator

Mr. Roth we have concluded the allotted time for this call. I would like to turn the conference back over to you.

Jim Roth - *Huron Consulting Group Inc - CEO and President*

Thank you for spending time with us this afternoon. We look forward to speaking with you again in February when we announce our fourth-quarter and year-end results. Good evening.

Operator

That concludes today's conference call. Thank you everyone for your participation.