

# A bitter pill

## Online medical industry tries to cheat death

By Sandeep Junnarkar  
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**Led by Netscape Communications founder Jim Clark, online health companies once promised to revolutionize the way patients, doctors, drug manufacturers and insurance carriers do business.**

In the five or so years since, little has changed. The original grand ambitions have been stymied by a wide range of problems that include offline competition, the New Economy bust, opposition by physicians and daunting technological obstacles.

Making matters worse, the entire industry is facing a 2002 government deadline to electronically modernize the way health claims are processed. In the meantime, companies such as WebMD are struggling simply to stay alive.

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In their rush to make a name for themselves, online companies have underestimated the monumental difficulties of integrating the massively outdated technologies used to run the medical business.

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It took awhile for them to get started, but the health insurance carriers have stunted progress of the dot-com medical companies by joining forces to protect their control of the industry.

### **Culture: Not what the doctor ordered** Page 8

Despite their reliance on cutting-edge science, physicians are notorious for their resistance to change--and their refusal to adopt cost- and time-saving business technologies is no exception.

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**You can actually transfer more types of claims and transactions over the Internet than you can through EDI. (The Internet) is a faster, more fluid system. You can have real-time transactions, which you can't in EDI.”**

—Stacey Rich, health care analyst, Jupiter Media Metrix

### **Moving to the Internet: Side effect of 1996 law**

**A 1996 federal law has inadvertently laid the foundation for use of the Internet to keep medical records and process claims.**

The Health Insurance Portability and Accountability Act has no specific provisions involving the Internet, but it does order the use of standard formats and codes for medical and administrative electronic transactions—making the Web a natural place to do this business for patients, doctors, insurers and employer health plans.

Under the law, by Oct. 16, 2002, all parties must adhere to a specific format for such electronic transactions as eligibility confirmation, enrollment checks, treatment authorization, referrals and certification. HIPAA will also establish a new minimum standard to replace the competing formats and codes that now inundate the industry.

The timeline has given a de facto deadline to Internet companies such as WebMD, TriZetto Group and the members of the MedUnite consortium to meet its requirements.

The legislation does not require or even recommend electronic maintenance of medical records, but it does make those who want to use the medium beholden to a minimum federal standard for privacy and security. That portion of the law will be implemented in spring 2003.

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## Technology: A beast untamed

**During a routine examination over the summer, Dr. Prem Misra spent as much time on the phone with an insurance company as he did with his patient.**

The harried gastroenterologist had to punch in a series of ID numbers, codes and passwords on Cigna HealthCare's automated telephone system before getting the necessary eight-digit referral number—a cumbersome procedure he endures dozens of times a day. Still, Misra feels more comfortable with the phone than he does with a computer.

**"I wouldn't want to get referrals through a computer. Every company has a different system over the Internet,"** he said, surrounded by stacks of medical journals and other papers littering his office. **"Why bother? Dialing in is simple enough."**

Such inertia is but one of a panoply of obstacles that have kept the health industry's technologies frozen in Silicon Valley's version of the Stone Age. Several years after Internet pioneer Jim Clark left Netscape Communications to shake up the way health care providers and insurance companies do business, little has changed.

As originally envisioned, Internet companies would revolutionize everything from insurance payments to prescription drug refills, automating every stage of the paperwork process

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—Gastroenterologist Dr. Prem Misra

and clearing away generations of stagnant bureaucracy. Instead, start-ups such as WebMD have been overwhelmed by the sheer size and depth of the technological challenge, encountering unforeseen problems in trying to integrate and update massively outdated systems for billing, insurance and even simple bookkeeping.

**"What people always forget is that health care is a one-to-many business. You aren't connecting (General Motors) to 15 of its plants,"** said Roger Holstein, an executive at WebMD. **"It is like connecting 500,000 doctors to their insurance payers, with each doctor probably having relationships with up to 75 insurers. The challenge is difficult."**

These technological obstacles, compounded by the New Economy bust and cultural obstinacy within the medical profession, have slowed progress in the nascent industry and left it vulnerable to competition from the insurance companies whose operations were the primary target of the medical dot-coms. In one of the sharpest challenges to Internet-based health, a consortium of seven major insurers, including Aetna, Anthem, Cigna and Oxford, formed MedUnite, a company that plans to provide a Web-based transaction system.

Whichever side wins will face yet another daunting obstacle in this multibillion-dollar business: a government-imposed deadline that increasingly seems impossible to meet. The 1996 Health Information Portability and Accounting Act mandates that a greater percentage of medical transactions be conducted electronically by October 2002.

**"Many people think HIPAA lets the federal government barge into a medical practice and dictate how to provide health care, but the law is much less slick in real life,"** said Elisa Chase, principal at Consulting Solutions, a firm that helps medical facilities meet HIPAA-mandated requirements. **"What the feds are saying is that if you bill electronically, let's all do it in the same format."**

There is already resistance to HIPAA's first deadline, with bills before Congress asking that all requirements be implemented in one big bang rather than phased in. The delay could push the timeline back three to five years.

**"That will essentially kill HIPAA. Technologies now being used will mostly be outdated, XML will be more accessible and powerful, and no one is going to get plans rolling for such a far-off deadline,"** Chase said. **"The industry will fragment even more during that time, making it difficult to change."**

Experts helping the medical and insurance industries meet the letter of the law stress that the requirement applies only to those who are already doing business electronically—not to those who continue to work with paper. So what is the incentive to switch to an electronic platform and attract the government's watchful eye and regulations?

As the largest insurer with its Medicare program, the federal government sets different rates for paper claims and electronic claims to give physicians an incentive to move toward electronic processing.

—S.J.

Continued

## Technology: A beast untamed

### A problematic legacy

Modernizing the way health insurance carriers assess patients and process claims is a mind-boggling endeavor. Endless categories of benefits and payments for different medical situations vary from patient to patient depending on such factors as how they are insured, the size of their employers, and the type of health plan negotiated by their companies.

Perhaps underestimating the enormity of that task, online medical companies confidently promised new technologies that would allow doctors to review the full benefit plan of a specific patient immediately and at any given time, regardless of carrier. The information would be constantly updated to show how each patient's medical and prescription history relates to the current examination, the number of visits allowed under the designated health plan, and the latest pricing and payment procedures.

"To get to that point of service for transactions on the Internet will require that the full-fledged complexity of the payer back-end systems be open to the provider," said Jeff Margolis, chief executive at TriZetto Group, an Internet company that provides transaction services for the medical industry. "Not only do (the insurers) have to open up the back-end systems, but the front-end Internet interface has to be kept in constant sync."

"Opening up" back-end systems means sharing company and patient information—something that hospitals and insurance companies historically have been reluctant to do for privacy and competitive reasons. And even when such cooperation can be negotiated, getting these systems to work together is a daunting proposition.

The procedure appears so intricate that most have opted to continue using older Electronic Data Interchanges (EDIs)—closed networks that connect different insurance companies to physicians through clearinghouses—rather than to overhaul them through the Web. But the 1996 health law mandates that patients have the right to obtain their medical records in a timely fashion, and the Internet is the only network that can make that possible.

For an example of the technical challenge, consider the translation of code sets used in EDI to XML, the ubiquitous programming language that serves to transmit formatted data on the Internet. If a physician's office transmits to the Net all of its claims at the end of the day in a single batch—the most common practice today—the data explodes exponentially because of tagging issues, bringing systems to a crawl.

The problem is considered so unmanageable that Humana, a regional insurance company, avoids using XML-based products for transmission of large batches. The company prefers to support XML transactions when they are processed a single claim at a time. But the flexibility of using XML—the ability to add information quickly and in real time—is lost in large data files.

"On real-time transactions, the amount of information transferred tends to be

relatively small. Therefore, the overhead of added tags is inconsequential compared to the greater flexibility that their use offers," said Bruce Goodman, chief information officer at Humana in Louisville, Kentucky.

### Getting ahead of themselves

Both MedUnite and its online rivals initially thought they could create an entirely new system based on the Web that would house, update and disseminate medical records in real time. But that goal has proven overly ambitious, at least within the schedule set by the health law.

Given the technological challenges, MedUnite and its online rivals have acknowledged that they need to learn to live with EDI for a while longer. The consortium, for one, is now trying to link its members in EDI clearinghouses. And WebMD and other online start-ups are offering various services running on the Web or proprietary EDI networks.

"You have to do two things at once: both integrate services into existing systems and migrate (physicians) toward the new Web-based technologies," WebMD's Holstein said. "The level of complexity is incredible. It is difficult for the health plans to write software to respond to a real-time query."

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—Roger Holstein, chief executive, consumer services, WebMD

Continued

## Technology: A beast untamed

Online companies have had some success with smaller insurance carriers, using off-the-shelf systems that can adequately handle their needs. Web start-up TriZetto sold one such system to Humana.

“We built an operational data store which was taking all the critical information out of the legacy systems overnight and putting it in a database that serves as our Web front access,” said Humana’s Goodman. “We basically implemented a plug-and-play system so it is easy for us to plug in another Web site whose back end connects to our Web site.”

But larger insurers have massive systems that require custom software to work with the Web. That is one reason cited by the insurance companies behind MedUnite, which maintains that only the insurers themselves are capable of integrating such large-scale systems and connecting them to the Internet.

Despite an initial fear of creating a system that may allow them to steal each other’s customers or otherwise compromise private data, the competing health insurance companies that formed MedUnite insist they came together largely because they saw no other choice.

“We came to the conclusion that a physician is only going to adopt a different way of doing business and electronic solutions if the system works with different payers,” said Marjorie O’Malley, a senior vice president at Cigna who is overseeing the company’s integration with MedUnite. “Otherwise, working electronically over various systems would be far too complicated.”

MedUnite’s online rivals disagree, arguing that they would eventually be able to manage larger-scale systems as

well. They contend that the real reason for the creation of MedUnite was to allow the insurance companies to maintain absolute control over their industry.

Both sides are looking for profits.

“HIPAA is promoting electronic claims so it is a huge boon to whoever gets in the middle,” said Stacey Rich, health care analyst at research firm Jupiter Media Metrix. The insurance companies “are getting in there because there is a threat of payers and other providers connecting and shutting them out from getting a cut of those transaction fees.”

Like its online counterparts, however, MedUnite faces its own share of problems. The coalition has gotten a late start, having been formed years after companies such as WebMD, and seemed virtually dormant in its first year of existence.

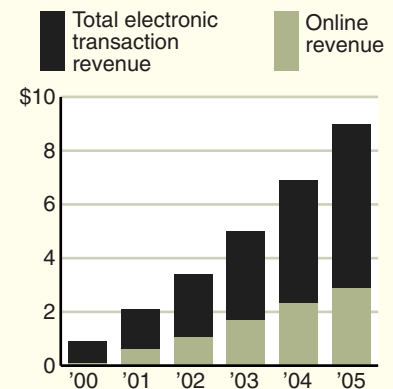
Many industry analysts and executives referred to MedUnite as a mere “press release” put together by the leading insurance companies to undermine the efforts of the Internet start-ups. Chief Executive David Cox defended MedUnite’s silence, saying it had been working with focus groups trying to design a system that would operate across the entire medical sector.

The coalition has come to the realization that it cannot tackle the modernization effort alone, and in June it acquired an EDI company named NDCHealth. WebMD had made a similar move more than a year earlier, acquiring an EDI medical clearinghouse called Envoy.

Regardless of the technologies they use, it is clear that neither MedUnite nor the online start-ups will be able to forge anything close to the versatile and powerful Internet systems touted in

### SLOW SHIFT ONLINE

As electronic business-to-business transactions in the health field grow from just under \$1 billion in 2000 to \$9 billion in 2005, online systems will capture a growing percentage away from EDI.



Source: Jupiter Research

business plans that lured investors at the height of dot-com mania—not, at least, by next fall.

“You can actually transfer more types of claims and transactions over the Internet than you can through EDI,” said Jupiter’s Rich. The Internet “is a faster, more fluid system. You can have real-time transactions, which you can’t in EDI.”

Rich added, “WebMD had this vision of a beautifully integrated health system, and it will get there, but it just won’t get there as quickly as Jim Clark initially had envisioned.”

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## Business: Old-line companies revolt

The online medical industry's dramatic reversal of fortune can be traced to a single day in the spring of last year.

The shares of such companies as WebMD and TriZetto Group began a precipitous slide on March 30, 2000, when The New York Times reported that six of the largest insurance companies were planning to form a consortium, later to be called MedUnite, that would provide similar services to those promised by the Internet start-ups.

"There is no question that part of the timing of MedUnite making its presence felt had to do with trying to disrupt the momentum," TriZetto's Jeff Margolis said. "The timing also won time for the different health plans and MedUnite to come up with a better answer for their physicians and members."

Although dot-com health companies probably would have been caught a few weeks later in the crash that befell most Nasdaq-traded stocks, many executives in the Internet health-data business are certain that news of the consortium speeded the unusually rapid decline in their stocks.

Adding further insult, the Internet companies themselves may have unwittingly played a hand in this fate by riling the health care companies into action with a series of highly public boastings.

"To some extent, the consortium emerged in response to some of the outspokenness of Jim Clark and the Healthon folks, who I think probably were also carried away by their enthusiasm," WebMD's Roger Holstein said. "In their desire to create a new wave, they spoke so loudly...that they scared the health plans into believing...these new Internet businesses could displace them in meaningful ways."

MedUnite and its founding members dismiss the issue of competition, saying simply that the time was right because the appropriate technology to overhaul their processes had finally arrived. "The attention WebMD and others were getting was not a prime motivator for us," Cigna's Marjorie O'Malley said.

Nevertheless, basic survival instincts did seem to come into play when insurance companies decided to team with one

### Key Players

#### WebMD

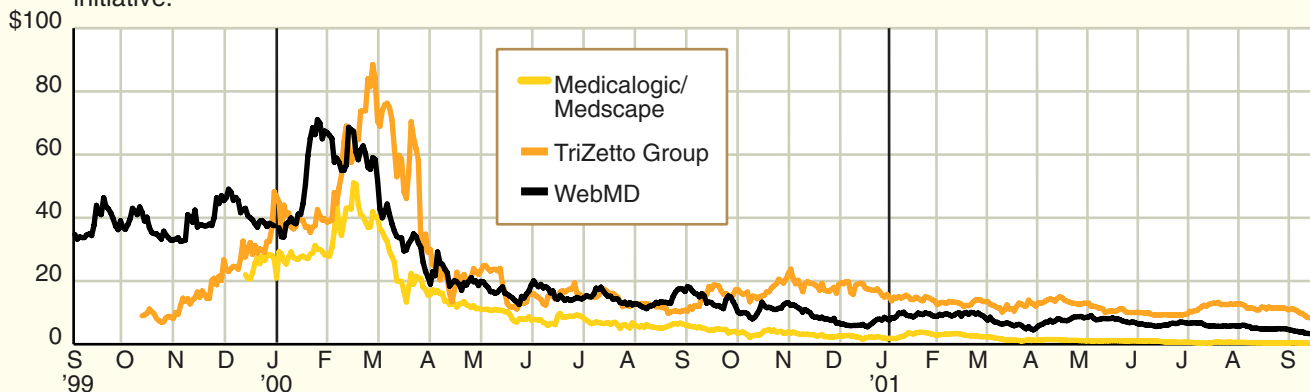
Elmwood Park, N.J.

Formed by the megamerger of Jim Clark's Healthon with WebMD in 1999, the company has suffered an exodus of executives in its recent history. Clark, of Netscape fame, unceremoniously quit WebMD's board of directors last year along with its co-CEO, Jeff Arnold. Co-founder and CTO Pavan Nigham also slipped out around that time. Just last week, WebMD said its president, Marvin Rich, is resigning. Despite the crowded field, once high-flying WebMD with its backing from VC legend John Doerr is the most closely watched of the online health care companies as an indicator of how the sector will fare.

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## RISE AND FALL

Stock prices of notable online health companies from Sept. 1, 1999, to Sept. 21, 2001, showing a dramatic drop in early 2000 following word that traditional insurers would launch a competing initiative.



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## Business: Old-line companies revolt

another rather than go it alone. Their combined forces effectively gave notice to the fledgling Internet companies that they were still the power in the sector.

“I think the health plans said, ‘Hell, the value of some of these Internet companies is greater than the values of our companies,’” said one executive in the thick of the battle. “I don’t want to question their motives going forward, but I think they thought that if the values of companies like WebMD and others declined, it could possibly be leverage to force mergers or acquisitions.”

At least one advantage in the battle may go to whichever side offers the quickest switch from EDI to the Web—not so much for technical reasons as for business demands.

At Pentucket Medical Associates, a practice based in the Northeast with three office locations and about 65 physicians, the move to the Internet is hung up on a licensing issue. The EDI service that the practice now uses, WebMD’s Healthwire, reaches 95 percent of the insurers they deal with, while WebMD’s Web-based product would reach only about 60 percent of the providers at this time, according to Frank MacNeil, Pentucket’s director of information technology.

“The whole benefit to being online is to get one interface regardless of what HMO we are dealing with,” he said. “If WebMD called me and said they had all the HMOs on their Web-based product, I would start the switch-over process immediately.”

### The enemy within

Ironically, the membership of MedUnite could be the consortium’s own worst enemy.

Like any large industry, health insurance has a long history of internal mistrust and bitter rivalry that could hinder the

cooperation necessary for MedUnite to succeed. In addition, the consortium’s collective power in the sector could draw the attention of federal regulators concerned about the possibility of collusion and control of access and prices.

Those obstacles have been encountered by the auto industry’s Covisint, the only other consortium attempting an online conversion of similar scale; it has been mired in technological problems, administrative bickering and a souring market for business-to-business exchanges. Although Covisint came under scrutiny by the Federal Trade Commission, the Justice Department and the European Commission, it was eventually cleared by antitrust authorities.

MedUnite, however, presents a unique conflict of interest for regulators. The federal government, which is charged with protecting consumers from predatory pricing and collusion by large corporations, is in fact the nation’s largest insurer with its Medicare program—and, therefore, has much to gain in cost savings if a standard is established for processing claims electronically. State governments could also reap tremendous savings for Medicaid programs that offer insurance coverage to their indigent populations.

Federal agencies declined to discuss any potential conflict of interest in regulating MedUnite, saying only that the consortium is not under any antitrust scrutiny. MedUnite sees no reason for such concerns, saying that consumers stand to benefit from the long-overdue lancing of an inflamed bureaucracy.

“There are no antitrust issues with what we are doing,” said MedUnite Chief Executive Dave Cox. “What we are saying is that nobody else has the ability to make the changes that are necessary other than the insurance companies.”

### TriZetto Group Newport Beach, Calif.

Reflecting the ongoing consolidation in the industry, TriZetto Group emerged in October 1997 after System One, an early online electronic funds-transfer company, merged with Margolis Health Enterprises, a company that offered technology consulting to health care organizations. TriZetto has fueled its growth over the years with acquisitions, including bringing Creative Business Solutions, FinServ Health Care Systems and HealthWeb Systems under its wings. The company went public Oct. 8, 1999.

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—Stacey Rich, health care analyst,  
Jupiter Media Metrix

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## Business: Old-line companies revolt

“**A company whose only purpose is to play in the middle is a company that is challenged to survive over the long term. You have to throw MedUnite into that category.**”

—A medical industry executive

MedUnite said it is helping health plans electronically streamline their administrative processes. Once the systems have been modernized, the coalition said, it will allow competitors to use its processing networks for claims and benefits.

### Precedents follow the money

Many analysts play down any antitrust concerns, pointing to precedents in the financial industry. Since the early 1980s, automated teller machines operated by competing financial institutions have been linked over vast electronic networks, allowing customers access to their bank accounts regardless of location.

“There are a lot of interconnections for (financial institutions) but also a lot of competition,” said David Main, executive director of the Healthcare Technology Network of Greater Washington, an association that studies the merits of technology in different parts of the health care industry. “I don’t think consolidation has to result in the type of anti-competitive behavior that the federal government would have to be concerned about.”

In the absence of antitrust considerations, Internet medical companies are hoping to exploit the expense and inefficiency that

characterize many large consortiums.

“A company whose only purpose is to play in the middle is a company that is challenged to survive over the long term. You have to throw MedUnite into that category,” one medical industry executive said. “If one health plan comes up with a less-expensive way to directly interact with its constituents, is MedUnite at any less risk than WebMD? I don’t think so.”

But MedUnite’s online rivals face other risks as well. Like all Internet companies, the health start-ups are hoping to stay afloat until the overall economy recovers and business gains traction. For now, most financial analysts concede that the e-health industry seems more a concept than a reality.

“We believe that a couple more quarters could bring signs of material adoption rates at a handful of companies,” James Kumpel, an analyst at Raymond James, wrote in a report last month.

The several dozen companies outside that chosen few, meanwhile, are confronting the dark prospect of looming extinction.

“This is a highly fragmented industry with at least 20 to 25 public and privately funded companies duking it out,” said Jupiter’s Stacey Rich. “There is no way the marketplace can support all these companies.”

“**There are no antitrust issues with what we are doing. What we are saying is that nobody else has the ability to make the changes that are necessary, other than the insurance companies.**”

—David Cox,  
MedUnite CEO

### MedUnite San Diego, Calif.

Seven major health insurance companies played a pivotal part in sending WebMD to the sickbed when they came together to form a consortium that promised to provide the same services as WebMD. Aetna, Anthem, Cigna, Health Net, Oxford, PacifiCare and WellPoint Health Networks officially became strange bedfellows on Nov. 15, 2000, when they announced the formation of MedUnite. With early promises of creating Web-based products, MedUnite is emerging as yet another closed-network player.

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## Culture: Not what the doctor ordered

For all its cutting-edge diagnostic and surgical technologies, the medical field remains largely in the dark ages when it comes to processing claims.

Despite widespread complaints about HMO-mandated administrative chores, resistance to new claims-management technology is endemic and entrenched in the field, according to physicians, health analysts and executives. Executives at Net-based companies who promise to provide such technologies complain of the oppressive struggle to change physicians' behavior.

Most doctors say they have little time to learn new administrative tricks when it is difficult enough keeping up with scientific breakthroughs in their specialties. But others attribute their stubbornness more to simple inertia and a discomfort with new technology among older physicians.

"Doctors are people who cling to their own patterns and routines," said Healthcare Technology Network's David Main. "Getting doctors together to do anything is like herding cats. The barriers are economic, force of habit, and some of it is age."

Of the estimated 30 billion claims processed per year by physicians' offices, hospitals, pharmacies and the insurance companies, industry executives and analysts note that only about 5 billion are conducted electronically. Of those, the vast majority are processed through antiquated and high-maintenance EDI systems despite nearly universal claims of lower costs in doing business over the Internet.

Take the case of Dr. Mark Michael and his Cincinnati, Ohio-based allergy and asthma practice. He has been using software made by Lytec Systems for the past decade, sending electronic claims over a closed EDI network. Although his interest is piqued by the many promises

“**Getting doctors together to do anything is like herding cats. The barriers are economic, force of habit and...age.**”

—David Main, executive director, Healthcare Technology Network of Greater Washington

of lower expense and greater efficiency on the Net, he doesn't feel compelled to do anything differently.

"I have been using the same software since it came out, and I am happy with it," Michael said. "If you tell me I need to use new software to get to the Internet, I don't think I would switch."

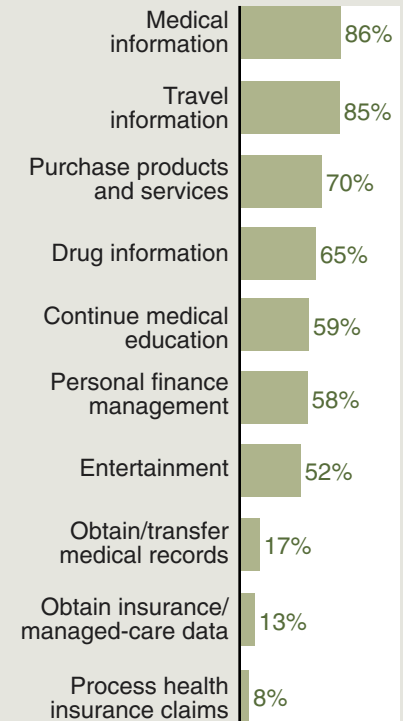
A recent study by the American Medical Association reinforces those sentiments. Only 8 percent of physicians surveyed said they used the Web to process their health insurance claims. At the same time, however, doctors have dramatically increased their use of technology—75 percent report using a computer and 70 percent use the Internet—for medical research and access to information on sites such as Medline, WebMD and Medscape.

“**I have been using the same software since it came out, and I am happy with it. If you tell me I need to use new software to get to the Internet, I don't think I would switch.**”

—Dr. Mark Michael, allergist

### No claims

Physicians turn to the Web for a range of activities, but obtaining medical records and dealing with health insurance claims are low on the list. What they seek and do:



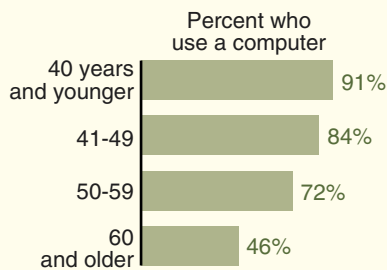
Source: American Medical Association

Continued

## Culture: Not what the doctor ordered

### AGE RESISTANCE

Computer use among physicians decreases as age increases.



Source: American Medical Association

“The resistance is not resistance to EDI or the Internet,” MedUnite’s David Cox said. “It is just that physicians don’t yet see any what they were doing before—that’s the big hang-up.”

The passing of time offers some hope for online technology in the profession. As older doctors retire and are succeeded by younger, more computer-savvy physicians, Net-based claims services may see growing popularity.

The AMA study reinforces anecdotal indications that age is a major factor in how quickly the Internet is being assimilated as a medical and administrative tool for health professionals. The study found that 91 percent of physicians 40 years of age or younger use a computer; among those 60 or older, however, only 46 percent use a PC.

The larger online medical companies have been buying more traditional EDI network technologies as an interim measure in response to the dual barriers of physician resistance and the usage of outdated technology, hoping to ease the transition of physicians to the Internet over the long term. WebMD acquired Envoy last year, and MedUnite acquired the claims processing business of NDCHealth this summer.

“If a physician wants to use only EDI, that is fine. We will try to move them to the additional robustness of real-time, Web-enabled functionality,” Cigna’s Marjorie O’Malley said. “We will work with physicians at whatever rate they want and when they are ready.”

That may be the most progress online medical companies can hope for at this time. On the bright side, though, the doctors who do learn to use processing technologies often become loyal fans—once they finally agree to try them.

“The speed of getting your money is great! Really, I would never go back to paper claims,” Michael said of his EDI system. “Compared to the paper claim we used to send, it is like having a luxury car vs. a horse and buggy.” ■

“**The resistance is not resistance to EDI or the Internet. It is just that physicians don’t yet see any advantages over what they were doing before—that’s the big hang-up.**”

—David Cox, MedUnite CEO

### Online Health Resources

#### The companies

**WebMD**

<http://www.webmd.com>

**TriZetto Group**

<http://www.trizetto.com>

**Medscape**

<http://www.medscapeinc.com>

#### The consortia

**MedUnite**

<http://www.medunite.com>

**Aetna U.S. Healthcare**

<http://www.aetnaushc.com>

**Anthem**

<http://www.anthem.com>

**Cigna HealthCare**

<http://www.cigna.com/consumer/index.html>

**Health Net**

<http://www.health.net/home.asp>

**PacifiCare Health Systems**

<http://www.pacificare.com>

**WellPoint Health Networks**

<http://www.wellpoint.com>

#### The observers

**American Medical Association**

<http://www.ama-assn.org>

**The Health Insurance Portability and Accountability Act of 1996 (HIPAA) page**

Health Care Financing Administration  
<http://www.hcfa.gov/hipaa/hipaahm.htm>

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