WEBMD CORP /NEW/
Form 10-Q
August 14, 2001
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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2001

or

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 0-24975

WEBMD CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

(State or Other Jurisdiction of Incorporation or Organization)

94-3236644

(I.R.S. Employer Identification Number)

669 River Drive, Center 2

Elmwood Park, New Jersey 07407-1361

(Address of Principal Executive Offices)

(201) 703-3400

(Registrant s telephone number, including area code)

Check whether the registrant: (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes x No o

As of July 27, 2001, there were 359,708,024 shares of the

Registrant s Common Stock outstanding.

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WEBMD CORPORATION

QUARTERLY REPORT ON FORM 10-Q

For the Period Ended June 30, 2001

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CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

This quarterly report on Form 10-Q contains both historical and forward-looking statements. All statements other than statements of historical fact are, or may be deemed to be, forward-looking statements within the meaning of section 27A of the Securities Act of 1933, as amended, and section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements are not based on historical facts, but rather reflect management s current expectations concerning future results and events. These forward-looking statements generally can be identified by use of statements that include phrases such as believe, expect, anticipate, intend, plan, foresee, likely, wi similar words or phrases. Similarly, statements that describe our objectives, plans or goals are or may be forward-looking statements. These forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause our actual results, performance or achievements to be different from any future results, performance and achievements expressed or implied by these statements. In addition to the risk factors described in Management s Discussion and Analysis of Financial Condition and Results of Operations Factors that may affect future results of operations beginning on page 20, the following important risks and uncertainties could affect future results, causing these results to differ materially from those expressed in our forward-looking statements:

the expected benefits from our restructuring and integration efforts not being fully realized or not being realized within the expected time frames

the failure to achieve sufficient levels of physician utilization and market acceptance of new services or newly integrated services

the inability to successfully deploy new applications or newly integrated applications the inability to attract and retain qualified personnel

outcome of pending litigation and claims

general economic, business or regulatory conditions affecting the Internet and healthcare communications industries being less favorable than expected.

These factors and the risk factors described in Management s Discussion and Analysis of Financial Condition and Results of Operations Factors that may affect future results of operations beginning on page 20 are not necessarily all of the important factors that could cause actual results to differ materially from those expressed in any of our forward-looking statements. Other unknown or unpredictable factors also could have material adverse effects on our future results. The forward-looking statements included in this quarterly report on Form 10-Q are made only as of the date of this quarterly report. We expressly disclaim any intent or obligation to update any forward-looking statements to reflect subsequent events or circumstances.

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PART I

FINANCIAL INFORMATION

ITEM 1. *Financial Statements*

WEBMD CORPORATION

CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands, except share data)

	June 30, 2001	December 31, 2000
	(unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	$491,855	$490,797
Short-term marketable securities	96,376	
Accounts receivable, net	182,107	195,071
Current portion prepaid content, services and distribution	10,493	5,268
Assets held for sale	214,556	214,556
Other current assets	26,369	38,941

Total current assets	1,021,756	944,633
Marketable securities	8,560	219,686
Property and equipment, net	75,459	90,356
Prepaid content, services and distribution	118,240	229,081
Intangible and other assets, net	5,306,652	6,971,875
	$6,530,667	$8,455,631

LIABILITIES AND STOCKHOLDERS EQUITY

Current liabilities:		
Accounts payable	$15,524	$19,563
Accrued expenses	252,477	272,932
Deferred revenue	51,473	45,891
Total current liabilities	319,474	338,386
Other long-term liabilities	1,894	15,260
Series B convertible redeemable preferred stock, $0.0001 par value; 200 shares authorized; 100 shares issued and outstanding	10,000	10,000
Stockholders equity:		
Series A convertible preferred stock; $0.0001 par value; 213,000 shares authorized; 155,951 shares issued and outstanding at December 31, 2000		710,746
Common stock, $0.0001 par value; June 30, 2001: 600,000,000 shares authorized; 365,225,845 shares issued; December 31, 2000: 600,000,000 shares authorized;		

361,233,643 shares issued
37 36
Additional paid-in capital
11,641,541 11,028,461
Treasury stock, at cost, June 30, 2001: 5,676,595 and December 31, 2000: 5,163,509
(33,594) (30,759)
Unrealized gain on marketable securities
5,860 4,996
Deferred stock compensation
(76,375) (144,467)
Accumulated deficit
(5,338,170) (3,477,028)

Total stockholders equity
6,199,299 8,091,985

$6,530,667 $8,455,631

See notes to condensed consolidated financial statements.

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WEBMD CORPORATION

CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data, unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2001	**2000**	**2001**	**2000**
Revenue (1)	$178,714	$101,074	$363,205	$166,955
Costs and expenses:				
Cost of operations	119,366	78,194	244,710	137,559
Development and engineering	9,141	14,684	21,513	26,258
Sales, marketing, general and administrative				

	113,809	124,136	242,367	224,662
Depreciation and amortization	755,073	416,428	1,514,870	755,138
Restructuring and integration charge	11,211		219,894	
Interest income, net	8,103	14,064	19,007	26,893
Net loss	$(821,783)	$(518,304)	$(1,861,142)	$(949,769)
Basic and diluted net loss per common share	$(2.30)	$(2.64)	$(5.21)	$(5.11)
Weighted-average shares outstanding used in computing basic and diluted net loss per common share	357,878	196,471	357,342	185,756

(1) Includes revenue from related parties of $0 and $10,063 for the three months ended June 30, 2001 and 2000, respectively and $3,000 and $23,048 for the six months ended June 30, 2001 and 2000, respectively.

See notes to condensed consolidated financial statements.

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WEBMD CORPORATION

CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands, unaudited)

	Six Months Ended June 30,	
	2001	**2000**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss	$(1,861,142)	$(949,769)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,514,870	755,138
Non-cash stock compensation	53,550	26,806
Amortization of non-cash prepaid content, services and distribution	16,383	39,260
Non-cash portion of restructuring and integration charge	185,498	
Changes in operating assets and liabilities:		
Accounts receivable	9,962	(24,445)
Prepaid content, services and distribution	(10,310)	
Other assets	5,098	(9,036)
Accounts payable	(4,762)	(27,070)
Accrued expenses	(13,880)	(34,911)
Deferred revenue	5,004	(2,493)
Net cash used in operating activities	(99,729)	(226,520)

CASH FLOWS FROM INVESTING ACTIVITIES:

Redemptions of marketable securities	119,000	
Purchases of marketable securities		(62,500)
Purchases of property and equipment	(14,381)	(14,042)
Cash paid in business combinations, net of cash received	(6,042)	(285,223)
Net cash provided by (used in) investing activities	98,577	(361,765)

CASH FLOWS FROM FINANCING ACTIVITIES:

Proceeds from issuance of common stock, net of repurchase and issuance costs	7,208	944,789
Principal payments of capital lease obligations	(2,163)	(2,572)
Purchases of treasury stock	(2,835)	
Net cash provided by financing activities	2,210	942,217
Net increase in cash and cash equivalents	1,058	353,932
Cash and cash equivalents at beginning of period	490,797	291,286

Cash and cash equivalents at end of period	$491,855	$645,218

SUPPLEMENTAL SCHEDULE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:

Issuance of equity securities in connection with strategic alliances and services	$17,500	$
Issuance of common stock for asset purchases	$	$2,395,518
Issuance of preferred stock for asset purchases	$	$629,000
Deferred compensation related to options granted	$	$93,752

See notes to condensed consolidated financial statements.

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WEBMD CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(In thousands, except share and per share amounts)

1. Summary of Significant Accounting Policies

Organization and Business

WebMD Corporation (the Company) was incorporated in December 1995 and commenced operations in January 1996, as Healtheon Corporation. In May 1998, the Company merged with ActaMed Corporation (ActaMed) in a transaction accounted for as a pooling of interests. In November 1999, the Company completed the acquisitions of WebMD, Inc., MedE America Corporation (MedE America) and Greenberg News Networks, Inc. (Medcast) and changed its name from Healtheon Corporation to Healtheon/WebMD Corporation. In January 2000, the Company completed its acquisition of Kinetra LLC (Kinetra). In May 2000, the Company completed its acquisition of Envoy Corporation (Envoy). In September 2000, the Company completed its acquisitions of Medical Manager Corporation (Medical Manager), CareInsite, Inc. (CareInsite) and OnHealth Network Company (OnHealth) and changed its name from Healtheon/WebMD Corporation to WebMD Corporation. All financial information has been presented to reflect the combined operations of the Company and the WebMD, Inc., MedE America, Medcast, Envoy, Medical Manager, CareInsite and OnHealth acquisitions for the period subsequent to each respective acquisition date.

Basis of Presentation

The unaudited condensed consolidated financial statements have been prepared by management and reflect all adjustments that, in the opinion of management, are necessary for a fair presentation of the interim periods presented. The results of operations for the three and six months ended June 30, 2001 are not necessarily indicative of the results to be expected for any subsequent period or for the entire year ending December 31, 2001. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted under the Securities and Exchange Commission s rules and regulations.

These unaudited condensed consolidated financial statements and notes included herein should be read in conjunction with the Company s audited consolidated financial statements and notes for the year ended December 31, 2000, which were included in our annual report on Form 10-K filed with the Securities and Exchange Commission.

Revenue

The Company provides a range of transaction and information services and technology solutions for participants across the entire continuum of healthcare, including physicians and other healthcare providers, payers, patients and suppliers. The revenue associated with these solutions provided by the Company are aggregated into four primary product groupings as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2001	2000	2001	2000
Transaction services	$96,895	$54,995	$194,413	$86,516
Physician services	65,128	9,171	130,226	15,953
Portal services	15,860	26,752	35,771	48,171
Other	831	10,156	2,795	16,315

$178,714	$101,074	$363,205	$166,955

Revenue recognized from arrangements deemed to be non-monetary exchanges of our products and services for customer products and services totaled approximately $5,813 and $11,508 during the three and

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WEBMD CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

six months ended June 30, 2001, respectively, and $6,221 and $9,301 during the three and six months ended June 30, 2000, respectively. Revenue was determined at the time of the exchange based upon the fair value of the products and services to be provided or received, whichever is more clearly evident.

Revenue from related parties consists of revenues for services provided to Microsoft for the three and six months ended June 30, 2001, revenue for services provided to News Corporation for the three months ended March 31, 2001 and revenue for services provided to News Corporation, Microsoft and UnitedHealth Group for the three and six months ended June 30, 2000. Revenue from UnitedHealth Group ceased being considered from a related party in January 2000 when the Chairman and Chief Executive Officer of UnitedHealth Group resigned from our board of directors. Revenue from News Corporation ceased being considered from a related party as of February 15, 2001 when News Corporation surrendered the Company s Series A convertible preferred stock.

Reclassifications

Certain reclassifications have been made to the financial statements to conform with the current year presentation. These reclassifications had no effect on previously reported financial position or results of operations.

2. Business Combinations and Strategic Relationships

American Online, Inc.

In May 2001, the Company entered into an agreement for a strategic alliance with AOL Time Warner, Inc. (AOL). The term of the agreement is three years. Under the agreement, the Company will be the primary provider of healthcare content, tools and services for use on AOL properties that include AOL, AOL.com, CompuServe and Netscape.com. In addition, the Company will create a co-branded personalized health service for AOL that will feature the Company s personalized news, health assessment and monitoring tools, communities and newsletters, integrated with AOL s calendaring and reminders. The Company and AOL intend, through the co-branded services, to provide users with the ability to communicate with their health plans, physicians, pharmacies and other providers. The Company and AOL will share revenue from advertising (whether or not related to healthcare), commerce and programming on the health channels of the AOL properties and on the co-branded service, with the Company receiving 80% of revenues up to an agreed-upon annual threshold and 60% thereafter. The Company will not make any cash payments for carriage fees to AOL. In connection with the strategic alliance, WebMD issued to AOL a warrant to purchase 2,408,908 shares of WebMD common stock at an exercise price of $9.25 per share. The warrant was valued at approximately $17,500 using the Black Scholes options pricing model and is being amortized over the term of the strategic alliance as a non-cash sales and marketing expense.

Microsoft

The Company originally entered into a strategic relationship with Microsoft in May 1999. In April 2001, the Company and Microsoft entered into definitive agreements to implement a new relationship effective as of January 1, 2001. The original relationship and the new relationship are each described below.

Original strategic relationship

Under the terms of the original strategic relationship, the Company has been developing, hosting and maintaining on its servers a health channel for MSN and was required to pay Microsoft an aggregate of

WEBMD CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

$162,000 in carriage fees for the distribution of that content. In addition, Microsoft and the Company each committed co-marketing funds of $50,000 over the first two years of the term.

Microsoft was required to remit to the Company 100% of the net revenue over the term of the agreement from banner and other advertising and e-commerce transactions generated on the health channel or advertising that Microsoft placed on WebMD.com each year during the term until the Company received an amount equal to that year s carriage fees, including guaranteed minimum amounts of $22,500 in each of the first two years of the term, and was required to share revenue equally after that. The Company was required to pay Microsoft a 25% commission on the portion of the revenue received up to the annual guaranteed minimum amounts for all advertisements placed by Microsoft. The Company recognized this advertising revenue when Microsoft notified the Company that advertisements had been placed on the health channel and billed by Microsoft, not based on the guaranteed minimum amounts.

Microsoft agreed to sponsor up to 5.0 million subscriber months to the Company s physician Web site for $29.95 per month over the term of the agreement. The Company was required to pay a $5 per month commission on all subscriptions placed by Microsoft.

The Company was required to share with Microsoft 50% of net revenue from banner and other advertising on its physician Web site generated by sponsored subscriptions until Microsoft received the amount it had incurred for its sponsored subscriptions. Thereafter, the Company was required to share 25% of this revenue with Microsoft. In addition, the Company was required to share with Microsoft 15% of its net revenue from e-commerce transactions and additional services not included in the basic subscription to the Company s physician Web site generated by these sponsored subscriptions.

New strategic relationship

To implement the new relationship, the Company and Microsoft entered into two definitive agreements. Under the first agreement: (i) the Company has agreed to adopt the PocketPC, Windows 2000 and SQL Server 2000 as the development platform for ULTIA, the Company s new handheld solution for physicians, which operates on a wireless LAN and integrates with the physician s practice management system; (ii) the Company has agreed to make Intergy, its new physician practice management system, available to run on Windows 2000 and SQL Server 2000; (iii) Microsoft has agreed to provide performance-based funding tied to the roll-outs of ULTIA and Intergy; (iv) the Company has agreed to continue to transition the WebMD.com portal to Windows 2000 and SQL Server 2000 when the Company makes additional investments in its portal; and (v) Microsoft has agreed to provide consulting services, support and other resources in connection with these undertakings. The amount of the performance-based funding to be received by the Company pursuant to this agreement will be determined based on the number of physicians to whom Microsoft software is deployed in connection with deployments of ULTIA and Intergy. The Company will be obligated to pay agreed upon fees to Microsoft to license such software from Microsoft. The term of this agreement is scheduled to expire on December 31, 2004 and became subject to termination by either party under its terms beginning on May 18, 2001 because the parties had not reached agreement at that time on terms for an Application Services Agreement (ASP Agreement) and related documents to govern deployments by the Company of Microsoft software on an ASP basis. This agreement is also subject to mutual agreement on certain technology-related requirements.

Under the second agreement, the Company will provide programming to the MSN health channel, and the Company and MSN will share revenues derived from advertising, sponsorship and e-commerce on the MSN health channel site, with the Company receiving 100% of revenues up to an agreed upon annual threshold (or until an agreed upon maximum for the contract period is reached), and 60% thereafter. The term of this agreement is scheduled to expire on June 30, 2004.

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WEBMD CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

As a result of the execution of these agreements, Microsoft is no longer responsible for funding the sponsorship of subscriptions to the Company s physician portal, and the Company is no longer required to share with Microsoft revenue generated by physician usage of the Company s healthcare portals. Additionally, the Company will no longer be required to pay Microsoft carriage fees for the distribution of content.

The Company has neither received nor made any payments relating to the new relationship for the three and six months ended June 30, 2001.

News Corporation

Pursuant to an agreement signed and publicly announced in December 1999 and closed in January 2000, the Company entered into a strategic relationship with News Corporation. On December 29, 2000, this strategic alliance was revised by the parties. On February 15, 2001, the Company completed all transactions related to its revised strategic relationship with News Corporation. The original relationship and the revised relationship are each described below.

Original strategic relationship

The financial terms of the strategic relationship included $700,000 in media branding services by News Corporation, comprised of $400,000 domestically and $300,000 internationally over 10 years; a $100,000 cash investment commitment by News Corporation in an international joint venture; a $60,000 five-year licensing agreement for syndication of WebMD daily broadcast content; and the transfer to the Company of 50% interests in The Health Network, a health-focused cable network, and thehealthnetwork.com. The Company issued an aggregate of 155,951 shares of Series A preferred stock, convertible into 21,282,645 shares of the Company s common stock. In addition, affiliates of News Corporation purchased 2,000,000 shares of the Company s common stock for an aggregate purchase price of $100,000 in cash.

New strategic relationship

The Company retained the right to receive $205,000 in domestic media services from News Corporation over ten years and will continue to provide content for use across News Corporation s media properties for the next four years. News Corporation transferred its 50% interest in the international joint venture to the Company and was relieved of its commitment to provide any future capital to the international joint venture and its commitment to provide any international media services. The Company transferred its interest in The Health Network to News Corporation. The Company was also relieved of all future capital commitments to The Health Network. In connection with the revisions to the relationship, News Corporation surrendered 155,951 shares of WebMD s Series A Convertible Preferred Stock. The Company granted to News Corporation a warrant to acquire 3,000,000 shares of its common stock at an exercise price of $15 per share.

2001 Acquisitions

During May and June of 2001, the Company acquired the assets of four physician services companies for approximately $9,800. The purchase price consisted primarily of cash. These acquisitions were accounted for using the purchase method of accounting with the purchase price being allocated to assets acquired and liabilities assumed based on their fair values. The goodwill related to these transactions is being amortized over five years. The results of operations of these physician services companies have been included in the Company s financial statements as of their respective acquisition dates.

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WEBMD CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

2000 Acquisitions

On September 12, 2000, the Company completed its acquisition of Medical Manager, a provider of physician practice management systems in the U.S. and its publicly traded subsidiary, CareInsite, a developer of an Internet-based healthcare e-commerce network that links physicians, suppliers and patients. The total purchase consideration was approximately $2,906,856, comprised primarily of common stock. Both acquisitions were accounted for using the purchase method of accounting.

On September 12, 2000, the Company completed its acquisition of OnHealth, a source of consumer-oriented health and wellness information, products and services on the Web. The total purchase consideration was approximately $363,010, comprised primarily of common stock. The acquisition was accounted for using the purchase method of accounting.

On May 26, 2000, the Company completed its acquisition of Envoy, a provider of electronic data interchange and transaction processing services to participants in the healthcare market. The total purchase consideration was approximately $2,440,240, comprised primarily of common stock. The acquisition was accounted for using the purchase method of accounting.

On January 31, 2000, the Company completed its acquisition of Kinetra, a provider of health information networks and e-commerce services. The total purchase consideration was approximately $291,538, comprised primarily of common stock. The acquisition was accounted for using the purchase method of accounting.

Unaudited Pro Forma Financial Information

The following unaudited pro forma financial information gives effect to the acquisitions of Kinetra, Envoy, Medical Manager, CareInsite and OnHealth, including the amortization of goodwill and other intangible assets, as if they had occurred as of the beginning of each period presented. The effect of all other business combinations was not material to the pro forma financial information presented below. The information is provided for illustrative purposes only and is not necessarily indicative of the operating results that would have occurred if the transactions had been consummated at the dates indicated, nor is it necessarily indicative of future operating results of the combined company and should not be construed as representative of these amounts for any future periods.

	Three Months Ended June 30, 2000	Six Months Ended June 30, 2000
Total revenue	$ 208,048	$ 391,684
Net loss	$ (908,173)	$ (1,803,759)
Basic and diluted net loss per share	$ (2.53)	$ (5.07)

3. Restructuring and Integration Charge

In the third quarter of 2000, the Company s board of directors approved a restructuring and integration plan, with the objective of eliminating duplication and redundancies as a result of the acquisitions made by the Company since November 1999 and consolidating the Company s operational infrastructure into a common platform to more efficiently serve its customers.

Additionally, as part of the Company s restructuring and integration efforts, the Company also undertook a review of its existing strategic relationships in light of several criteria, including strategic relevance to both the Company and its partners, potential conflicts with other agreements as a result of the numerous acquisitions made by the Company, profitability and impact on future revenue streams. As a

WEBMD CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

result of this process, the Company has been and is in discussions with several of its partners in an effort to redefine the relationships in a manner that better serves the needs of each party. These discussions have resulted in revisions to some strategic relationships. It is possible that, as a result of continuing discussions, additional relationships may be revised or terminated, which may result in additional restructuring charges. During calendar year 2000, the Company s restructuring and integration efforts resulted in the identification and notification of approximately 1,100 employees whose positions with the Company were to be terminated primarily as a result of eliminating duplicate functions within the combined company, the identification of duplicate facilities to be vacated and the restructuring of several strategic relationships including those with News Corporation and DuPont.

The Company s restructuring and integration efforts continued in 2001. In connection with these efforts, a charge was recorded for the three months ended June 30, 2001 of $11,211, which consists of $8,000 in payments made to customers to exit contractual obligations and $3,211 of additional integration costs for employee retention arrangements related to exit activities. For the six months ended June 30, 2001 a charge of $219,894 was recorded, which consists of: (i) $138,039 relating to the restructuring of our strategic relationships primarily associated with Microsoft, of which $133,500 represented non-cash charges related to the write-off of intangible assets associated with the Company s original Microsoft agreement recorded as part of the Company s acquisition of WebMD, Inc. in 1999, (ii) personnel-related costs of $63,463, of which $51,998 represented non-cash stock option compensation charges primarily related to the resignation or termination of certain employees pursuant to the applicable employment and separation arrangements, with the remaining personnel-related charge relating to severance and outplacement services for approximately 350 additional employees that the company identified and notified of termination during the three months ended March 31, 2001, (iii) facilities charges of $1,985, comprised of future lease obligations and lease cancellation penalties related to vacating additional facilities identified during the three months ended March 31, 2001, (iv) $8,000 in payments made to customers to exit contractual obligations, (v) $8,407 of integration costs, consisting of employee retention arrangements related to exit activities. Integration costs are recorded as expense in the period in which they arise.

The following tables presents activity in the restructuring and integration related accrual through June 30, 2001:

	Severance	Facilities	Other	Total
Balance at December 31, 2000	$8,599	$35,843	$8,683	$53,125
Accruals	11,465	1,985	20,947	34,397
Cash payments	(15,022)	(4,910)	(15,753)	(35,685)
Balance at June 30, 2001				

$5,042	$32,918	$13,877	$51,837

The Company expects to pay substantially all the remaining restructuring and integration liabilities noted above, other than those related to lease payments that are long-term in nature, by the end of 2001.

4. Stockholders Equity

On March 29, 2001, the Company announced a stock buy-back program (the Program). Under the Program, the Company may use up to $50,000 to purchase shares of its common stock from time to time beginning on April 2, 2001, subject to market conditions. As of June 30, 2001, the Company has repurchased 513,086 shares at a cost of approximately $2,835 under the Program. These shares are currently held as treasury shares.

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WEBMD CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

5. Assets Held for Sale

In connection with the acquisition of Medical Manager and the related integration and consolidation of the Company s acquired businesses, its board of directors approved management s plan to dispose of Porex Corporation and its other plastics and filtration technologies subsidiaries, referred to collectively as Porex. Porex Corporation was a wholly owned subsidiary of Medical Manager prior to the completion of the acquisition of Medical Manager on September 12, 2000. Porex designs, manufactures and distributes porous and solid plastic components and products used in life sciences, healthcare, industrial and consumer applications. The expected net proceeds and the cash flows of Porex until sold were allocated to net assets held for sale in the allocation of the Medical Manager purchase price and is included in current assets. Any difference between the actual and expected net proceeds will result in an adjustment of goodwill unless there is a difference caused by a post-acquisition event. The Company has received competitive bids for Porex as a whole as well as for portions of Porex and is in the process of evaluating these bids.

Activity in net assets held for sale from the acquisition date to June 30, 2001 is as follows:

Allocation of purchase price	$204,356
Estimated net income through disposition	10,200
Balance at June 30, 2001	

$214,556

Porex had net income of $3,590 and $6,203 for the three and six months ended June 30, 2001, respectively, and net income of $8,959 from the acquisition date to June 30, 2001. Porex s results of operations and cash flows have been excluded from the consolidated statement of operations for the three and six months ended June 30, 2001.

6. Marketable Securities

All highly liquid marketable securities with an original maturity from date of purchase of three months or less are considered to be cash equivalents. Management determines the appropriate classification of its investments in debt securities at the time of purchase and re-evaluates such determinations at each balance sheet date. Debt securities are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity. Debt securities that the Company does not have the intent or ability to hold to maturity are classified as available-for-sale. Available-for-sale securities are carried at fair value as of the balance sheet date. At June 30, 2001, the Company s investments consisted principally of U.S. Treasury Notes. These investments, which had an aggregate market value of $96,376 and a cost of $93,273, were classified as available-for-sale. Unrealized gains on these securities were $3,103 at June 30, 2001.

In addition, at June 30, 2001 the Company had equity investments in publicly traded companies with an aggregate market value of $8,560 and a book value of $5,803. Unrealized gains on these securities were $2,757 at June 30, 2001.

7. Net Loss Per Common Share

Basic net loss per common share and diluted net loss per common share are presented in conformity with Statement of Financial Accounting Standards No. 128, Earnings Per Share (SFAS No. 128). Under SFAS No. 128, basic net income per share is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted net income per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock.

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WEBMD CORPORATION

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

The Company has excluded all convertible redeemable preferred stock, convertible preferred stock, warrants, and outstanding stock options from the calculation of diluted loss per common share because all such securities are anti-dilutive for the periods presented. The total number of shares excluded from the calculation of diluted net loss per share was approximately 159,400,000 shares at June 30, 2001 and approximately 104,700,000 shares at June 30, 2000.

8. Recent Accounting Pronouncements

On July 20, 2001, the Financial Accounting Standards Board (FASB) issued SFAS No. 141, Business Combinations and SFAS No. 142, Goodwill and Other Intangible Assets. The Company is required to adopt these pronouncements beginning January 1, 2002. SFAS No. 141 requires all business combinations initiated after June 30, 2001 to be accounted for using the purchase method of accounting. The impact of adopting SFAS No. 141 is not expected to be significant. SFAS No. 142 changes the accounting for goodwill and other intangible assets. Goodwill will no longer be subject to amortization over its estimated useful life. Rather, goodwill will be subject to at least an annual assessment for impairment by applying a fair-value-based test. All other acquired intangibles should be separately recognized if the benefit of the intangible asset is obtained through contractual or other legal rights, or if the intangible asset can be sold, transferred, licensed, or exchanged, regardless of the acquirer s intent to do so. Other intangibles will be amortized over their useful lives. The Company has not yet determined the impact of adopting the fair-value-based test provisions of SFAS No. 142.

9. Commitments and Contingencies

In July and August, 2001, three purported class action lawsuits were filed against Morgan Stanley & Co. Incorporated and Goldman Sachs & Co., underwriters of the initial public offering of the Company (then known as Healtheon) in the United States District Court for the Southern District of New York. One of these suits also named the Company and two of its former officers as defendants in the case. The complaints allege violations of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder because of failure to disclose certain practices alleged to have occurred in connection with the distribution of shares in the Healtheon IPO. The suit that names the Company and its former officers as defendants also alleges violations of Section 11 of the Securities Exchange Act. Similar suits have been filed against the underwriters of other companies that went public in 1999 and 2000, following reports of governmental investigations of the distribution of shares in certain initial public offerings. The Company believes that the claims alleged in the lawsuits are primarily directed at the underwriters and, as they relate to the Company, are without merit. To the extent that these claims concern practices and disclosures relating to the plan of distribution in the Healtheon initial public offering, the Company believes it will have a claim for indemnification from the underwriters.

In the normal course of business, the Company and its subsidiaries are involved in various claims and legal proceedings. While the ultimate resolution of these matters, including those discussed above and in our 2000 annual report on Form 10-K under the heading Legal Proceedings, has yet to be determined, the Company does not believe that their outcome will have a material adverse effect on our financial position.

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ITEM 2. ***Management s Discussion and Analysis of Financial Condition and Results of Operations***

Overview

WebMD Corporation is a Delaware corporation that was incorporated in December 1995 and commenced operations in January 1996 as Healtheon Corporation. Our common stock has traded on the Nasdaq National Market under the symbol HLTH since February 11, 1999. In November 1999, Healtheon completed mergers with WebMD, Inc., MedE America and Medcast. Following these mergers, Healtheon changed its name to Healtheon/WebMD Corporation. Healtheon/WebMD completed acquisitions of Kinetra and Envoy in January 2000 and May 2000, respectively. On September 12, 2000, Healtheon/WebMD completed mergers with Medical Manager, CareInsite and OnHealth and changed its name to WebMD Corporation.

As a result of the completion of these transactions, our core business encompasses the following products and services:

Transaction services. We offer value-added solutions designed to increase productivity for both providers and payers, to speed healthcare reimbursements and to improve communications among healthcare participants. From simple point-of-service devices to fully integrated transaction processing applications and Internet solutions, we offer a full suite of products and services to automate key business and clinical functions.

Physician services. We develop and market integrated physician practice management systems, including administrative, financial and clinical applications, under The Medical Manager® brand.

Portal services. We offer a variety of services for advertisers, sponsors, consumers, physicians and physician office managers through our online distribution channels and the online and offline distribution channels of our strategic partners.

In the third quarter of 2000, our board of directors approved a restructuring and integration plan, with the objective of eliminating duplication and redundancies as a result of all the acquisitions made by us since November 1999 and consolidating our operational infrastructure into a common platform to more efficiently serve our customers.

As part of our restructuring and integration efforts, we also undertook a review of our existing strategic relationships in light of several criteria, including strategic relevance to both us and our partners, potential conflicts with other agreements as a result of the numerous acquisitions made by us, profitability and impact on future revenue streams. As a result of this process, we have been and are in discussions with several of our partners in an effort to redefine the relationships in a manner that better serves the needs of each party. These discussions have resulted in revisions to some strategic relationships. It is possible that as a result of continuing discussions during the remainder of 2001, additional relationships may be revised or terminated, which may result in additional restructuring charges.

In connection with our restructuring and integration efforts, we recorded restructuring and integration charges of $11.2 million in the three months ended June 30, 2001, and $219.9 million, of which $185.5 million were non-cash charges, in the six months ended June 30, 2001. As we continue our consolidation and integration efforts during the remainder of 2001, we are likely to incur additional costs relating to asset impairments and write-offs, severance, employee retention arrangements related to exit activities, moving and relocations that will be expensed according to the applicable accounting guidelines.

As we announced on September 28, 2000, our board of directors approved management s plan to dispose of Porex, which we acquired in our merger with Medical Manager on September 12, 2000. Porex designs, manufactures and distributes porous and solid plastic components and products used in life sciences, healthcare, industrial and consumer applications. Accordingly, our consolidated statements of operation and consolidated statements of cash flows exclude the results of Porex. We have received competitive bids for Porex as a whole as well as for portions of Porex and are in the process of evaluating these bids.

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Results of Operations

The following discussion includes a comparison of the June 30, 2001 results of operations to the June 30, 2000 results on both an actual and pro forma basis. The effect of all other business combinations was not material to the pro forma information presented below. The pro forma information gives effect to the acquisitions of Kinetra, Envoy, Medical Manager, CareInsite and OnHealth (the 2000 Acquisitions) as if they had occurred at the beginning of each period presented. The information is provided for illustrative purposes only and is not necessarily indicative of the operating results that would have occurred if the transactions had been consummated at the dates indicated, nor is it necessarily indicative of future operating results of the combined company and should not be construed as representative of these amounts for any future periods.

Revenue. Revenue for the three and six months ended June 30, 2001 and 2000 and pro forma revenues for the three and six months ended June 30, 2000 were as follows:

	Three Months Ended June 30,					
	2001		2000		Pro Forma 2000	
	$	%	$	%	$	%
Transaction services	$96,895	54.2%	$54,995	54.4%	$90,198	43.3%
Physician services	65,128	36.4	9,171	9.1	74,632	35.9
Portal services	15,860	8.9	26,752	26.5	29,863	14.4
Other	831	0.5	10,156	10.0	13,355	6.4
Total	$178,714	100.0%	$101,074	100.0%	$208,048	100.0%

	Six Months Ended June 30,					
	2001		2000		Pro Forma 2000	
	$	%	$	%	$	%
Transaction services	$194,413	53.5%	$86,516	51.8%	$180,184	46.0%

Physician services	130,226	35.9	15,953	9.6	137,014	35.0
Portal services	35,771	9.8	48,171	28.9	53,264	13.6
Other	2,795	0.8	16,315	9.8	21,222	5.4
Total	$363,205	100.0%	$166,955	100.0%	$391,684	100.0%

The increase in transaction service revenues for both the three and six months ended June 30, 2001 compared to the prior year periods was primarily attributable to the 2000 Acquisitions. The increase in physician service revenue for both the three and six months ended June 30, 2001 compared to the prior year periods was primarily attributable to the acquisition of Medical Manager in September 2000 offset in part by the elimination of revenue related to the sponsorship of physician subscriptions to our physician portal as a result of the termination of our agreement with DuPont in December 2000 and the new arrangement with Microsoft which was effective as of January 1, 2001. The decrease in portal service revenue for both the three and six months ended June 30, 2001 compared to the prior year periods was primarily attributable to the termination of the agreement with DuPont in December 2000, the new arrangement with News Corporation agreed to in December 2000 and the impact of the softness in the market for internet advertising on us and certain of our carriage partners. The decrease in other revenues for both the three and six months ended June 30, 2001 compared to the prior year periods is primarily attributable to our decision during 2000 to exit our information technology consulting and outsourcing relationships.

The increase in transaction service revenues for both the three and six months ended June 30, 2001 compared to the prior year periods on a pro forma basis was primarily attributable to an increase in the volume of electronic transactions processed. The decrease in physician service revenue for both the three and six months ended June 30, 2001 compared to the prior year periods on a pro forma basis was primarily attributable to the elimination of revenues related to the sponsorship of physician subscriptions to the Company s physician portal as a result of the termination of the agreement with DuPont in December

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2000 and the new arrangement with Microsoft which was effective as of January 1, 2001. The decrease in portal service revenues for both the three and six months ended June 30, 2001 compared to the prior year periods on a pro forma basis was primarily attributable to the termination of the agreement with DuPont in December 2000, the new arrangement with News Corporation agreed to in December 2000 and the impact of the softness in the market for internet advertising on WebMD and certain of our carriage partners. The decrease in other revenues for both the three and six months ended June 30, 2001 compared to the prior year periods on a pro forma basis is primarily attributable to our decision during calendar year 2000 to exit our information technology consulting and outsourcing relationships.

Revenue from related parties consists of revenue for services to Microsoft for the three and six months ended June 30, 2001 and revenues for services to News Corporation for the three months ended March 31, 2001 and revenue for services provided to News Corporation, Microsoft and UnitedHealth Group for the three and six months ended June 30, 2000. Revenue from related parties was $3.0 million for the six months ended June 30, 2001 compared to $10.1 million and $23.0 million for the three and six months ended June 30, 2000, respectively. The decrease was primarily attributable to the new arrangement with Microsoft, which was effective January 1, 2001. Revenue from UnitedHealth Group ceased being considered from a related party in January 2000 when the Chairman and Chief Executive Officer of UnitedHealth Group resigned from our board of directors. Revenue from News Corporation ceased being considered from a related party as of February 15, 2001 when News Corporation surrendered the Company s Series A convertible preferred stock.

Cost of operations. Cost of operations primarily consists of the expenses associated with maintaining our networks and providing products and services. Cost of operations was $119.4 million and $244.7 million for the three and six months ended June 30, 2001, respectively, compared to $78.2 million and $137.6 million for the three and six months ended June 30, 2000, respectively. The increase is primarily attributable to the cost of operations associated with the 2000 Acquisitions.

Cost of operations decreased to $119.4 million and $244.7 million for the three and six months ended June 30, 2001, respectively, compared to $134.8 million and $254.9 million on pro forma basis for the three and six months ended June 30, 2000, respectively. This decrease is primarily related to the decrease in revenue as compared to the pro forma prior periods. Cost of operations represented 66.8% and 67.4% of revenues for the three and six months ended June 30, 2001, respectively, compared to 64.8% and 65.1% of revenues on a pro forma basis for the three and six months ended June 30, 2000, respectively. This increase in cost of operations as a percentage of revenues is primarily due to changes in the mix of product revenues.

Development and engineering. Development and engineering expense consists primarily of salaries paid to engineering personnel, fees paid to outside contractors and consultants, facilities expenses and maintenance of capital equipment used in the development process. Development and engineering expense decreased to $9.1 million and $21.5 million for the three and six months ended June 30, 2001, respectively, compared to $14.7 million and $26.3 million for the three and six months ended June 30, 2000, respectively. This decrease is primarily due to the impact of cost reductions resulting from our restructuring and integration efforts, offset in part by the costs associated with the 2000 Acquisitions.

Development and engineering expense decreased to $9.1 million and $21.5 million for the three and six months ended June 30, 2001, respectively, compared to $29.0 million and $53.8 million on a pro forma basis for the three and six months ended June 30, 2000, respectively. This decrease is a result of the elimination of costs as a result of our restructuring and integration.

Sales, marketing, general and administrative. Sales, marketing, general and administrative expense consists primarily of advertising, product and brand promotion, salaries and related expenses for sales, administrative, finance, legal, human resources and executive personnel. Also included in sales, marketing, general and administrative expense is amortization of non-cash prepaid content, services and distribution and amortization of non-cash deferred stock compensation.

Sales, marketing, general and administrative expense was $113.8 million and $242.4 million for the three and six months ended June 30, 2001, respectively, compared to $124.1 million and $224.7 million for the three months and six months ended June 30, 2000, respectively. Sales, marketing, general and administrative expense excluding non-cash amortization of prepaid content, services, and distribution and non-cash stock compensation was $82.1 million and $172.4 for the three and six months ended June 30, 2001, respectively, and $77.8 million and $158.6 million for the three and six months ended June 30, 2000, respectively. This increase is primarily due to costs associated with the 2000 Acquisitions, which were largely offset by the impact of cost reductions resulting from our restructuring and integration efforts. Amortization of non-cash prepaid content, services and distribution expense was $8.2 million and $16.4 million for the three and six months ended June 30, 2001, respectively, and $20.7 million and $39.3 million for the three and six months ended June 30, 2000, respectively. The decrease from the comparable prior year periods was a result of the restructuring of our strategic relationships with Microsoft and News Corporation. Non-cash stock compensation was $23.4 million and $53.5 million for the three and six months ended June 30, 2001, respectively and $25.6 million and $26.8 million for the three and six months ended June 30, 2000, respectively. The increase for the six months ended June 30, 2001 is primarily a result of the impact of amortization of deferred stock compensation related to stock options issued and assumed in connection with the 2000 Acquisitions.

Sales, marketing, general and administrative expense was $113.8 million and $242.4 million for the three and six months ended June 30, 2001, respectively, compared to $196.7 million and $379.7 million on a pro forma basis for the three and six months ended June 30, 2000, respectively. Sales, marketing, general and administrative expense excluding non-cash amortization of prepaid content, services, and distribution and non-cash stock compensation was $82.1 million and $172.5 million for the three and six months ended June 30, 2001, respectively, and $134.0 million and $269.2 million on a pro forma basis for the three and six months ended June 30, 2000, respectively. This decrease is primarily due to the impact of cost reductions resulting from our restructuring and integration efforts. Amortization of non-cash prepaid content, services and distribution expense was $8.2 million and $16.4 million for the three and six months ended June 30, 2001, respectively, and $20.7 million and $39.3 million on a pro forma basis for the three and six months ended June 30, 2000, respectively. The decrease from the comparable prior year period was a result of the restructuring of our strategic relationships with Microsoft and News Corporation. Non-cash stock compensation was $23.4 million and $53.5 million for the three and six months ended June 30, 2001, respectively and $42.0 million and $71.2 million on a pro forma basis for the three and six months ended June 30, 2000, respectively. The decrease from the comparable prior year period is primarily related to the vesting schedules of stock options issued and assumed in connection with the 2000 Acquisitions.

Depreciation and amortization. Depreciation and amortization expense was $755.1 million and $1,514.9 million for the three and six months ended June 30, 2001, respectively, compared to $416.4 million and $755.1 million for the three and six months ended June 30, 2000, respectively. The increase was attributable to the amortization of intangible assets related to the 2000 Acquisitions, which are being amortized over expected lives of one to five years.

Restructuring and integration charge. In September 2000, our board of directors approved a restructuring plan to consolidate offices and data centers, to reduce marketing and promotional expenses and to substantially eliminate redundancies that were created in the 2000 Acquisitions. During calendar year 2000, the Company s restructuring and integration efforts resulted in the identification and notification of approximately 1,100 employees whose positions with the Company were to be terminated primarily as a result of eliminating duplicate functions within the combined company, the identification of duplicate facilities to be vacated and the restructuring of several strategic relationships including those with News Corporation and DuPont.

During the six months ended June 30, 2001, the Company s restructuring and integration efforts continued. In connection with these efforts, a charge was recorded for the three months ended June 30, 2001 of $11.2 million, which consists of $8.0 million in payments made to customers to exit contractual obligations and $3.2 million of additional integration costs for employee retention arrangements related to exit activities, and a charge was recorded for the six months ended June 30, 2001 of $219.9 million which consists of:

$138.0 million relating to the restructuring of strategic relationships primarily associated with Microsoft, of which $133.5 million represented non-cash charges related to the write-off of intangible assets associated with the Company s original Microsoft agreement recorded as part of the Company s acquisition of WebMD, Inc. in 1999,

personnel-related costs of $63.5 million, of which $52.0 million represented non-cash stock option compensation charges primarily related to the resignation or termination of certain employees pursuant to the applicable employment and separation arrangements, with the remaining personnel-related charge relating to severance and outplacement services for approximately 350 additional employees that the company identified and notified of termination during the three months ended March 31, 2001,

facilities charges of $2.0 million, comprised of future lease obligations and lease cancellation penalties related to vacating additional facilities identified during the three months ended March 31, 2001,

$8.0 million in payments made to customers to exit contractual obligations,

$8.4 million of integration costs, consisting of employee retention arrangements related to exit activities, moving and relocation expenses, as well as outside professional fees related to the integration of our business.

We expect that our restructuring and integration efforts, including the consolidation of our operational infrastructure into a common platform, will result in further cost reductions during 2001.

Liquidity and Capital Resources

As of June 30, 2001, we had approximately $588.2 million in cash, cash equivalents and short-term marketable securities, and working capital of $702.3 million.

In September 2000, our board of directors approved a restructuring and integration plan, with the objective of eliminating duplication and redundancies as a result of all the acquisitions made by us since November 1999 and consolidating our operational infrastructure into a common platform to more efficiently serve our customers. As part of our restructuring and integration efforts, we also undertook a review of our existing strategic relationships in light of several criteria, including strategic relevance to both us and our partners, potential conflicts with other agreements as a result of the numerous acquisitions made by us, profitability, and impact on future revenue streams. As a result of this process, we have been and are in discussions with several of our partners in an effort to redefine the relationships in a manner that better serves the needs of each party. These discussions have resulted in revisions to some strategic relationships. It is possible that, as a result of continuing discussions, additional relationships may be revised or terminated, which may result in additional restructuring charges.

As we announced on September 28, 2000, our board of directors approved management s plan to dispose of Porex, which we acquired in our acquisition of Medical Manager on September 12, 2000. Porex designs, manufactures and distributes porous and solid plastic components and products used in life sciences, healthcare, industrial and consumer applications. The expected net proceeds and the cash flows of Porex until sold were allocated to assets held for sale in the allocation of the Medical Manager purchase price and are included in the line item assets held for sale. Any difference between the actual and expected amounts will result in an adjustment of goodwill unless there is a difference caused by a post-acquisition event.

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Cash used in operating activities was $99.7 million for the six months ended June 30, 2001. The cash used was primarily attributable to net operating losses and payments made related to our restructuring and integration efforts.

Cash provided by investing activities was $98.6 million for the six months ended June 30, 2001 primarily related to $119.0 million of net proceeds from the redemption of marketable securities.

Cash provided by financing activities was $2.2 million for the six months ended June 30, 2001, primarily related to the proceeds from the exercise of stock options.

As of June 30, 2001, we did not have any material commitments for capital expenditures. We had entered into agreements that provided for us to make aggregate guaranteed payments in the following estimated amounts, net of sublease income, under operating and capital leases and our strategic relationships:

Year Ended December 31,	Amount
2001	$ 41.1 million
2002	30.7 million
2003	16.0 million
2004	13.1 million
2005	9.3 million
Thereafter	71.5 million

On March 29, 2001, we announced a stock buy-back program (the Program). Under the Program, we may use up to $50.0 million to purchase shares of our common stock from time to time beginning on April 2, 2001, subject to market conditions. As of June 30, 2001, we have repurchased 513,086 shares at a cost of approximately $2.8 million under the Program.

We believe that we will have sufficient cash resources to meet our presently anticipated working capital and capital expenditure requirements for at least the next 12 months. However, we expect to incur losses before restructuring and integration charges, depreciation, amortization and other non-cash items, until the end of 2001. Our future liquidity and capital requirements will depend upon numerous factors, including the success of the integration of our businesses, our existing and new applications and service offerings, competing technologies and market developments, potential future acquisitions and additional repurchases of our common stock. We may need to raise additional funds to support expansion, develop new or enhanced applications and services, respond to competitive pressures, acquire complimentary businesses or technologies or take advantage of unanticipated opportunities. If required, we may raise such additional funds through public or private debt or equity financing, strategic relationships or other arrangements. There can be no assurance that such financing will be available on acceptable terms, if at all, or that such financing will not be dilutive to our stockholders.

Factors that may affect future results of operations

Our business will suffer if we fail to successfully integrate acquired businesses and technologies

We have in the past acquired, and may in the future acquire, businesses, technologies, services, product lines or content databases. For example, we completed our mergers with WebMD, Inc., MedE America and Medcast in November 1999, our mergers with Kinetra in January 2000 and Envoy in May 2000 and our mergers with Medical Manager, CareInsite and OnHealth in September 2000. In September 2000, our board of directors approved a restructuring and integration plan, with the objective of eliminating duplication and redundancies as a result of the acquisitions made by us since November 1999 and of consolidating our operational infrastructure. We are in the process of integrating and consolidating the operations, products and services, technologies and personnel of these companies. In connection with our restructuring and integration efforts, we recorded restructuring and integration charges of $452.9 million, of which $380.0 million were non-cash charges, in the year ended December 31, 2000 and of $219.9 million, of which $185.5 million were non-cash charges, in the six months ended June 30, 2001. As we continue our consolidation and integration efforts, we are likely to incur additional costs relating to asset

impairments and write-offs, severance, stay bonuses, moving and relocations that will be expensed according to the applicable accounting guidelines. We expect our restructuring and integration efforts will continue during 2001. For additional information regarding our restructuring and integration efforts, see Results of Operations Restructuring and integration charge on page 18 and note 3 to the condensed consolidated financial statements in this quarterly report. The successful integration of the acquired businesses into our operations is critical to our future performance.

The amount and timing of the benefits of our restructuring and integration efforts and the success of the contemplated integration and rationalization of our businesses are subject to significant risks and uncertainties. These risks and uncertainties include, but are not limited to, those relating to

ability to cross-sell products and services to payers and providers with which we have established relationships and those with which the acquired companies have established relationships

the loss of key personnel

diversion of management s attention from other ongoing business concerns

potential conflicts in payer, provider, strategic partner, sponsor or advertising relationships

coordination of organizations that are geographically diverse and have different business cultures

compliance with regulatory requirements.

We cannot guarantee that any acquired businesses will be successfully integrated with our operations in a timely manner, or at all. Failure to successfully integrate acquired businesses or to achieve operating synergies, revenue enhancements or cost savings could have a material adverse effect on our business, financial condition and results of operations.

Integrating any additional acquired organizations and technologies in the future could also be expensive and time consuming and may strain our resources and would be subject to the same challenges, risks and uncertainties as our current integration efforts, as described above.

We are dependent on strategic relationships to generate some of our revenue

Our ability to generate revenue will suffer if we cannot establish and maintain successful strategic relationships. We have entered into strategic relationships with leading online and media distribution and healthcare partners. Successful strategic relationships are an important means to increase the number of transactions processed over our network, generate traffic on our Web site and capitalize on additional distribution and revenue opportunities. As previously announced, we have been renegotiating some of the strategic relationships we currently have in place and some of these relationships have been modified or terminated. It is possible that additional relationships may be modified or terminated. We expect that we will face intensified competition for strategic relationships.

Disputes with strategic partners and customers may be resolved unfavorably to us and may harm our relationships. Some of our strategic partners have initiated or threatened to initiate litigation or other dispute resolution mechanisms regarding alleged breaches of our agreements and other claims. Similarly, in some cases, we have initiated or threatened to initiate litigation or other dispute resolution mechanisms when we believed our partner or customer is in breach of its obligations, if we have been unable to resolve the dispute through negotiations. We cannot provide assurance that these disputes will be resolved in our favor or, even if resolved in our favor, that we will be able to preserve the benefits we expected to achieve from our relationships with those partners, which could adversely affect our financial position and results of operations.

We share revenue with our strategic partners and will incur significant expense in connection with our strategic relationships, and this expense may exceed the net revenue these relationships generate. We have agreed to share some of our revenue with some of our strategic partners and, in some cases, to make guaranteed payments to our strategic partners. We may enter into additional arrangements with current or future strategic partners that require us to share revenue, make guaranteed payments or incur other

significant expenses. We cannot give assurances that we will generate sufficient revenue from our arrangements with strategic partners to offset all required payments and expenses. Failure to do so could have a material adverse effect on our financial condition or results of operations.

We have invested in some of our strategic partners, many of which are in early stages of development. We have made equity investments in some of our strategic partners. In many instances, these investments are in the form of illiquid securities of private companies engaged in e-Health and were made in conjunction with the parties entering into a strategic agreement. Typically, these strategic partners entered into agreements that obligate them to purchase advertising or other services from us. These companies are typically in an early stage of development and may be expected to incur substantial losses and may not generate sufficient revenue to pay the advertising and e-commerce fees due us. In addition, due to recent market volatility, some of these companies have altered their plans to go public, and others that have gone public have experienced or may experience significant decreases in the trading prices of their common stock, adversely affecting the value of our investments. Some of these companies may go out of business before we are able to sell our investments.

We have granted exclusive rights to strategic partners. We have agreed that some of our strategic partners will be our exclusive providers of some of our applications and content. For example, we have entered into strategic agreements with e-commerce companies to be our exclusive partners supplying online pharmacy services and to be our exclusive providers of various categories of content and services. These agreements may limit our access to other applications and content we might otherwise be able to make available to subscribers and consumers or to payer and provider customers. Our inability to offer other applications and content could cause our business to suffer. In addition, we have granted exclusive rights to strategic partners which restrict our ability to pursue some business opportunities. For example, in connection with our acquisition of Envoy from Quintiles Transnational Corp., we granted to Quintiles the exclusive license to use some of the de-identified data available to us by virtue of our transaction services and some exclusive rights in the pharmaceutical market.

Relationships with customers and strategic partners may conflict

We have developed and rely upon important relationships with payers, providers, practice management system vendors and strategic partners, some of which may involve conflicting contractual rights, including conflicts which may result from our acquisitions. As a result of conflicts or perceived conflicts resulting from our acquisitions or our business plans and strategic initiatives, we may lose relationships with, or be subject to litigation by, some other customers and strategic partners, who may then establish relationships with our competitors. For example, we are currently in the process of negotiating new arrangements with Medic, a practice management system vendor whose products compete with The Medical Manager products, that would replace prior arrangements and better serve the needs of each party. However, we cannot provide assurance that these negotiations will be successful. If these negotiations are not successful, there could be litigation or other proceedings that arise out of the relationship or its termination. Some of our other customers and strategic partners have initiated or threatened to initiate litigation or other dispute resolution mechanisms to enforce rights they purport to have as a result of conflicts with our other relationships or with our business plans or strategic initiatives, or their belief that these conflicts exist. We cannot provide assurance that these disputes will be resolved in our favor or, even if resolved in our favor, that we will be able to preserve the benefits we expected to receive from our relationships with those partners. In addition, we may not be able to maintain or establish relationships with key participants in the healthcare and Internet industries if any of the companies we acquired had already established relationships with competitors of these key participants.

If contractual or relationship conflicts or other issues cannot be resolved, we could lose the benefits of some of our relationships with payers, providers or strategic partners. Losses of any significant relationships could harm our business or results of operations.

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Our ability to generate revenue could suffer if we do not offer new applications and services

Healthcare information exchange and transaction processing is a relatively new and evolving market. The pace of change in our markets is rapid and there are frequent new product introductions and evolving industry standards. We may be unsuccessful in responding to technological developments and changing customer needs. In addition, our applications and services offerings may become obsolete due to the adoption of new technologies or standards.

We currently offer a limited number of applications on our Internet-based platform and some of our service offerings, including our handheld solution, are not fully developed or launched. We must introduce new applications and services and improve the functionality of our existing services in a timely manner in order to attract and retain customers.

We rely on a combination of internal development, strategic relationships, licensing and acquisitions to develop these applications and services. Each of our applications, regardless of how it was developed, must be integrated and customized to operate with the existing legacy computer systems of payer and provider customers and our platform. We are currently in the process of integrating acquired applications and products and services. Developing, integrating and customizing these applications and services will be time consuming, and these applications and services may never achieve market acceptance, which could also cause our business to suffer.

New or newly integrated products and services will not become profitable unless they achieve sufficient levels of physician penetration and market acceptance

There can be no assurance that physicians will accept new or newly integrated products and services from us, including the products and services we are developing to integrate our transaction services and portal services into their office workflow, such as our handheld solution. Even physicians who are already our customers may not purchase new or newly integrated products or services, especially when they are initially offered. Physicians using our existing products and services may refuse to adopt new or newly integrated products and services when they have made extensive investments in hardware, software and training relating to those existing products and services. Similarly, other healthcare participants may not accept new or newly integrated products and services from us developed for their use. In addition, there can be no assurance that any pricing strategy that we implement for any such products and services will be economically viable or acceptable to the target markets. Failure to achieve broad penetration in target markets with respect to new or newly integrated products and services could have a material adverse effect on our business prospects.

Achieving market acceptance for new or newly integrated products and services is likely to require substantial marketing efforts and expenditure of significant funds to create awareness and demand by participants in the healthcare industry. In addition, deployment of new or newly integrated products may require the use of additional resources for training our existing sales force and customer service personnel and for hiring and training additional salespersons and customer service personnel. There can be no assurance that the revenue opportunities from new or newly integrated products and services will justify amounts spent for their development, marketing and roll-out.

Our business model for providing Internet-based services is unproven, and we may not achieve profits from this business

Our business model for providing Internet-based services is evolving, and our revenue and profit potential from these services is unproven. We intend to:

- offer provider and payer customers our Internet-based transaction services, to the extent that is appropriate to their needs

- integrate these transaction services with our Medical Manager practice management systems and similar systems provided by others build usage of our portal services by consumers, physicians and physician officer managers

generate e-commerce revenue from the sale of healthcare products or services of our strategic partners and other suppliers over the Internet.

However, the provision of services over the Internet to the healthcare industry is a developing business that is inherently riskier than businesses in industries where companies have established operating histories and there can be no assurance that our initiatives in this area will be profitable.

We may not be able to generate significant advertising revenue from our portal services

We derive a portion of our revenue from advertising on our Web site and other Web sites that license our content. Advertising revenue is generally derived from short-term advertising contracts in which we typically guarantee a minimum number of impressions or pages to be delivered over a specified period of time for a fixed fee. Advertising revenue may also include barter transactions, which are exchanges by us of advertising space on our Web site for goods and services from strategic partners and which might not generate any cash receipts.

The Internet advertising market is new and rapidly evolving, and no standards have been widely accepted to measure its effectiveness as compared to traditional media advertising. If no standards develop, existing advertisers may not continue their current level of Internet advertising, and advertisers that have traditionally relied on other advertising media may be reluctant to advertise on the Internet. Moreover, filter software programs that limit or prevent advertising from being delivered to a Web user s computer are available. Widespread adoption of this software could adversely affect the commercial viability of Internet advertising. Demand for Internet advertising in general has, during the first half of 2001, been weaker than in recent periods and there can be no assurance that such demand will return to the levels seen previously. Our business would be adversely affected if the market for Internet advertising fails to develop or develops more slowly than expected.

Various pricing models are used to sell advertising on the Internet. It is difficult to predict which, if any, will emerge as the industry standard, thereby making it difficult to project our future advertising rates and revenue. The level of traffic on our Web site and other Web sites that license our content is likely to be a factor in determining advertising rates.

Lengthy sales and implementation cycles for our applications could adversely affect our ability to generate revenue

A key element of our strategy is to market our solutions directly to large healthcare organizations. We will be unable to control many of the factors that will influence the buying decisions of these organizations. We expect that the sales and implementation processes will be lengthy and will involve a significant technical evaluation and commitment of capital and other resources by our customers. The sale and implementation of our solutions are subject to delays due to our payer and provider customers internal budgets and procedures for approving large capital expenditures and deploying new technologies within their networks.

Failure to continue to expand and adapt our platform to accommodate increased usage could make it difficult to successfully implement our Internet-based services

To successfully implement our Internet-based services, we must continue to expand and adapt our platform and transaction networks to accommodate additional users, increased transaction volumes and changing customer requirements. Our infrastructure may not accommodate increased use while maintaining acceptable overall performance. To date, we have processed a limited number and variety of Internet-based transactions. In addition, our Internet-based products and services have only been used by a limited number of physicians and healthcare consumers. An unexpectedly large increase in the volume of traffic on our Web site or transactions processed over our networks may require us to expand and further

upgrade our platform. This expansion could be expensive and could divert our attention from other activities.

Performance problems with our systems could damage our business

Our payer and provider customer satisfaction and our business could be harmed if we or our customers experience system delays, failures or loss of data. We currently process our payer and provider transactions and data at our facilities and rely on a data center operated by a third party to perform EDI transaction processing, other than real-time EDI transaction processing. This data center is located in Tampa, Florida and is operated by Verizon Data Services, with whom we have contracted for these processing services. We rely primarily on this facility to process batch claims and other batch medical EDI transaction sets. Our contract with Verizon requires Verizon to maintain processing capability and a hot site disaster recovery system. We have a contingency plan for emergencies with our systems; however, we have limited backup facilities to process information if these facilities are not functioning. The occurrence of a major catastrophic event or other system failure at any of our facilities or at the Verizon facility could interrupt data processing or result in the loss of stored data, which could have an adverse impact on our business.

If our systems or the Internet experience security breaches or are otherwise perceived to be insecure, our business could suffer

A material security breach could damage our reputation or result in liability. We retain confidential information, including patient health information, in our processing centers. It is critical that these facilities and infrastructure remain secure and be perceived by the marketplace as secure. We may be required to expend significant capital and other resources to protect against security breaches or to alleviate problems caused by breaches. Despite the implementation of security measures, this infrastructure may be vulnerable to physical break-ins, computer viruses, programming errors, attacks by third parties or similar disruptive problems. In addition, any well-publicized compromise of Internet security, whether or not related to our own operations, could damage our Internet-based businesses.

Performance problems with the systems of our service and content providers could disrupt our Web site

We depend on service and content providers to provide information and data feeds on a timely basis. Our Web site could experience disruptions or interruptions in service due to the failure or delay in the transmission or receipt of this information.

Our Internet-based services are dependent on the development and maintenance of the Internet infrastructure and the adoption of broadband connections by physician offices

Our ability to deliver our Internet-based services is dependent on the development and maintenance of the infrastructure of the Internet by third parties. This includes maintenance of a reliable network backbone with the necessary speed, data capacity and security, as well as timely development of complimentary products such as high-speed modems, for providing reliable Internet access and services. The Internet has experienced, and is likely to continue to experience, significant growth in the number of users and the amount of traffic. If the Internet continues to experience increased numbers of users, increased frequency of use or more complex requirements, the Internet infrastructure may be unable to support the demands placed on it. In addition, the performance of the Internet may be harmed by increased users or more complex requirements.

The Internet has experienced a variety of outages and other delays as a result of damages to portions of its infrastructure, and it could face outages and delays in the future. These outages and delays could reduce the level of Internet usage as well as the availability of the Internet to us for delivery of our Internet-based services. In addition, the Internet could lose its viability due to delays in the development or adoption of new standards and protocols to handle increased levels of activity or due to increased governmental regulation. The infrastructure and complimentary products or services necessary to make the

Internet a viable commercial marketplace for the long-term may not be developed successfully or in a timely manner. Our financial condition could be materially harmed if the Internet is not available to us for the delivery of our services and products.

In addition, our customers who utilize our Web-based services depend on Internet service providers, online service providers and other Web site operators for access to our Web site. All of these providers have experienced significant outages in the past and could experience outages, delays and other difficulties in the future due to system failures unrelated to our systems. Any significant interruptions in our services or increases in response time could result in a loss of potential or existing users of and advertisers and sponsors on our Web site and, if sustained or repeated, could reduce the attractiveness of our services.

Some of our services require a continuous broadband connection between the physician s office and our data center and/or the Internet. The availability of broadband connectivity varies widely from location to location and even within a single geographic area, due to factors such as the distance of a site from the central switching office. The future availability of broadband connections is unpredictable and is not within our control. While we expect that many physician office locations will remain without ready access to broadband connectivity for some period of time, we cannot predict how long that will be. Accordingly, the lack of these broadband connections will continue to place limitations on the number of sites that are able to utilize our Internet-based services and the revenue we can expect to generate from those services.

Our Internet platform infrastructure and scalability are not proven, and we may not be able to adequately accommodate increased functionality or usage

To date, we have processed a limited number and variety of Internet transactions over our platforms. Similarly, a limited number of healthcare participants use these Internet platforms. Our systems may not accommodate increased use while maintaining acceptable overall performance. We must continue to expand and adapt our network infrastructure to accommodate additional users, increased transaction volumes and changing payer and provider customer requirements.

Our business could be adversely affected if we cannot attract and retain key personnel

Our future operating results substantially depend on the ability of our officers and key employees to manage changing business conditions and to implement and improve our technical, administrative, financial control and reporting systems. We need to attract, integrate, motivate and retain highly skilled technical people. In particular, we need to attract and retain experienced computer, engineering, marketing, management and other professionals capable of developing, selling and installing complex healthcare information systems. We face intense competition for these people.

We face significant competition for our products and services

The markets in which we operate are intensely competitive, continually evolving and subject to rapid technological change. We have many competitors, including:

- healthcare information system vendors, including physician practice management system vendors
- transaction processing companies, including those providing EDI and/or Internet-based services and those providing services through other means, such as paper and fax
- large information technology consulting service providers
- online services, portals or Web sites targeted to the healthcare industry, healthcare consumers and/or physicians generally
- consortiums of health insurance companies and of pharmacy benefit managers that have announced that they are developing Web-based transaction services for use by their members and other potential customers

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- publishers and distributors of traditional offline media, including those targeted to healthcare professionals, many of which have established or may establish Web sites
- general purpose consumer online services and portals and other high-traffic Web sites which provide access to healthcare-related content and services
- public sector and non-profit Web sites that provide healthcare information without advertising or commercial sponsorships
- vendors of healthcare information, products and services distributed through other means, including direct sales, mail and fax messaging.

We also compete, in some cases, with alliances formed by the above competitors, including alliances that are intended to allow the participants to pursue a strategy similar to our strategy of integrating transaction processing capabilities and portal services with physician practice management systems. Major software and information systems companies, both with and without healthcare companies as their partners, offer or have announced their intention to offer products or services that are competitive with some of our solutions, including wireless handheld solutions that will compete with ULTIA, our handheld solution. In addition, some of our existing payer and provider customers and some of our strategic partners may also compete with us or plan to do so or belong to alliances that compete with us or plan to do so. For example, some payers currently offer electronic data transmission services to healthcare providers that establish a direct link between the provider and payer, bypassing third party EDI service providers. Any significant increase in the utilization of direct links between healthcare providers and payers could have a material adverse effect on our business and results of operations.

Many of our competitors have greater financial, technical, product development, marketing and other resources than we do. These organizations may be better known than we are and have more customers than we do. We cannot provide assurance that we will be able to compete successfully against these organizations or any alliances they have formed or may form.

Our business may be subject to litigation

Our business and operations may subject us to claims, litigation and other proceedings brought by private parties and governmental authorities. For information regarding certain proceedings to which we are currently a party, see Legal Proceedings on page 35 and the information under Legal Proceedings in our 2000 annual report on Form 10-K.

Healthcare regulation could adversely affect our business

The healthcare industry is highly regulated and is subject to changing political, regulatory and other influences. These factors affect the purchasing practices and operation of healthcare organizations. Federal and state legislatures and agencies periodically consider programs to reform or revise the U.S. healthcare system. These programs may contain proposals to increase governmental involvement in healthcare, lower reimbursement rates or otherwise change the environment in which healthcare industry participants operate. Healthcare industry participants may respond by reducing their investments or postponing investment decisions, including investments in our applications and services. We are unable to predict future proposals with any certainty or to predict the effect they would have on our business.

Existing laws and regulations also could create liability, cause us to incur additional cost and restrict our operations. Many healthcare laws are complex, applied broadly and subject to interpretation by courts and other governmental authorities. In addition, many existing healthcare laws and regulations, when enacted, did not anticipate the methods of healthcare e-commence and other products and services that we provide. However, these laws and regulations may nonetheless be applied to our products and services. Our failure, or the failure of our business partners, to accurately anticipate the application of these healthcare laws, or other failure to comply, could create liability for us, result in adverse publicity and negatively affect our business.

HIPAA administrative simplification. Under the Health Insurance Portability and Accountability Act of 1996, or HIPAA, Congress mandated a package of interlocking administrative simplification rules to establish standards and requirements for the electronic transmission of certain health information. Five of these rules were published in proposed form in 1998, with two of the five recently published in final form. The two rules published in final form are Standards for Electronic Transactions, published August 17, 2000, and Standards for Privacy of Individually Identifiable Health Information, published December 28, 2000. These rules took effect on October 16, 2000 and April 14, 2001, respectively, with compliance required by healthcare providers, healthcare clearinghouses and large health plans two years following the respective effective dates. Small health plans are given an additional year to comply. These rules apply to certain of our operations as well as the operations of many of our customers. Compliance with these final rules will be costly and could require complex changes in our systems.

HIPAA transaction standards. The HIPAA Standards for Electronic Transactions rule is commonly referred to as the transaction standards rule. This rule establishes format standards for eight of the most common healthcare transactions, using technical standards promulgated by recognized standards publishing organizations. These transactions include health claims, enrollment, payment and eligibility. Under the new standards, any party transmitting or receiving any of these eight healthcare transactions electronically will send and receive data in a single format, rather than the large number of different data formats currently used.

The transaction standards are applicable to that portion of our business involving the processing of healthcare transactions among physicians, payers, patients and other healthcare industry participants. The transaction standards also are applicable to many of our customers and to our relationships with those customers. We intend to comply with the transaction standards by their compliance date. This compliance may require costly modifications to some of our systems, products and services. We believe that we are well-positioned to effectuate these changes and to facilitate compliance efforts of our customers and strategic partners. However, there can be no assurance that we or our customers or strategic partners will be able to do so or that we will be able to take advantage of any business opportunities that implementation of the transaction standards may provide to us.

Other regulation of transaction services. Other state and federal statutes and regulations governing transmission of healthcare information may affect our operations. For example, Medicaid rules require some processing services and eligibility verification to be maintained as separate and distinct operations. We carefully review our practices with regulatory experts in an effort to ensure that we are in compliance with all applicable state and federal laws. These laws, though, are complex and changing, and the courts and other governmental authorities may take positions that are inconsistent with our practices.

HIPAA privacy standards. The HIPAA Standards for Privacy of Individually Identifiable Health Information rule is commonly referred to as the privacy standards rule. This rule establishes a set of basic national privacy standards and fair information practices for the protection by health plans, healthcare clearinghouses, healthcare providers and their business associates of individually identifiable health information. Due to a technical error in the delivery of the privacy standards rule to Congress, the effective date was delayed until April 14, 2001, which also extends the compliance date for most entities to April 14, 2003. Also, on February 28, 2001, the final privacy standards rule was converted to a final rule with request for comments to permit public comment for a limited period before the rule becomes effective. This comment period did not further delay the effective date of the privacy standards rule. However, U.S. Department of Health and Human Services Secretary Thompson has stated publicly that his department intends to make or propose further changes to that rule in the near future. The privacy standards rule applies to the portions of our business that process healthcare transactions and provide technical services to other participants in the healthcare industry. This rule provides for civil and criminal liability for its breach and requires us, our customers and our partners to use health information in a highly restricted manner, to establish policies and procedures to safeguard the information, to obtain individual consents in some cases, and to provide certain access rights to individuals. This rule may require us to incur significant costs to change our platform and services, may restrict the manner in which we transmit and use the information, and may adversely affect our ability to generate revenue from the provision of de-

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identified information to third parties. We are unable to predict what changes to the privacy standards rule will be made in the future or how those changes could affect our business.

Other restrictions regarding confidentiality and privacy of patient information. Numerous state and federal laws other than HIPAA govern the collection, dissemination, use, access to and confidentiality of patient health information. Many states are considering new laws and regulations that further protect the confidentiality of medical records or medical information. These state laws are not in all cases preempted by the HIPAA privacy standard and may be subject to interpretation by various courts and other governmental authorities, thus creating potentially complex compliance issues for us and our customers and strategic partners. The definitions in the various state and federal laws concerning what constitutes individually identifiable data sometimes differs and sometimes is not provided, creating further complexity. In addition, determining whether data has been sufficiently de-identified may require complex factual and statistical analyses. The HIPAA privacy standards rule contains a restrictive definition of de-identified information, which is information that is not individually identifiable, that could create a new standard of care for the industry. These other privacy laws at a state or federal level, or new interpretations of these laws, could create liability for us, could impose additional operational requirements on our business, could affect the manner in which we use and transmit patient information and could increase our cost of doing business. In addition, parties may also have contractual rights that provide additional limits on our collection, dissemination, use, access to and confidentiality of patient health information. Claims of privacy right or contractual breaches, even if we are not found liable, could be expensive and time-consuming to defend and could result in adverse publicity that could harm our business.

International data regulation. Other countries also have, or are developing, their own laws governing the collection, use, storage and dissemination of personal information or patient data. These laws could create liability for our international operations, impose additional operations requirements or restrictions on our business, affect the manner in which we use or transmit data and increase our cost of doing business.

Consumer protection regulation. The Federal Trade Commission, or FTC, and many state attorneys general are applying federal and state consumer protection laws to require that the online collection, use and dissemination of data, and the presentation of Web site content, comply with certain standards for notice, choice, security and access. Courts may also adopt these developing standards. In many cases, the specific limitations regarding these standards are subject to interpretation by courts and other governmental authorities. We believe that we are in compliance with these consumer protection standards, but a determination by a state or federal agency or court that any of our practices do not meet these standards could result in liability and adversely affect our business. New interpretations of these standards could also require us to incur additional costs and restrict our business operations.

Regulation of healthcare relationships. There are federal and state laws that govern patient referrals, physician financial relationships and inducements to beneficiaries of federal healthcare programs. The federal anti-kickback law prohibits any person or entity from offering, paying, soliciting or receiving anything of value, directly or indirectly, for the referral of patients covered by Medicare, Medicaid and other federal healthcare programs or the leasing, purchasing, ordering or arranging for or recommending the lease, purchase or order of any item, good, facility or service covered by these programs. The anti-kickback law is broad and may apply to some of our activities or our relationships with our customers, advertisers or strategic partners. Penalties for violating the anti-kickback law include imprisonment, fines and exclusion from participating, directly or indirectly, in Medicare, Medicaid and other federal healthcare programs. Many states also have similar anti-kickback laws that are not necessarily limited to items or services for which payment is made by a federal healthcare program. We carefully review our practices with regulatory experts in an effort to ensure that we comply with all applicable laws. However, the laws in this area are both broad and vague and it is often difficult or impossible to determine precisely how the laws will be applied, particularly to new services similar to ours. Any determination by a state or federal regulatory agency that any of our practices violate any of these laws could subject us to civil or criminal penalties and require us to change or terminate some portions of our business.

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We currently provide billing services and intend to provide repricing services to providers and, therefore, may be subject to state and federal laws that govern the submission of claims for medical expense reimbursement. These laws generally prohibit an individual or entity from knowingly presenting or causing to be presented a claim for payment from Medicare, Medicaid or other third party payers that is false or fraudulent, or is for an item or service that was not provided as claimed. These laws also provide civil and criminal penalties for noncompliance. We have designed our current transaction services and will design any future services to place the responsibility for compliance with these laws on provider customers. However, we cannot guarantee that state and federal agencies will regard billing errors processed by us as inadvertent and not in violation of these laws. In addition, changes in current healthcare financing and reimbursement systems could cause us to make unplanned modifications of applications or services, or result in delays or cancellations of orders or in the revocation of endorsement of our applications and services by healthcare participants.

Regulation by the U.S. Food and Drug Administration. The Food and Drug Administration, or the FDA, has jurisdiction under the 1976 Medical Device Amendments to the Federal Food, Drug and Cosmetic Act, or the FDA Act, to regulate computer products and software as medical devices if they are intended for use in the diagnosis, cure, mitigation, treatment or prevention of disease in humans. The FDA has issued a final rule under which manufacturers of medical image storage devices and related software are required to submit to the FDA premarket notification applications, which are each referred to in this document as a 510(k) application, and otherwise comply with the requirements of the FDA Act applicable to medical devices. We have attempted to design our services so that our computer applications and software are not considered to be medical devices. However, the FDA may take the position that our services are subject to FDA regulation. In addition, we may expand our services in the future to areas that subject us to FDA regulation. For example, Medical Manager Health Systems is distributing in the U.S. a medical image management device, referred to herein as the image device, which was granted clearance by the FDA on August 25, 2000, and is manufactured by Medical Manager Health Systems in accordance with specifications set forth in the cleared 510(k) application. Medical Manager Health Systems has created an interface between The Medical Manager practice management system and the image device and is marketing the interface and the image device as the DIMDX System. We believe that the addition of our practice management system to the image device does not change the image device s intended use or significantly change the safety or efficacy of the product to the extent that a new 510(k) application is required. The FDA is currently reviewing its policy for the regulation of computer software, and there is a risk that The Medical Manager software or other of our software or hardware components could in the future become subject to some or all of the above requirements. Except with respect to Medical Manager Health Systems and Porex, we have no experience in complying with FDA regulations. We believe that complying with FDA regulations may be time consuming, burdensome and expensive and could delay our introduction of new applications or services.

The FDA also regulates pharmaceuticals, including the regulation of pharmaceutical advertisements or descriptions posted on a Web site or delivered electronically to physicians or consumers. Many of our advertisers are pharmaceutical companies and the content of their ads is subject to FDA scrutiny and regulation. We have attempted to disclaim responsibility for the content of these ads and to keep the FDA compliance burden squarely on our advertisers. We cannot guarantee that the FDA will not hold us also responsible in some way for this compliance, which could adversely affect or restrict our relationships with our advertisers.

Medical professional regulation. The practice of most healthcare professions requires licensing under applicable state law. In addition, the laws in some states prohibit business entities from practicing medicine, which is referred to as the prohibition against the corporate practice of medicine. We do not believe we engage in the practice of medicine and we have attempted to structure our Web site, strategic relationships and other operations to avoid violating these state licensing and professional practice laws. A state, however, may determine that some portion of our business violates these laws and may seek to have us discontinue those portions or subject us to penalties or licensure requirements. We provide Web site capabilities for our physician customers. Many states regulate the ability of medical professionals to

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advertise or maintain referral services. We do not represent that a physician s use of our Web site will comply with these or other state laws regulating professional practice and we do not monitor or control the content that physicians post on their individual practice Web sites using our Web site application. It is possible a state or a court may determine we are responsible for any non-compliance with these laws, which could affect our ability to offer this service to our customers. We employ and contract with physicians who provide only medical information to consumers, and we have no intention to provide medical care or advice. We do not maintain professional liability insurance because we believe we are not a healthcare provider. Any determination that we are a healthcare provider and acted improperly as a healthcare provider may result in liability for which we are not insured.

Regulation of the Internet could adversely affect our business

The Internet and its associated technologies are subject to government regulation. Our failure, or the failure of our business partners, to accurately anticipate the application of applicable laws and regulations, or any other failure to comply, could create liability for us, result in adverse publicity, or negatively affect our business. In addition, new laws and regulations, or new interpretations of existing laws and regulations, may be adopted with respect to the Internet or other online services covering user privacy, patient confidentiality, consumer protection and other issues, including pricing, content, copyrights and patents, distribution, and characteristics and quality of products and services. We cannot predict whether laws or regulations will change or how such changes will affect our business. Government regulation of the Internet could limit the effectiveness of the Internet for the methods of healthcare e-commerce that we are providing or developing or even prohibit the sale of particular products and services.

For more information regarding government regulation of the Internet to which we are or may be subject, see Healthcare regulation could adversely affect our business beginning on page 27.

We face potential liability related to the privacy and security of personal information we collect on our Web sites

Internet user privacy has become a controversial issue both in the U.S. and abroad. We have privacy policies posted on our consumer portal and our professional portal that we believe comply with applicable laws requiring notice to users about our information collection, use and disclosure practices. However, whether and how existing privacy and consumer protection laws in various jurisdictions apply to the Internet still is uncertain and may take years to resolve. Any legislation or regulation in the area of privacy of personal information could affect the way we operate our Web sites and could harm our business. Further, we can give no assurance that the statements on our portals, or our practices, will be found sufficient to protect us from liability or adverse publicity in this area.

For more information regarding regulation of the collection, use and disclosure of personal information to which we may be subject, see Healthcare regulation could adversely affect our business beginning on page 27.

Third parties may challenge the enforceability of our online agreements

The law governing the validity and enforceability of online agreements and other electronic transactions is evolving. We could be subject to claims by third parties that our online agreements with consumers and physicians that provide the terms and conditions for use of our portal services and physician services are unenforceable. A finding by a court that these agreements are invalid could harm our business and require costly changes to our portals.

Third parties may bring claims as a result of the activities of our strategic partners

We could be subject to claims by third parties, and to liability, as a result of the activities, products or services of our strategic partners. We state on our portals that we do not control or endorse the products or services of our strategic partners. However, there can be no assurance that the statements made in our portal will be found to be sufficient to ensure that we are not held responsible for such activities, products

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or services. Furthermore, even if these claims do not result in liability to us, investigating and defending these claims could be expensive, time-consuming and result in adverse publicity that could harm our business.

Third parties may bring claims against us as a result of content provided on our Web site, which may be expensive and time consuming to defend

We could be subject to third party claims based on the nature and content of information supplied on our Web site by us or third parties, including content providers, medical advisors or users. We could also be subject to liability for content that may be accessible through our Web site or third party Web sites linked from our Web site or through content and information that may be posted by users in chat rooms, bulletin boards or on Web sites created by professionals using our Web site application. Even if these claims do not result in liability to us, investigating and defending against these claims could be expensive and time consuming and could divert management s attention away from operating the business.

Our intellectual property may be subject to infringement claims or may be infringed upon

Our intellectual property is important to our business. We could be subject to intellectual property infringement claims as the number of our competitors grows and the functionality of our applications overlaps with competitive offerings. These claims, even if not meritorious, could be expensive and divert management s attention from our operations. If we become liable to third parties for infringing their intellectual property rights, we could be required to pay a substantial damage award and to develop noninfringing technology, obtain a license or cease selling the applications that contain the infringing intellectual property. We may be unable to develop noninfringing technology or obtain a license on commercially reasonable terms, or at all. In addition, we may not be able to protect against misappropriation of our intellectual property. Third parties may infringe upon our intellectual property rights. If we do not detect any unauthorized use, we may be unable to enforce our rights.

The proposed disposition of our plastics and filtration technologies business may not be completed in the manner expected or at all

If our proposed disposition of Porex fails to be completed, is not completed in a timely manner or does not provide us with the proceeds anticipated, we may not be able to execute strategies that are important to our business. We cannot guarantee that the disposition of Porex will be successfully completed in the manner planned, or at all. Failure to successfully complete this proposed disposition as anticipated or to complete it in a timely manner could have a material adverse effect on our business, financial condition and results of operations.

Until we dispose of our plastics and filtration technologies business, we will be subject to risks associated with that business

Until the proposed disposition of our plastic and filtration technologies business is completed, we will continue to operate that business and to be subject to additional risks associated with that business, which include:

We face significant competition for the products and services of our plastic and filtration technologies business. Competition in our plastics and filtration technology business is characterized by the introduction of competitive products at lower prices. We believe that Porex s principal competitive strengths are its manufacturing processes, quality control, relationships with its customers and distribution of its proprietary healthcare products.

In the porous plastics area, Porex s competitors include other producers of porous plastic materials as well as companies that manufacture and sell products made from materials other than porous plastics which can be used for the same purposes as Porex s products. In this area, Porex has several direct competitors in the U.S., Europe and Asia. Porex s porous plastic pen nibs compete with felt and fiber tips manufactured by a variety of suppliers worldwide. Other Porex industrial products made of porous plastic

compete, depending on the industrial application, with porous metals, metal screens, fiberglass tubes, pleated paper, resin-impregnated felt, ceramics and other substances and devices.

The market for Porex s injection molded solid plastic components and products, including its medical products, is highly competitive and highly fragmented. Porex s pipette tips and racks also compete with similar products manufactured by domestic and foreign manufacturers. Porex s injection molding and mold making services compete with services offered by several foreign and domestic companies. The MEDPOR® Biomaterial products compete for surgical use against autogenous and allograph materials and alloplastic biomaterials. Porex s surgical drains and markers compete against a variety of products from several manufacturers.

Healthcare regulation could adversely affect our plastics and filtration technologies business. Porex manufactures and distributes medical/ surgical devices, such as plastic and reconstructive surgical implants and tissue expanders, which are subject to government regulations, under the FDA Act and additional regulations promulgated by the FDA. Future healthcare products may also be subject to these regulations and approval processes. Compliance with these regulations and the process of obtaining approvals can be costly, complicated and time-consuming, and we cannot assure you that these approvals will be granted on a timely basis, if ever.

The nature of Porex s products exposes it to product liability claims and may make it difficult to get adequate insurance coverage. The products sold by Porex expose it to potential risk for product liability claims, particularly with respect to Porex s life sciences, clinical, surgical and medical products. We believe that Porex carries adequate insurance coverage against product liability claims and other risks. We cannot assure you, however, that claims in excess of Porex s insurance coverage will not arise. In addition, Porex s insurance policies must be renewed annually. Although Porex has been able to obtain adequate insurance coverage at an acceptable cost in the past and believes that it is adequately indemnified for products manufactured by others and distributed by it, we cannot assure you that in the future Porex will be able to obtain this insurance at an acceptable cost or be adequately protected by this indemnification.

Since March 1991, Porex has been named as one of many co-defendants in a number of actions brought by recipients of silicone gel mammary implants. For more information regarding these actions, see the information under Legal Proceedings in our 2000 annual report on Form 10-K.

Our stock price has been volatile in the past and may continue to be volatile

The market price of our common stock has fluctuated since the date of our initial public offering and is likely to fluctuate in the future. Changes in the market price of our common stock may result from, among other things, quarter-to-quarter variations in operating results, operating results being less than analysts estimates, changes in analysts earnings estimates, announcements of new technologies, products and services or pricing policies by us or our competitors, announcements of acquisitions or strategic relationships by us or our competitors, developments in existing customer or strategic relationships, actual or perceived changes in our business strategy, developments in pending litigation and claims, sales of large amounts of our common stock, changes in market conditions in the

Internet and healthcare industries, changes in prospects for healthcare reform, changes in general economic conditions, and fluctuations in the securities markets in general.

In addition, the market prices of Internet and healthcare information technology stocks in general, and of our common stock in particular, have experienced large fluctuations, sometimes quite rapidly. These fluctuations often may be unrelated or disproportionate to the operating performance of these companies.

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Sales of large amounts of our shares and the lapse of transfer restrictions could adversely affect prevailing stock prices

Sales of substantial amounts of our common stock in the public market, or the perception that these sales may occur, could materially and adversely affect the prevailing market prices for our common stock and make it more difficult for us to raise capital through the sale of equity or equity-related securities in the future. Substantial amounts of our outstanding common stock will become freely transferable from time to time until the second quarter of 2002, as contractual restrictions on transfer lapse. Additional amounts of our common stock will also become available for sale, from time to time, as holding periods under applicable securities regulations are met.

ITEM 3. ***Quantitative and Qualitative Disclosures About Market Risk***

Interest Rate Sensitivity

The primary objective of our investment activities is to preserve principal and maintain adequate liquidity, while at the same time maximizing the yield we receive from our investment portfolio. This objective is accomplished by adherence to our investment policy, which establishes the list of eligible securities and credit requirements for each investment.

Changes in prevailing interest rates will cause the principal amount of the investment to fluctuate. To minimize this risk, we maintain our portfolio of cash equivalents, short-term investments and marketable securities in commercial paper, non-government debt securities, money market funds and highly liquid U.S. Treasury notes. We view these high grade securities within our portfolio as having similar market risk characteristics. Principal amounts for short-term investments and marketable securities expected to mature are $94.8 million during 2002.

We have not utilized derivative financial instruments in our investment portfolio.

Exchange Rate Sensitivity

Currently, the majority of our sales and expenses are denominated in U.S. dollars and, as a result, we have experienced no significant foreign exchange gains and losses to date. We conduct only limited transactions in foreign currencies, and we do not anticipate that foreign exchange gains or losses will be significant in the foreseeable future. We have not engaged in foreign currency hedging activities to date.

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PART II

OTHER INFORMATION

ITEM 1. *Legal Proceedings*

Quintiles v. WebMD

As part of the transaction in which WebMD acquired Envoy from Quintiles, Quintiles and WebMD entered into a Data Rights Agreement in May 2000. Under the Data Rights Agreement, Quintiles retained the right to continue to receive in perpetuity deidentified healthcare claims data, to the extent not prohibited by customer contracts or any applicable law. Quintiles uses this data to provide market research and related products and services to third parties. In the transaction documentation, Quintiles represented to WebMD that its data practices complied with all applicable laws and material customer contracts and agreed to indemnify WebMD for any losses that result from a breach of such representations.

On February 23, 2001, WebMD provided notice to Quintiles that WebMD s subsidiary Envoy, which provides electronic transaction services for the healthcare industry, would be temporarily suspending the provision of data under the Data Rights Agreement between the parties.

On February 25, 2001, Quintiles filed an action for breach of contract seeking temporary and permanent injunctive relief and unspecified damages, and obtained an *ex parte* Temporary Restraining Order from the Superior Court of Wake County, North Carolina, requiring WebMD to continue to provide data to Quintiles. WebMD removed the action to the United States District Court for the Eastern District of North Carolina.

Thereafter, the access specifications pursuant to which data is transmitted to Quintiles were modified to further de-identify patient information. On March 13, 2001, the District Court entered an order continuing the state court temporary restraining order. A further hearing was conducted by the District Court on March 15, 2001 and, on March 16, 2001, the District Court ordered WebMD to continue to provide data to Quintiles in the form represented to the court during the March 15, 2001 hearing. That form reflected the modified access specifications. On March 21, 2001, the District Court entered an order continuing in effect the injunction. Currently, WebMD is providing data to Quintiles pursuant to this order.

In the course of this litigation, WebMD presented opinions of counsel that the transmission of data pursuant to the Data Rights Agreement violated certain state privacy laws. Quintiles disputed these legal interpretations. In response to this litigation, WebMD commenced a comprehensive review of the data mining practices established during the period Quintiles owned Envoy to determine whether the practices complied with applicable law and contracts. WebMD has raised with Quintiles its concern that certain of the data practices may not comply with other applicable laws or contracts. Quintiles disputes these contentions of WebMD.

Further proceedings in the matter have been stayed until October 1, 2001 and the parties are currently engaged in settlement discussions. Either party has the right to terminate the stay prior to October 1, 2001 upon seven business days written notice to the other party. While WebMD is hopeful that it will be able to resolve these issues amicably with Quintiles, there can be no assurance that the matter can be resolved without further litigation.

For additional information, see our 2000 annual report on Form 10-K under the heading Governmental Regulation.

InfoCure Corporation v. WebMD and Envoy

On March 8, 2001, InfoCure Corporation (d/b/a VitalWorks) filed a complaint against WebMD and Envoy in the Superior Court of the County of Fulton in the State of Georgia. The complained asserted, among other things, that WebMD had breached its marketing agreement with VitalWorks and sought damages in excess of $46.5 million. On July 20, 2001, VitalWorks and WebMD announced that the

litigation was settled without admission of liability by either side and announced their entry into a new three-year transaction processing agreement. Pursuant to the settlement agreement, WebMD paid approximately $2.5 million to VitalWorks, which settled all claims and amounts due under the parties prior agreements, and VitalWorks delivered to WebMD the stock certificate evidencing the 1,929,012 shares of VitalWorks common stock that was issued by VitalWorks earlier this year under the prior agreements.

Litigation regarding distribution of shares in Healtheon initial public offering

In July and August, 2001, three purported class action lawsuits were filed against Morgan Stanley & Co. Incorporated and Goldman Sachs & Co., underwriters of the initial public offering of WebMD (then known as Healtheon) in the United States District Court for the Southern District of New York. One of these suits also named WebMD and two former officers of WebMD as defendants in the case. The complaints allege violations of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder because of failure to disclose certain practices alleged to have occurred in connection with the distribution of shares in the Healtheon IPO. The suit that names WebMD and former officers as defendants also alleges violations of Section 11 of the Securities Exchange Act. Similar suits have been filed against the underwriters of other companies that went public in 1999 and 2000, following reports of governmental investigations of the distribution of shares in certain initial public offerings. We believe that the claims alleged in the lawsuits are primarily directed at the underwriters and, as they relate to us, are without merit. To the extent that these claims concern practices and disclosures relating to the plan of distribution in the Healtheon initial public offering, we believe that WebMD will have a claim for indemnification from the underwriters.

Other legal proceedings

In the normal course of business, we and our subsidiaries are involved in various other claims and legal proceedings. While the ultimate resolution of these matters, including those discussed above and in our 2000 annual report on Form 10-K under Legal Proceedings, has yet to be determined, we do not believe that their outcome will have a material adverse effect on our financial position.

ITEM 2. *Changes in Securities and Use of Proceeds*

In connection with the strategic alliance between WebMD and AOL described in note 2 to the financial statements contained in this quarterly report, WebMD issued to AOL a warrant to purchase 2,408,908 shares of WebMD common stock at an exercise price of $9.25 per share. The issuance of the warrant was exempt from registration under Section 4(2) of the Securities Act of 1933.

On June 28, 2001, WebMD issued 2,000,000 shares of its common stock to Cerner Corporation in exchange for approximately $400,000 in cash and the cancellation of various contractual obligations of WebMD to Cerner. The issuance of the shares was exempt from registration under Section 4(2) of the Securities Act.

On May 23, 2001, WebMD issued a convertible note with a principal amount of $900,000 in payment for a portion of the purchase price for the acquisition of the assets of MMS Development Corporation. On June 1, 2001, WebMD issued a convertible note with a principal amount of $800,000 in payment for a portion of the purchase price for the acquisition of the assets of MCS Systems Inc. On June 7, 2001, WebMD issued a convertible note with a principal amount of $375,000 in payment for a portion of the purchase price for the acquisition of the assets of Business and Industrial Computer Company. Each note is payable on the first anniversary of issuance or, in the alternative, WebMD (but not the holder) can cause the note to be converted into WebMD common stock commencing one month prior to the first anniversary of issuance, which will satisfy all obligations of WebMD to pay principal and interest on the note. The conversion price under each note would be based on a price per share of WebMD common stock equal to 90% of the then current market price at the time of conversion. The issuance of each convertible note was exempt from registration under Section 4(2) of the Securities Act.

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ITEM 5. ***Other Information***

At a meeting of the Board of Directors of WebMD Corporation (WebMD) on August 7, 2001, the Board resolved to change WebMD s registered agent as currently set forth in WebMD s Tenth Amended and Restated Certificate of Incorporation, as amended, to The Corporation Trust Company, the location of which is 1209 Orange Street, City of Wilmington, County of New Castle, Delaware 19801. As authorized by the Board, a Certificate of Change of Registered Agent and Location of Registered Office, a copy of which is included as an exhibit to this quarterly report on Form 10-Q, was filed with the Secretary of State of the State of Delaware on August 8, 2001 to effect this change.

Also at that meeting, the Board considered and approved certain amendments to WebMD s Amended and Restated Bylaws and determined to amend and restate them in their entirety. A copy of the Amended and Restated Bylaws of the Company as so adopted (the Bylaws) and in force on the date hereof is included as an exhibit to this quarterly report on Form 10-Q.

The Board of Directors has set November 16, 2001 as the date for the 2001 annual meeting of WebMD s stockholders and September 28, 2001 as the record date for the determination of stockholders entitled to vote at that meeting. Proposals that WebMD s stockholders intend to present at that meeting must be received by WebMD not later than the close of business on August 24, 2001, in order that they may be considered for possible inclusion in WebMD s proxy statement and form of proxy relating to that meeting. In addition, the Bylaws establish an advance notice procedure pursuant to which stockholder proposals not included in WebMD s proxy statement may be brought before a meeting of stockholders. For nominations or other business to be properly brought before the meeting by a stockholder, that stockholder must provide written notice delivered to the secretary of WebMD not later than the close of business on August 24, 2001. All notices of proposals by stockholders, whether or not to be included in WebMD s proxy materials, should be sent to: Secretary, WebMD Corporation, 669 River Drive, Center 2, Elmwood Park, New Jersey 07407-1361.

ITEM 6. ***Exhibits and Reports on Form 8-K***

(a) The exhibits listed in the accompanying Exhibit Index on page E-1 are filed as part of this quarterly report.

(b) No reports on Form 8-K were filed during the quarter ended June 30, 2001.

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SIGNATURES

In accordance with the requirements of the Securities Exchange Act, the Registrant has caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

WEBMD CORPORATION

By: /s/ ANTHONY VUOLO

Anthony Vuolo
Executive Vice President and Chief
Financial Officer

Date: August 13, 2001

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EXHIBIT INDEX

Exhibit No.	Description
3.1	Certificate of Change of Registered Agent and Location of Registered Office of WebMD Corporation
3.2	Amended and Restated Bylaws of WebMD Corporation
4.1	Form of Convertible Promissory Note