

Bloomberg

UnitedHealth Races McKesson in \$11 Billion Health-Tech Hunt

By Alex Nussbaum and Pat Wechsler - Aug 25, 2010

[UnitedHealth Group Inc.](#), the biggest U.S. insurer, and [McKesson Corp.](#), the largest drug distributor, are vying for billions of dollars in added sales by bulking up their information-technology units.

The companies are expanding beyond their core business to help insurers cope with the health overhaul, which threatens to swamp industry computer systems, said [Joanne Galimi](#), a Boston-based analyst for technology researcher Gartner Inc.

Bracing for added taxes and regulations, insurers are upgrading long-neglected systems used to enroll members, track care and process claims, Galimi said. They also face a 2013 switch to a new government-mandated system for classifying diseases. As a result, insurer spending on data technology will jump 24 percent by 2013, to \$11.3 billion, according to a March report by [IDC Health Insights](#), of Framingham, Massachusetts.

“Every health-care payer in the world needs an upgrade,” said [Stephen Krupa](#), a founder of Psilos Group Managers LLC, a venture capital fund with \$580 million invested in Click4Care and other medical companies. “You or I are talking about getting an iPad. They are still getting off mainframes.”

Insurers are seeking savings to offset costs from the legislation signed by President [Barack Obama](#) in March. The law calls for \$240 billion in taxes and Medicare cuts on [insurers](#) over the next decade, while adding as many as 32 million customers. It also caps the amount of premiums spent on administrative costs, and bans denials of coverage based on preexisting medical conditions.

Potential Acquisitions

The technology push may spur acquisitions of a growing crop of software vendors catering to the industry, among them [Click4Care Inc.](#) and ZeOmega, Galimi said.

UnitedHealth, based in Minnetonka, Minnesota, bought two closely held software companies during the last five weeks to expand its Ingenix data unit. For McKesson, technology sales are likely to be the San Francisco-based company’s biggest growth area over the next four years, said [Helene Volk](#), an

analyst at Sanford C. Bernstein & Co. in New York.

UnitedHealth, the biggest insurer by sales, rose 5 cents to \$31.09 in New York Stock Exchange composite [trading](#) at 9:42 a.m. It gained 4.5 percent in the 12 months before today. McKesson dropped 11 cents to \$60.21, after rising 7 percent in the past 12 months.

Insurers lag behind the banking industry, where customers routinely track accounts and make transactions online, Galimi said. That's partly because many of the [1,300 U.S. health plans](#) are nonprofits that haven't had the resources to stay current, the analyst said. Consolidation has also left companies with multiple, often redundant systems, she said.

Paper Records

"So many health insurers have manual processes, workarounds, paper-based records," Galimi said in a telephone interview. "The very big ones are doing better because they have dollars to spend, but they've also had more acquisitions under their belts, so they have more siloed systems."

A Gartner survey of 60 insurers in December 2008 found 70 percent had at least two back-end claims systems. Thirty-two percent had four or more.

Health plans are also retooling to comply with [ICD-10](#), a federally mandated system for classifying patients' medical conditions. The change will add thousands of disease codes as of Oct. 1, 2013, said Maureen O'Neil, another [Gartner](#) analyst. Installing and testing software may take insurers as long as 2½ years, she said.

"Virtually every core application is going to need to be changed," O'Neil said in a telephone interview.

Psilos Niche

That's created a niche for entrepreneurs like Krupa, the venture capitalist, who sees a market in using information- technology to streamline a U.S. health system that spends \$2.5 trillion annually.

Krupa's [Psilos](#) fund sold ActiveHealth Management and its care-coordination software to Hartford, Connecticut-based [Aetna Inc.](#), the third-largest U.S. insurer, for \$400 million in 2005. New York-based Psilos has investments in about 18 health-care companies today, among them Click4Care and Burlington, Massachusetts-based [HealthEdge Software Inc.](#), vendors that analyze patient data and organize benefits.

The companies have seen "unprecedented growth" in sales this year, said [Robert Gillette](#), CEO at both. Click4Care, based in Powell, Ohio, makes software that sifts through prescriptions, electronic

medical records, claims data and other information to identify patients at risk of developing a particular illness.

The company aims to help insurers flag the diabetic who hasn't been taking insulin or the 40-year-old due for a prostate exam, Gillette said. It's developing other programs that cater to patients and caregivers.

Texting Grandma

"If grandma's had a hip replacement, you'd get a text message reminding you to drive her to physical therapy," Gillette said. "We're working on an iPad application so you can track her care."

At some insurers, such "care management" work is still done by employees using "spreadsheets and sticky notes," Gillette said. Click4Care's programs do it automatically. HealthEdge makes software to track policy benefits and provider rates. Gillette declined to give specifics about either business's sales or to comment on the potential for being acquired.

Health-plan executives "finally understand after quite a few years that they need to transform," Gillette said. "A lot of them are looking at the technological transformation as a way to rally the organization."

ZeOmega Growth

Closely held [ZeOmega](#) sells software used to manage more than 10 million customers' medical care, up from about 7 million two years ago, Chief Financial Officer Nandini Ragaswamy said by telephone. She said the Frisco, Texas-based company expects "triple-digit growth," spurred by an aging U.S. population and rising medical costs.

"Health-care reform is the event that set it off, although the underlying factors have been there for years," said Ragaswamy, who founded ZeOmega with its CEO, her husband Sam. "The industry is coming to the conclusion that care management is going to be the critical solution to reduce health-care costs and still maintain quality."

She declined to discuss the chance of an acquisition.

Insurers may look to buy vendors to streamline their own systems and to improve the data they get from doctors and hospitals, said [David Larsen](#), an analyst at Leerink Swann & Co., a healthcare investment bank based in Boston. Among potential targets, he cited Portico Systems of Blue Bell, Pennsylvania; iHealth Technologies Inc. of Atlanta; and Benefitfocus of Charleston, South Carolina.

All are closely held.

Ingenix Deals

UnitedHealth's information-technology unit, Ingenix, said Aug. 16 that it would buy closely held Axolotl Corp., a San Jose, California-based creator of networks for doctors and hospitals to share medical data online. The insurer said July 22 that it had reached an agreement to acquire Picis Inc. of Wakefield, Massachusetts, a maker of software for emergency rooms and intensive care units. Terms of both deals were undisclosed.

Ingenix generated \$1.13 billion in [sales](#) last year, up from \$867 million in 2007. Health-technology and consulting are among UnitedHealth's biggest opportunities for growth, as the health law squeezes profit margins for traditional insurance, Chief Executive Officer [Stephen Hemsley](#) said in a July 20 conference call with analysts.

[McKesson](#) had \$3.1 billion in technology sales last year, about 3 percent of total revenue. While insurers have cut technology budgets amid the recession, they're working to automate as many administrative functions as they can, said Matthew Zubiller, a company vice president.

'Hand-Holding'

Labor-intensive systems for preauthorizing care are prime targets, according to Zubiller.

"These systems need a lot of hand-holding," he said in a telephone interview. "Every single authorization is touched by somebody."

[TriZetto Group Inc.](#), a closely held rival to Ingenix and McKesson, has also seen sales grow, said [Jeffrey Rideout](#), chief medical officer at the Greenwood Village, Colorado-based company. He declined to give specific figures. Insurers are rushing to comply with health-law mandates that take effect this year, among them a ban on lifetime benefit limits and extended coverage for some beneficiaries' adult children, he said.

"People don't understand how challenging this can be for insurers," Rideout said in a telephone interview. "It's not like you can go into the basement and flip a switch."

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