HEALTHWATCH INC
Form S-4/A
March 05, 2001

As filed with the Securities and Exchange Commission on March 5, 2001
Registration No. 333-48546

U. S. SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

Amendment No. 3
to
Form S-4
REGISTRATION STATEMENT
Under
The Securities Act of 1933

HEALTHWATCH, INC.
(Name of Registrant as specified in its charter)

Minnesota	7373	84-0916792
(State or jurisdiction of incorporation or organization)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification No.)

1100 Johnson Ferry Road
Suite 670
Atlanta, Georgia 30342
(404) 256-0083
(Address, including zip code, and telephone number, including area code, of Registrant's principal executive offices)

MICHAEL M. SMITH, ESQ.
J. CRAIG LEE, ESQ.
Gambrell & Stolz, L.L.P.
Suite 4300, SunTrust Plaza
303 Peachtree Street, N.E.
Atlanta, Georgia 30308
(404) 577-6000
Facsimile: (404) 221-6501
(Name, address, including zip code, and telephone and facsimile numbers, including area code, of agent for service)

Copy to:

GREGORY M. FRASSRAND
Gomel & Davis, LLP
700 Marquis Two Tower
285 Peachtree Center Avenue, N.E.
Atlanta, Georgia 30303
(404) 223-5900
Facsimile: (404) 524-4755

Approximate date of commencement of proposed sale to the public: As soon as practicable after this registration statement becomes effective and all other conditions to the merger of Halis, Inc. ("Halis") with and into the HealthWatch

Merger Sub, Inc. ("Merger Sub") pursuant to an Agreement and Plan of Merger, dated as of June 29, 2000, and as amended by amendments dated September 29, 2000 and January 31, 2001, described in the enclosed joint proxy statement/prospectus have been satisfied or waived.

If any of the securities being registered on this form are being offered in connection with the formation of a holding company and there is compliance with General Instruction G, check the following box. [_]

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [_]

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. [_]

CALCULATION OF REGISTRATION FEE

Title of each class of securities to be registered	Amount to be registered (1)	Proposed maximum offering price per share (2)	Proposed maximum aggregate offering price (2)	Amount of registration fee
Common Stock, $.05 par value ...	2,910,219 shares	$.312	$1,815,977	$453.99

(1) The registration statement relates to shares of common stock of the Registrant that may be issued to the stockholders of Halis, Inc., a Georgia corporation (excluding all shares owned directly by the Registrant), pursuant to the proposed merger, assuming the exercise of all outstanding options to purchase Halis common stock.

(2) Estimated solely for the purpose of calculating the registration fee required by the Securities Act of 1933, as amended, and computed pursuant to Rules 457(f)(1) and (c) under the Securities Act based on the average of the high and low per share prices of common stock of Halis, Inc. (HLIS.OB) as reported on the Nasdaq Securities Market on February 27, 2001 divided by the exchange ratio of 0.050.

The Registrant hereby amends this registration statement on such date or dates as may be necessary to delay its effective date until the Registrant shall file a further amendment which specifically states that this registration statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until this registration statement shall become effective on such date as the Commission, acting pursuant to said Section 8(a), may determine.

HEALTHWATCH, INC
1100 Johnson Ferry Road
Suite 670
Atlanta, Georgia 30342

To Our Stockholders:

You are cordially invited to attend a special meeting of stockholders of HealthWatch, Inc., to be held on March 29, 2001 at The W At Perimeter Center Hotel, 111 Perimeter Center West NE, Atlanta, Georgia 30346 at 10:00 a.m., local time.

The proposals expected to be acted upon at the meeting relate to the issuance of HealthWatch common stock in connection with a merger among HealthWatch, Inc., Halis, Inc. and HealthWatch Merger Sub, Inc. (a newly formed, wholly-owned subsidiary of HealthWatch) and the transactions associated with the merger that will cause Halis, Inc. to merge with and into HealthWatch Merger Sub, Inc. In addition, HealthWatch stockholders will be asked to approve an amendment to HealthWatch's Articles of Incorporation to increase the number of authorized shares of capital stock and to approve other proposals relating to the terms of outstanding HealthWatch preferred stock and other securities. These proposals are described in detail in the attached notice of special meeting of stockholders and proxy statement/prospectus.

In the merger, Halis stockholders would receive for each share of common stock of Halis, Inc. outstanding immediately prior to the effective time of the merger, one twentieth (.05) of a share of HealthWatch common stock (the "Merger Consideration"), thus for every twenty outstanding shares of Halis common stock (excluding those shares held by HealthWatch) we will issue one share of HealthWatch common stock. In addition, outstanding Halis, Inc. employee and director stock options would be converted into options to purchase HealthWatch common stock using the same exchange ratio. Based on the number of shares of Halis common stock outstanding on December 31, 2000, HealthWatch will issue approximately 2,300,000 shares of HealthWatch common stock to Halis stockholders in the merger, excluding Halis common stock owned by HealthWatch. HealthWatch intends to continue listing its common stock on the Nasdaq SmallCap Market under the symbol "HEAL."

After careful consideration, your board of directors has determined that the merger agreement and the transactions associated with it, including the stock issuance, are fair to and in the best interests of HealthWatch and its stockholders and has approved the merger agreement and other proposals.

Your board of directors recommends that you vote FOR the merger agreement and the transactions associated with it, including the stock issuance, and FOR each of the other proposals on which you may vote.

The merger, the merger agreement, the stock issuance and the other proposals are described in the accompanying joint proxy statement/prospectus, which you should read carefully, including the section describing risk factors that begins on page 15. If you have any questions or require additional information about the special meeting or the merger, please call Ms. Marilyn May, Vice President--Investor Relations, at (404) 256-0083.

Sincerely,

Paul W. Harrison
Chairman, President & Chief Executive Officer

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the HealthWatch common stock to be issued under this joint proxy statement/prospectus or determined if this joint proxy statement/prospectus is accurate or adequate. Any representation to the contrary is a criminal offense.

This joint proxy statement/prospectus is dated March , 2001 and was first mailed to stockholders on or about March , 2001.

HealthWatch, Inc.
1100 Johnson Ferry Road
Suite 670
Atlanta, Georgia 30342

NOTICE OF SPECIAL MEETING OF STOCKHOLDERS

TO BE HELD MARCH 29, 2001 AT 10:00 A.M.

To Our Stockholders:

A special meeting of the stockholders of HealthWatch, Inc. ("HealthWatch") will be held at located at The W At Perimeter Center Hotel, 111 Perimeter Center West NE, Atlanta, Georgia 30346 on March 29, 2001 at 10:00 a.m. for the following purposes:

1. To approve the issuance of shares of HealthWatch common stock in the merger of Halis, Inc. ("Halis") with and into HealthWatch Merger Sub, Inc., a wholly-owned subsidiary of HealthWatch ("Merger Sub"), as contemplated by the Agreement and Plan of Merger dated as of June 29, 2000, by and among Halis, Merger Sub and HealthWatch. In the merger, HealthWatch will issue one twentieth (.05) of a share of fully paid and non-assessable HealthWatch common stock for each share of Halis common stock outstanding;

2. To consider and vote upon proposed amendments to HealthWatch's Articles of Incorporation to:

   A: increase the number of authorized shares of HealthWatch common stock from 10,000,000 shares to 50,000,000 shares; and

   B: increase the number of authorized shares of HealthWatch preferred stock from 1,000,000 shares to 15,000,000 shares;

3. To ratify and approve anti-dilution provisions related to HealthWatch's outstanding preferred stock and related warrants contained in:

   A: the Certificate of Designation, Preferences and Rights of Series C 8% Convertible Preferred Stock (the "Series C Preferred");

   B: the Certificate of Designation, Preferences and Rights of Series D 8% Convertible Preferred Stock (the "Series D Preferred");

   C: warrants to purchase HealthWatch common stock issued to purchasers of the Series C Preferred in a bridge financing completed in February 2000 (the "Bridge Warrants");

   D: warrants to purchase HealthWatch common stock issued to purchasers of the Series D Preferred in a private placement completed in May 2000 (the "Offering Warrants"); and

   E: warrants to purchase HealthWatch common stock issued to an affiliate of Commonwealth Associates, L.P. in connection with a $2 million line of credit (the "Line of Credit Warrants");

4. To ratify and approve the conversion feature and the issuance of shares of HealthWatch common stock upon conversion of HealthWatch's outstanding Series P Preferred Stock (the "Series P Preferred"); and

5. To transact any other business that properly comes before the special meeting or any adjournment and postponements thereof.

The accompanying proxy statement/prospectus describes the proposed merger and other proposals in more detail. We encourage you to read the entire document carefully.

We have fixed the close of business on February 16, 2001 as the record date for the determination of our stockholders entitled to vote at this meeting.

By Order of the Board of Directors

Paul W. Harrison, Chairman,
President and Chief Executive
Officer

Atlanta, Georgia

Date: March , 2001

Halis, Inc.
1100 Johnson Ferry Road
Suite 670
Atlanta, Georgia 30342

To Our Stockholders:

Halis, Inc.'s board of directors has approved a merger which will result in the acquisition of Halis by HealthWatch, Inc., a publicly-traded company headquartered in Atlanta, Georgia. In the merger, each share of Halis, Inc. common stock will be converted into one twentieth (.05) of a share of HealthWatch common stock. Therefore, the exchange ratio will be one share of HealthWatch common stock for each twenty shares of Halis Common Stock. In addition, holders of Halis stock options will have their options converted into options to purchase HealthWatch common stock based on the same exchange ratio. HealthWatch common stock is traded on the Nasdaq SmallCap Market under the symbol "HEAL."

This joint proxy statement/prospectus is also the prospectus of HealthWatch regarding the HealthWatch common stock to be issued to Halis stockholders in exchange for their shares of Halis common stock in connection with the merger. Based on the number of shares of Halis common stock outstanding on December 31, 2000, HealthWatch will issue approximately 2,300,000 shares of HealthWatch common stock to Halis stockholders in the merger, excluding Halis common stock owned by HealthWatch.

The merger cannot be completed unless the holders of a majority of Halis' common stock approve the merger agreement and the merger. Only stockholders who hold common shares of Halis at the close of business on February 16, 2001 will be entitled to vote at the special meeting. After careful consideration, your board of directors has determined the merger is in your best interest and recommends that you vote in favor of the merger.

This joint proxy statement/prospectus provides you with detailed information concerning HealthWatch, Halis and the merger. Please give all of the information contained in the proxy statement/prospectus your careful attention. In particular, you should carefully consider the discussions in the section entitled "Risk Factors" on page 15 of the joint proxy statement/prospectus.

Each Company has scheduled a special meeting for its stockholders to vote on the merger agreement and the transactions associated with it. The special meeting of Halis stockholders will be held on March 29, 2001 at 12:30 p.m. local time at The W At Perimeter Center Hotel, 111 Perimeter Center West NE, Atlanta, Georgia 30346.

Please use this opportunity to take part in the affairs of Halis by voting on the adoption of the merger agreement. Whether or not you plan to attend the meeting, please complete, sign, date and return the accompanying proxy in the enclosed self-addressed stamped envelope. Returning the proxy does NOT deprive you of your right to attend the meeting and to vote your shares in person. YOUR VOTE IS VERY IMPORTANT.

We appreciate your interest in Halis and your consideration of this matter.

Dr. Joel Greenspan,
Member of Halis' Board of Directors

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved the HealthWatch common stock to be issued under this joint proxy statement/prospectus or determined if this joint proxy statement/prospectus is accurate or adequate. Any representation to the contrary is a criminal offense.

This joint proxy statement/prospectus is dated March , 2001 and was first mailed to stockholders on or about March , 2001.

Halis, Inc.
1100 Johnson Ferry Road
Suite 670
Atlanta, Georgia 30342

NOTICE OF SPECIAL MEETING OF STOCKHOLDERS

TO BE HELD MARCH 29, 2001 AT 12.30 P.M.

To Our Stockholders:

NOTICE IS HEREBY GIVEN that the special meeting of stockholders of Halis, Inc. ("Halis") will be held on March 29, 2001 at 12:30 p.m. at The W At Perimeter Center Hotel, 111 Perimeter Center West NE, Atlanta, Georgia 30346 to:

1. Consider and vote on the proposed merger of Halis, Inc. with and into HealthWatch Merger Sub, Inc., a wholly-owned subsidiary of HealthWatch, Inc., as contemplated by the Agreement and Plan of Merger dated as of June 29, 2000, by and among Halis, Inc., HealthWatch Merger Sub, Inc. and HealthWatch, Inc. In the merger, HealthWatch, Inc. will issue one twentieth (.05) of a share of fully paid and non-assessable HealthWatch, Inc. common stock in exchange for each outstanding share of Halis common stock; and

2. Transact such other business as may properly come before the Halis special meeting or any adjournment thereof.

Your board of directors has determined that the merger agreement and the merger are in your best interests and recommends that you vote to approve the merger agreement at the special meeting.

The board of directors has fixed the close of business on February 16, 2001 as the record date for the determination of stockholders entitled to notice of, and to vote at, the Halis special meeting. The merger cannot be completed unless holders of a majority of the outstanding shares of Halis common stock on the record date affirmatively vote to approve the merger agreement.

Accompanying this notice is a joint proxy statement/prospectus discussing the proposed merger and the related merger agreement. We encourage you to read this document carefully. Regardless of whether you expect to be present at the meeting, please mark, date and sign the enclosed proxy and return it in the envelope which has been provided. No postage is required for mailing in the United States. In the event you are able to attend the Halis special meeting, you may revoke your proxy and vote your shares in person.

By Order of the Board of Directors,

Dr. Joel Greenspan,
Member of the Board of Directors

Atlanta, Georgia

Date: March , 2001

TABLE OF CONTENTS

Page

ANNEXES:

A-- Agreement and Plan of Merger, dated as of June 29, 2000
B-- Amendment to Agreement and Plan of Merger, dated as of September 29, 2000
C-- Form of HealthWatch's Stock Option Agreement
D-- Fairness Opinion of New York Capital
E-- Certificate of Designation, Preferences and Rights of the Series C 8% Convertible Preferred Stock of HealthWatch, Inc.
F-- Certificate of Designation, Preferences and Rights of the Series D 8% Convertible Preferred Stock of HealthWatch, Inc.
G-- Warrant Agreement and Form of warrant representative of the Bridge Warrants, Offering Warrants and Line of Credit Warrants
H-- Certificate of Designation, Preferences and Rights of the Series P Preferred Stock of HealthWatch, Inc.
I-- Article 13 of the Georgia Business Corporations Code.

FORWARD LOOKING STATEMENTS MAY PROVE INACCURATE

This document and other communications to stockholders of HealthWatch and Halis may contain "forward looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These statements relate to expectations concerning matters that are not historical facts. Also, when we use words such as "believes," "expects," "anticipates" or similar expressions, we are making forward looking statements. Although each of HealthWatch and Halis believes that the expectations reflected in such forward looking statements are reasonable, neither of us can give any assurance that our expectations will prove to be correct. Important factors that could cause our actual results to differ materially from our expectations are disclosed herein, including, without limitation, the factors we discuss under the section entitled "RISK FACTORS" beginning on page 15. All forward looking statements attributable to HealthWatch and Halis are expressly qualified in their entirety by the factors which may cause actual results to differ materially from expectations described herein.

YOU SHOULD RELY ONLY ON THE INFORMATION CONTAINED IN THIS JOINT PROXY STATEMENT/PROSPECTUS TO VOTE ON THE MERGER AGREEMENT AND THE TRANSACTIONS ASSOCIATED WITH IT. WE HAVE NOT AUTHORIZED ANYONE TO PROVIDE YOU WITH INFORMATION THAT IS DIFFERENT FROM WHAT IS CONTAINED IN THIS JOINT PROXY STATEMENT/PROSPECTUS. THIS JOINT PROXY STATEMENT/PROSPECTUS IS DATED MARCH , 2001. YOU SHOULD NOT ASSUME THAT THE INFORMATION CONTAINED IN THIS JOINT PROXY STATEMENT/PROSPECTUS IS ACCURATE AS OF ANY DATE OTHER THAN SUCH DATE, AND NEITHER THE MAILING OF THIS JOINT PROXY STATEMENT/PROSPECTUS TO STOCKHOLDERS NOR THE ISSUANCE OF HEALTHWATCH COMMON STOCK IN THE MERGER SHALL CREATE ANY IMPLICATION TO THE CONTRARY.

QUESTIONS AND ANSWERS FOR HEALTHWATCH STOCKHOLDERS AND HALIS STOCKHOLDERS

Q: Why are the two companies proposing to merge and how will I benefit?

A: The combined company's breadth of technology, products, management and operational experience and financial resources should enable it to respond more quickly and effectively to technological change, intensifying competition, increasing consolidation and evolving market demands. Moreover, management of HealthWatch and Halis believe that the combined company could achieve operating synergies through cross marketing of each company's products, as well as possible cost savings related to more efficient administrative and support functions of the combined company. To review the reasons for the merger in greater detail, and related uncertainties, see pages 73 and 80.

Q: What will Halis stockholders receive in the merger?

A: Halis stockholders will receive for each share of Halis common stock one twentieth (.05) of a share of HealthWatch common stock (i.e., one share of

HealthWatch common stock for twenty shares of Halis common stock). HealthWatch will not issue fractional shares. Halis stockholders who would otherwise be entitled to receive a fractional share instead will receive a cash payment based on the average market value of the fractional share of HealthWatch stock during a specified period prior to the merger.

Holders of options or warrants to purchase shares of Halis common stock will receive options or warrants, as appropriate, to purchase shares of HealthWatch common stock after completion of the merger. The number and exercise price of the options or warrants received will be based on the same Exchange Ratio.

For Example:

If you currently own 250 shares of Halis common stock and assuming an average closing price of $3.00 for HealthWatch common stock, then after the merger you will be entitled to receive twelve (12) shares of HealthWatch common stock and a check for the market value of the .50 fractional share or $1.50 (.50 X $3.00).

If you currently own 200 shares of HealthWatch common stock, then you will continue to own those 200 shares after the merger.

Q: When do you expect the merger to be completed?

A: We are working towards completing the merger as quickly as possible. In addition to stockholder approvals, we must also satisfy other conditions described in the merger agreement. We hope to complete the merger during the first calendar quarter of 2001.

Q: What will HealthWatch's dividend policy be?

A: HealthWatch has never declared or paid dividends on its common stock, and does not expect to declare common dividends in the near future. Furthermore, the terms of HealthWatch's outstanding preferred stock restrict the payment of dividends on common stock until all preferred stock dividends were paid. HealthWatch's board of directors will use its discretion to decide whether to declare dividends and the amount of any dividends. In making its decision, the board will consider various factors, including tax efficiency, continuing investment opportunities and the earnings and financial condition of HealthWatch and its subsidiaries.

Q: What do I need to do now?

A: Just mail your signed proxy card in the enclosed return envelope as soon as possible, so that your shares will be represented at your special stockholders' meeting. If you do not include instructions on how to vote your properly signed proxy, your shares will be voted "FOR" approval of the merger.

Q: What do I do if I want to change my vote?

A: If you want to change your vote, send the secretary of HealthWatch or Halis, as the case may be, a later-dated, signed proxy card before your meeting or attend the meeting in person. You may also revoke your proxy by sending written notice to your company's secretary before the meeting.

Q: Should I send in my stock certificates now?

A: No. After the merger is completed, Halis stockholders will receive written instructions for exchanging their stock certificates. HealthWatch stockholders will keep their certificates, as the merger will not require surrender of outstanding HealthWatch stock certificates.

Q: Who can help answer further questions?

A: If you have any questions about the merger or how to submit your proxy, or if you need additional copies of this joint proxy statement/prospectus or the enclosed proxy card or voting instructions, you should contact:

. if you are a HealthWatch stockholder:

HealthWatch, Inc.
Investor Relations
1100 Johnson Ferry Road, Suite 670
Atlanta, Georgia 30342
(404) 256-0083

. if you are a Halis stockholder:

Halis, Inc.
Investor Relations
1100 Johnson Ferry Road, Suite 670
Atlanta, Georgia 30342
(404) 364-1871

3

SUMMARY OF THE JOINT PROXY STATEMENT/PROSPECTUS

This proxy statement/prospectus pertains to the merger of Halis with and into a newly formed wholly-owned subsidiary of HealthWatch, and is being sent to the stockholders of both companies. This summary may not contain all of the information that is important to you. You should read carefully this entire document and the other documents referenced in it for a more complete understanding of the merger. In particular, you should read the documents attached to this proxy statement/prospectus, including the merger agreement, which is attached as Annex A, and the opinion of New York Capital Corporation, which is attached as Annex D, and the opinion Houlihan Lokey Howard & Zukin Financial Advisors, Inc., which is attached as Annex L.

The Companies

HealthWatch, Inc.
1100 Johnson Ferry Road
Suite 670
Atlanta, Georgia 30342
(404) 256-0083

HealthWatch, Inc. is a healthcare information technology company operating as an Enterprise Applications Provider and an Application Service Provider for a variety of healthcare businesses. The primary difference between an Enterprise Service Provider and an Application Service Provider is where the software program and data is physically processed and stored. As an Enterprise Application Provider, HealthWatch offers its customers one comprehensive software program that will meet the customer's total information technology needs, which is installed and managed on the customer's system. As an Application Service Provider, HealthWatch offers its customers access to its software product through the Internet and charges a fee on a per user basis. HealthWatch offers an enterprise software program, known as the Healthcare Enterprise System (the "HES System"), which uses proprietary technology to distribute, in compressed digital format, one integrated system that includes over 50 information applications for the management of a healthcare enterprise's resources, patient data, clinical data and finances. The HES System is capable of processing and tracking information for the entire healthcare cycle from the doctor visit, specialty clinic or hospital stay, to the laboratory tests, pharmacy prescriptions, home care, insurance payments and more. The HES System can efficiently download applications over the Internet to a customer managed and operated environment or run applications efficiently on the Internet as an outsourced application, where HealthWatch will manage and maintain the HES System. HealthWatch is currently in the marketing and deployment stage for the HES System. HealthWatch first began offering the HES System as an Application Service Provider and Enterprise Service Provider in October 2000. However, as of the date hereof, HealthWatch has generated virtually no revenue from the sale of the HES System. Almost all revenue for the six months ended December 31, 2000, was from supplies, service and repair work associated with HealthWatch's medical device business, which has been discontinued.

In both the Enterprise Application Provider and Application Service Provider models, HealthWatch expects to market, deliver and maintain the HES System primarily over the Internet. The HES System can be used by physician practices, outpatient clinics, hospitals, long-term care facilities, home health providers, health insurance payors and other healthcare facilities.

Halis, Inc.
1100 Johnson Ferry Road
Suite 670
Atlanta, Georgia 30342
(404) 364-1871

Halis, Inc., based in Atlanta, Georgia, owns the HES System, which incorporates a software utility known as MERAD that provides an advanced database architecture and intelligent information processing algorithms that was developed by HealthWatch and has been licensed to Halis pursuant to a perpetual software license

4

agreement. Under a business collaboration agreement between HealthWatch and Halis, HealthWatch has a non-exclusive right to market the HES System and receive commissions from any sale made by HealthWatch. The business collaboration agreement expires on September 20, 2005 with automatic renewals for successive one-year terms.

Halis targets its healthcare software program business to healthcare industry participants, such as physician practices, outpatient clinics and hospitals that generally have 100 users or more. Halis expects to capitalize on the healthcare industry's demand for software that is flexible, easy to maintain and cost efficient. In addition, Halis' subsidiary, American Benefit Administrative Services, Inc., provides claims processing and other administrative services to major companies throughout the United States.

During the first quarter of fiscal year 1999, Halis' board of directors decided that in order to conserve its resources and to operate more efficiently, Halis would focus its attention on support and services to Halis' current HES System customers and on its claims processing capabilities, and would rely upon HealthWatch to market the HES System to new customers. HealthWatch is in the process of expanding this capability with the goal of identifying third party resellers for the HES System. Halis' corporate headquarters are located in Atlanta, Georgia. HealthWatch and Halis share office space and administrative support under a cost sharing arrangement. Halis' Chicago facility is the location for its American Benefit Administrative

Services subsidiary, which performs healthcare claims processing and other healthcare related services for employers.

Our Reasons for the Merger

The HealthWatch and Halis boards of directors have determined that the merger is in the best interests of their respective stockholders. In reaching their respective decisions, the boards of directors of the two companies considered the following factors, among other things:

- The two companies share common management and have similar philosophies with regard to future growth. In addition, the two companies have worked closely in the development and deployment of the HES System.

- The two companies can achieve potential synergies and operating efficiencies through combining the companies and cross-marketing each company's products and services. To review the reasons for the merger in greater detail, as well as related uncertainties, see pages 73 and 80.

- The merger would allow the combined company to lessen duplicate administrative and regulatory burdens, thus allowing it to focus more of its financial and personnel resources on the marketing, selling and support of its software products and services.

Risks of the Merger

In considering whether to approve the merger agreement, you should consider the risks of the merger, including the following:

- HealthWatch has operating losses totaling over $30 million and Halis has operating losses totaling over $38 million; together, the combined companies have lost over $69 million since inception and we expect losses to continue in the foreseeable future;

- HealthWatch first began marketing a pilot version of the HES System in 1998; however, to date there have been no sales from that effort;

- The exchange ratio for the merger is fixed, as such the value received by Halis stockholders and paid by HealthWatch could change if the market price of HealthWatch's common stock changes;

- HealthWatch's executive officers and directors and their affiliates have control over 29% of the voting power of HealthWatch, as such they will be able to control matters submitted to a vote of the stockholders of HealthWatch, including the election of directors;

- HealthWatch and Halis rely on the HES System as its sole product and our success is dependent on the healthcare industry's acceptance of that product.

We urge you to read carefully the factors described in "RISK FACTORS" on pages 15 through 25 in making your decision.

Conflicts of Interests (Page 84)

In considering the boards' recommendations that you vote to approve the merger, you should note that the directors and officers of HealthWatch and Halis participate in arrangements and have continuing indemnification against certain liabilities that provide them with interests in the merger that are different from, or in addition to, yours. These rights and interests include positions as directors and/or executive officers of HealthWatch following the merger and the right to continued indemnification and insurance coverage by HealthWatch for acts or omissions occurring prior to the merger. As a result, these directors and officers could be more likely to vote to approve the merger agreement than stockholders of HealthWatch and Halis generally.

In addition, Paul W. Harrison is the Chairman, President and CEO of both Halis and HealthWatch. Furthermore, John Gruber, Robert Tucker and John R. Prufeta, members of HealthWatch's board of directors, have current or past employment or contractual relationships with Commonwealth Associates, L.P., and pursuant to an agency agreement between Commonwealth Associates and HealthWatch, Commonwealth Associates will receive a fee equal to five percent of the consideration paid or received in the merger. While there are no agreements in place between the above named directors and Commonwealth Associates that would convey benefits directly to such directors, as a result of their current or past employment relationships, these directors could be more likely to vote to approve the merger agreement than stockholders of HealthWatch and Halis generally.

Recommendations to Stockholders

To HealthWatch Stockholders:

The HealthWatch board of directors believes that the merger is in your best interests and recommends that you vote FOR the proposal to approve the merger agreement and the transactions associated with it, including the issuance of shares of HealthWatch common stock to Halis stockholders and the conversion of Halis stock options into options to purchase HealthWatch common stock. In addition, the HealthWatch board of directors recommends that you vote FOR the proposals to amend the HealthWatch Articles of Incorporation to increase HealthWatch's authorized capital stock and ratify and approve anti-dilution provisions contained in its outstanding preferred stock and other securities. These recommendations were made by a vote of directors present at a meeting of the board of directors of HealthWatch to approve the merger agreement.

To Halis Stockholders:

The Halis Board believes that the merger is in your best interests and recommends that you vote FOR the proposal to approve the merger agreement and the transactions associated with it.

Stockholder Vote Required to Approve the Merger

HealthWatch:

The merger agreement and the transactions associated with it must be approved by the affirmative vote of a majority of shares present in person or by proxy at the special meeting of the HealthWatch stockholders and entitled to vote thereon, which may include persons who are directors and executive officers of HealthWatch, Halis, or in some cases both companies. As of December 31, 2000, directors and executive officers of HealthWatch held 153,021 shares or approximately 3.4% of the outstanding shares entitled to vote at the HealthWatch special meeting. This number includes 121,531 shares held by Paul W. Harrison, Chairman, President and CEO of HealthWatch and Halis. In addition, Halis holds 16,667 shares or .3% of the outstanding shares entitled to vote at the HealthWatch special meeting. The Halis board of directors and Mr. Harrison have both indicated their intent to vote FOR the merger in their capacity as stockholders of HealthWatch.

Halis:

The merger agreement and the transactions associated with it must be approved by the affirmative vote of the holders of a majority of the issued and outstanding stock entitled to vote at the special meeting of the Halis stockholders. This includes persons who are directors and executive officers of HealthWatch, Halis, or in some cases both companies. As of December 31, 2000, the directors and executive officers of Halis held approximately 5.3% of the outstanding shares of Halis entitled to vote at the Halis special meeting, of which 2,990,849 shares or 4.8% were held by Mr. Harrison. In addition, HealthWatch directly holds 15,763,655 shares or 25.7% of the outstanding shares of Halis entitled to vote on the merger. The HealthWatch board of directors and Mr. Harrison have both indicated their intent to vote FOR the merger in their capacity as stockholders of Halis. Assuming the Halis directors and officers, including Mr. Harrison, and HealthWatch vote FOR the merger proposal, only 12,093,107 shares or 28% of the remaining shares entitled to vote will be necessary to approve the merger.

Because the merger agreement and transactions associated with it must be approved by a majority of the outstanding capital stock entitled to vote, your abstention, failure to vote or your failure to instruct your broker as to how to vote your shares will have the effect of a vote "Against" the merger agreement and the transactions associated with it.

To review information relating to stockholder votes in greater detail, see "THE SPECIAL MEETINGS--Voting Securities and Record Dates Securities and Record Date" beginning on page 26.

HealthWatch Stockholder Vote Required to Approve Other Proposals

A majority of all issued and outstanding capital stock entitled to vote, including common stock, the Series C Preferred and the Series D Preferred voting as a single class, must approve HealthWatch's proposal to increase the authorized capital stock from 10 million shares of common stock and 1 million shares of preferred stock to 50 million shares of common stock and 15 million shares of preferred stock (Proposals 2.A and 2.B). Abstentions and broker non-votes will have the effect of a vote "Against" these proposals.

All other HealthWatch proposals (Proposals 3.A through 3.E and Proposal 4) must be approved by the affirmative vote of a majority of the voting power present in person or by proxy at the special meeting of the HealthWatch stockholders and entitled to vote thereon. For these proposals, abstentions are counted for the purposes of calculating shares entitled to vote, but are not counted as shares voting and therefore have the effect of a vote "Against" each such proposal. Also, for these proposals, broker non-votes are not counted as shares present at the meeting and entitled to vote and therefore have no effect.

The Merger

In the merger, Halis will merge with and into a wholly-owned subsidiary of HealthWatch named HealthWatch Merger Sub, Inc., a Georgia corporation. HealthWatch Merger Sub, Inc. will survive the merger and Halis will cease to exist as a separate corporate entity. The merger agreement is attached as Annex A at the back of this joint proxy statement/prospectus. We encourage you to read the merger agreement as it is the legal document that governs the merger.

What Stockholders Will Receive in the Merger

As a result of the merger, Halis stockholders will receive for each share of Halis common stock that they own one twentieth (.05) of a share of fully paid and non-assessable HealthWatch common stock; the exchange ratio shall be one share of HealthWatch common stock for twenty shares of Halis common stock, or .05. Halis stockholders will not receive fractional shares. Instead, they will receive a check in payment for any fractional share based on the average market value of HealthWatch common stock during a specified period prior to the merger.

In addition, at the time the merger is completed, holders of Halis stock options will have their options converted into options to purchase HealthWatch common stock. The exercise price of such converted options will be adjusted to reflect the exchange ratio.

Do not send in your stock certificates now. When the merger is completed you will receive written instructions for exchanging your Halis stock certificates. HealthWatch stockholders will continue to hold their HealthWatch stock certificates.

Ownership of HealthWatch Following the Merger

The shares of HealthWatch common stock issued to Halis stockholders in the merger will constitute approximately 52% of the outstanding HealthWatch common stock after the merger. The current stockholders of HealthWatch will hold the remaining approximately 48% of the outstanding HealthWatch common stock after the merger. However, if the holders of the Series C and D Preferred convert all of their Shares into HealthWatch common stock, the current stockholders of HealthWatch will own 66% of the outstanding HealthWatch common stock, and the former stockholders of Halis (excluding HealthWatch) will own 34% of the outstanding HealthWatch common stock.

Conditions to Completion of the Merger (see Page 93)

HealthWatch's and Halis' respective obligations to complete the merger are subject to the satisfaction or waiver of various closing conditions. Should either party fail to satisfy its respective obligations, the non-breaching party may be permitted to withdraw from the merger, and the breaching party may be subject to a $500,000 termination fee under certain circumstances. The material conditions that must be satisfied or waived before the completion of the merger include the following:

- The Halis stockholders must approve the merger agreement and merger and the HealthWatch stockholders must approve the issuance of HealthWatch common stock in the merger.

- HealthWatch, Halis and any of their subsidiaries must receive all consents, approvals and actions of, filings with and notices to, any governmental entity required to consummate the merger, and the other transactions contemplated thereby, must be obtained.

- No injunction or order preventing the completion of the merger may be in effect.

- HealthWatch and Halis each must receive an opinion of tax counsel to the effect that the merger will qualify as a transaction in which no gain or loss for United States federal income tax purposes will be recognized upon receiving HealthWatch shares.

- The shares of HealthWatch common stock to be issued in the merger must have been approved for listing on the Nasdaq SmallCap Market.

- A Form S-4 covering the shares of HealthWatch common stock to be issued in the merger must become effective under the Securities Act of 1933 prior to the mailing of this joint proxy statement/prospectus and no stop order or proceeding seeking a stop order may be threatened or initiated by the United States Securities and Exchange Commission.

- HealthWatch's and Halis' respective representations and warranties in the merger agreement must be true and correct in all material respects.

- No material adverse effect shall have occurred with respect to HealthWatch or Halis.

- HealthWatch and Halis must have complied in all material respects with their respective agreements and covenants in the merger agreement.

8

If either HealthWatch or Halis waives any conditions, each company will consider the facts and circumstances at that time and determine whether it is appropriate to resolicit proxies from its respective stockholders.

Termination (Page 94)

Together HealthWatch and Halis may agree to terminate the merger agreement without completing the merger, whether or not their respective stockholders have approved the merger agreement. The merger agreement may also be terminated by the board of directors of either company in certain other circumstances, including:

- If the merger is not completed on or before March 31, 2001, except that neither HealthWatch nor Halis may terminate the merger agreement if its breach of the merger agreement is the reason the merger has not been completed by that date;

- If the Halis or HealthWatch stockholders do not approve the merger;

- If the other company's board of directors has failed to recommend the merger to its stockholders or has withdrawn or adversely modified or qualified its recommendation of the merger; or

- If the other company has failed to perform certain of its obligations under the merger agreement.

Officers and Directors Following the Merger

Following the merger, the board of directors of HealthWatch will consist of six members, including Paul W. Harrison, who is a current member of both the Halis and HealthWatch boards. In addition, David M. Engert, Robert Tucker, John R. Prufeta, John Gruber and Harold Blue will continue to serve on the HealthWatch board of directors.

Following the merger, Paul W. Harrison, the current Chairman, President and Chief Executive Officer of Halis and HealthWatch, will continue to serve as Chairman, President and Chief Executive Officer of HealthWatch. In addition, the other officers of HealthWatch will continue to serve in their respective positions until their resignation or removal.

Important United States Federal Income Tax Consequences

We have structured the merger so that, in general, the exchange of Halis common stock for HealthWatch common stock will be tax-free to Halis stockholders for federal income tax purposes, except for cash paid for fractional shares. HealthWatch and Halis must receive legal opinions to this effect as a condition of the merger. To review the tax consequences to stockholders in greater detail, see page 97.

Tax matters are very complicated and the tax consequences of the merger to you will depend on your individual circumstances. You should consult your tax advisors for a full understanding of all of the tax consequences of the merger to you.

Dissenters' Rights (see Page 85)

Under Georgia law, Halis stockholders who submit a written demand for appraisal of their shares and who comply with the other applicable statutory procedures under Georgia law, including not voting in favor of adopting the merger agreement, will be entitled to appraisal rights and to receive payment in cash for the fair value of their shares.

Opinion of Financial Advisors

HealthWatch:

In deciding to approve the merger, the HealthWatch board of directors considered the opinion of its financial advisor, Houlihan Lokey Howard & Zukin Financial Advisors, Inc., as to the fairness, as of the date of the opinion, of the merger from a financial point of view to the HealthWatch public stockholders. The full text of this opinion, which contains the assumptions made, matters considered and the qualifications and limitations on the review undertaken, is attached as Annex L to this joint proxy statement/prospectus. We encourage you to carefully read this opinion in its entirety. This opinion does not address the price at which HealthWatch common stock will trade after the merger and does not constitute a recommendation as to how to vote with respect to any matter relating to the merger. For more information about the Houlihan Lokey opinion, see pages 74 through 79.

Halis:

In deciding to approve the merger, the Halis board of directors considered the opinion of its financial advisor, New York Capital Corporation, as to the fairness, as of the date of the opinion, of the exchange ratio from a financial point of view to the Halis stockholders. The full text of this opinion, which contains the assumptions made, matters considered and the qualifications and limitations on the review undertaken, is attached as Annex D to this joint proxy statement/prospectus. We encourage you to carefully read this opinion in its entirety. This opinion does not address the price at which HealthWatch common stock will trade after the merger and does not constitute a recommendation as to how to vote with respect to any matter relating to the merger. For more information about the New York Capital Corporation opinion, see pages 80 through 84.

Comparative Per Share Market Price Information

Shares of HealthWatch common stock are listed on the Nasdaq SmallCap Market and shares of Halis are quoted on the OTC Bulletin Board. On March 7, 2000, the last trading day before the announcement of the proposed merger, the

HealthWatch common stock closed at $6.875 per share and the Halis common stock closed at $0.39 per share. On March , 2001, the last trading day prior to the date of this joint proxy statement/prospectus, HealthWatch common stock closed at $ per share and Halis common stock closed at $ per share. For more information about the comparative market price information, see page 116.

Exchange Value Received by Halis Stockholders

The following table shows (1) the closing price for HealthWatch common stock and Halis common stock on (a) the day management first announced the merger and (b) the date of this joint proxy statement/prospectus and (2) the exchange value that Halis stockholders will receive on a per share basis and an aggregate basis.

	HealthWatch Common Stock	Halis Common Stock	Value Received by Halis Stockholders Per Share(1)	Aggregate(2)
March 7, 2000(3)............	$6.875	$.39	$.34	$790,625
March 8, 2000(4)............	$6.75	$.41	$.34	$776,250
March , 2001(5)............				

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(1) Calculated by multiplying the HealthWatch closing price by the exchange ratio (.050).
(2) Calculated by multiplying the per share value received by Halis stockholders by the approximate number of shares to be issued (2,300,000).
(3) The last day of trading prior to the announcement of the merger.
(4) The day the companies jointly announced the signing of a letter of intent for the merger.
(5) The date of this joint proxy statement/prospectus.

Comparative Rights of Stockholders (see Page 99)

The rights of stockholders of HealthWatch are governed by Minnesota law and its articles of incorporation and by-laws. The rights of Halis stockholders are governed by Georgia law and its articles of incorporation and by-laws. If the merger is completed, the rights of former Halis stockholders who become HealthWatch stockholders will be determined by Minnesota law and HealthWatch's articles of incorporation and by-laws, which differ in certain respects from Halis' articles of incorporation and by-laws.

Selected Historical and Pro Forma Consolidated Financial Data

The following tables show (1) selected historical consolidated financial data of HealthWatch, (2) selected historical consolidated financial data of Halis and (3) unaudited selected historical consolidated financial data reflecting the merger of HealthWatch and Halis (which is referred to as "pro forma" information). In presenting the pro forma statement of operations data for the fiscal year ended June 30, 2000, HealthWatch and Halis assume the companies had been merged throughout such respective periods. The pro forma balance sheet data as of December 31, 2000 assumes that HealthWatch and Halis merged on December 31, 2000. The following tables also show information about

HealthWatch's and Halis' historical earnings per share and book value per share and similar pro forma information.

The information in the following tables is based on the historical consolidated financial information contained elsewhere in this document. The financial information presented in this section is only a summary, and you should read it in connection with the detailed financial information provided elsewhere in this document, which you can find beginning on page F-1.

We expect to incur transaction costs consisting primarily of financial advisor, legal, accounting and investment banking fees, along with printing, mailing and registration expenses that are expected to be incurred to complete the merger. These costs have not been reflected in the selected unaudited pro forma condensed consolidated financial data due to their non-recurring nature. The selected unaudited pro forma condensed consolidated financial data is based on an exchange ratio of 0.05 shares of HealthWatch common stock for each outstanding Halis share and for each outstanding option or warrant for Halis stock, excluding Halis shares owned by HealthWatch.

The selected unaudited pro forma condensed consolidated financial data is not necessarily indicative of operating results that we would have achieved had the merger been completed as of the beginning of the period. You should not construe the pro forma data as representative of future operations. This selected unaudited pro forma condensed consolidated financial data should be read in connection with the unaudited pro forma financial statements included elsewhere in this document.

HealthWatch has allocated the total estimated purchase price of the transaction on a preliminary basis to assets and liabilities based on management's estimate of their fair market values. HealthWatch has allocated the excess of the purchase price over the fair market value of the net assets acquired to goodwill and other intangible assets. HealthWatch will update these preliminary allocations based on the results of final valuations of the assets acquired and liabilities assumed. The impact of such changes could be material.

11

HealthWatch Selected Historical Financial Data
(In Thousands, Except Shares and per Share Data)

	Years Ended June 30,				(Unaudited) Six Months Ended December 31,	
	1997	1998	1999	2000	2000	1999
Selected Financial Data:						
Revenue..............	$ 2,089	$ 1,383	$ 1,221	$ 552	$ 184	$ 322
Loss from continuing operations..........	2,189	4,084	1,749	3,640	1,938	1,077
Net Loss.............	2,189	4,084	1,749	3,474	1,938	912
Basic and diluted net loss per share(1)....	4.5	12.25	4.19	3.76	(2.51)	1.16
Basic and diluted weighted average shares..............	488,114	333,865	537,972	1,538,924	2,142,751	1,036,263
Cash and cash						

equivalents..........	$ 45	$ 854	$ 22	$ 16	52	223
Working capital.......	(404)	(340)	(1,430)	3,748	1,621	(932)
Total Assets..........	2,089	2,469	3,548	7,612	5,933	3,179
Long-Term obligations, net of current portion.............	--	--	--	--	--	--
Total Liabilities.....	1,461	1,775	1,644	541	693	1,317
Convertible preferred stock................	--	11	15	8	8	4
Total stockholders' equity (deficit).....	$ 627	$ 694	$ 1,904	$ 7,071	5,240	1,862

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(1) Calculated by dividing the loss attributable to common shares (net loss less preferred stock dividends--undeclared less amortization of beneficial conversion options on preferred stock) by the weighted average number of shares outstanding. Does not include convertible preferred stock, common stock options or warrants, or convertible debt in the loss per common share calculation, as their effect is anti-dilutive.

Halis Selected Historical Financial Data
(In Thousands, Except Shares and per Share Data)

	Year Ended December 31,			
	1997	1998	1999	2000
Selected Financial Data:				
Revenue..................	$ 10,135	$ 7,630	$ 5,082	$ 4,051
Operating Loss...........	14,848	3,910	794	704
Net Loss.................	20,502	3,149	1,445	777
Basic and diluted net loss per share(1)............	0.57	0.06	0.03	0.01
Basic and diluted weighted average shares..........	36,094,189	50,804,461	51,266,751	59,147,006
Cash and cash equivalents.	$ 1,161	$ 52	$ 14	328
Working capital..........	(1,791)	(2,458)	(2,116)	(1,045)
Total Assets.............	6,925	3,741	1,786	1,638
Long-Term obligations, net of current portion.......	145	36	209	143
Total Liabilities.........	4,208	3,918	2,669	1,896
Convertible preferred stock....................	--	--	--	--
Total stockholders' equity (deficit)...............	$ 2,727	$ (177)	$ (883)	(258)

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(1) Calculated by dividing the loss attributable to common shares by the weighted average number of shares outstanding. Does not include common stock options or warrants in the loss per common share calculation, as their effect is anti-dilutive.

Selected Unaudited Pro Forma Consolidated
Financial Data and Comparative per Share Information

for the HealthWatch/Halis Merger

The following selected unaudited pro forma condensed consolidated financial data gives effect to the merger using the purchase accounting method. The unaudited pro forma consolidated balance sheet data assumes the merger took place on December 31, 2000. The statement of operations and the pro forma adjustments described in the Notes to the Unaudited Pro Forma Condensed Combining Financial Information assumes the merger took place on July 1, 1999.

The unaudited pro forma consolidated and equivalent financial data does not reflect any cost savings or other synergies anticipated by management as a result of the merger. Also, in connection with the merger, the companies expect to incur charges for merger-related costs. Neither HealthWatch nor Halis have included the amount of these merger-related costs in their historical financial data. The pro forma earnings per share data does not reflect any of these costs. The companies may have performed differently if they had always been combined. You should not rely on the pro forma information as being indicative of the historical results the combined company would have had or the results they will experience in the future.

Selected Unaudited Pro Forma Condensed Consolidated Financial Data (1)
(In Thousands, Except Shares and Per Share Data)

	Year Ended June 30, 2000	Six Months Ended December 31, 2000
Unaudited Pro Forma Condensed Consolidated Statements of Operations Data:		
Revenue................................	$ 4,856	$ 2,260
Loss from Continuing Operations.........	4,427	2,503
Basic and diluted net loss per share....	1.78	1.35
Basic and diluted weighted average shares................................	3,788,019	4,391,846

	As of December 31, 2000
Unaudited Pro Forma Condensed Consolidated Balance Sheet Data:	
Cash and cash equivalents...............	$ 380
Working capital.........................	1,118
Total Assets............................	10,324
Long-Term obligations, net of current portion	143
Total Liabilities.......................	2,047
Convertible preferred stock.............	8
Total stockholders' equity (deficit)....	$ 8,276

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(1) For detailed information, see "Unaudited pro forma consolidated financial information" on pages 108 through 115.

HealthWatch, Halis and Pro Forma Comparative Per Share Data

The following table contains:

- Historical net loss per share and historical net tangible book value per share data of HealthWatch;
- Historical net loss per share and historical net tangible book value per share data of Halis;
- Unaudited pro forma condensed consolidated net loss per share and unaudited pro forma condensed consolidated net tangible book value per share data of the combined company giving effect to the merger; and
- Unaudited pro forma condensed consolidated net loss on a per share equivalent basis.

You should read the information in this table in conjunction with the historical financial statements of HealthWatch and Halis and the related notes contained in this joint proxy statement/prospectus and the unaudited pro forma condensed consolidated financial information and related notes also included elsewhere in this joint proxy statement/prospectus. The unaudited pro forma condensed consolidated financial information is not necessarily indicative of the net loss per share or book value per share that would have been achieved had the merger been completed as of the beginning of any period presented and should not be construed as representative of these amounts on any future dates or periods.

	Historical Data		Pro Forma Condensed
	HealthWatch	Halis	Consolidated
Net loss per share--basic and diluted for the year ended June 30, 2000	$3.76	$ .03	$1.78
Net loss per share--basic and diluted for the six months ended December 31, 2000	$2.51	$ .01	$1.35
Net tangible book value per share at December 31, 2000	$1.86	$(.01)	$ .37

- Historical net tangible book value per share is computed by dividing stockholders' equity less goodwill and other intangible assets by the number of shares of common stock outstanding at the end of the period.
- Pro forma condensed consolidated book value per share is computed by dividing pro forma stockholders' equity less goodwill and other intangible assets, including the effect of pro forma adjustments, by the pro forma number of shares of HealthWatch common stock that would have been outstanding had the merger been consummated as of June 30, 2000.

	For the Year Ended 6/30/00	For the Six Months Ended 12/31/00
Halis equivalent pro forma per share data:		
Net loss per share--basic and diluted	$.09	$.07

Net tangible book value per share................	$.05	$.02

. The Halis per share equivalent data are calculated by multiplying the HealthWatch pro forma amounts by .05, the exchange ratio to HealthWatch common stock.

RISK FACTORS

In addition to the other information contained in this joint proxy statement/prospectus, you should carefully consider the following risk factors in deciding whether to vote for the merger and other stockholder proposals. Unless the context clearly provides otherwise, these risks apply to the combined company and words such as "we" and "our" should be read to refer to the combined company after consummation of the proposed merger.

RISK FACTORS RELATING TO THE MERGER

Both companies have only a limited operating history that you may use to assess our future prospects.

While both HealthWatch and Halis have been in business for many years, their entrance into the healthcare software business was not until 1998. As such, HealthWatch and Halis have generated virtually no revenues from their information technology businesses. Our revenue and income potential are unproven and our business model is constantly evolving.

As a result of our limited operating history, our plan for growth, in particular through the formation of strategic business relationships and acquisitions, and the competitive nature of the markets in which we compete, our historical financial data is of limited value in anticipating future performance. We cannot assure you that we will be able to expand our customer base through acquisitions, or otherwise, and be able to attract new customers.

Both companies have a history of operating losses and HealthWatch expects losses to continue for the foreseeable future.

The companies have not achieved profitability and we cannot be certain that the combined company will realize sufficient revenue to achieve profitability. HealthWatch incurred net losses of $2,189,260 in the year ended June 30, 1997, $4,084,474 in the year ended June 30, 1998, $1,748,941 in the year ended June 30, 1999 and $3,474,246 in the year ended June 30, 2000. As of December 31, 2000, HealthWatch had an accumulated deficit of $30,510,031.

Halis incurred net losses of $20,502,494 in the year ended December 31, 1997, $3,148,799 in the year ended December 31, 1998, $1,444,827 in the year ended December 31, 1999 and $776,963 in the year ended December 31, 2000. As of December 31, 2000, Halis had an accumulated deficit of $38,838,966.

We plan to increase the combined company's operating expenses to expand our sales and marketing operations, broaden our customer support capabilities and continue to build our operational infrastructure. HealthWatch estimates that it will spend approximately $700,000 on its marketing, sales and customer support on an annual basis starting in fiscal year 2001, as compared to approximately $60,000 spent during the fiscal year ended June 30, 2000 and zero spent during the fiscal year ended June 30, 1999. This is only an estimate of its actual expenditures for these costs, actual costs could be more or less depending on the success it has in marketing its products. If growth in our revenues does not outpace the increase in expenses, we may not achieve or sustain profitability. We expect that the combined company will continue to lose money for the foreseeable future. Obviously, we cannot guarantee success and we may need an infusion of cash during fiscal 2001 in order for us to make any significant inroads in our business plan.

We have fixed the conversion ratio to be used in the merger, which may result in an increase or decrease in the value received by Halis stockholders.

The exchange rate for the merger is fixed at one share of HealthWatch common stock for twenty shares of Halis common stock. As such, should the market price for HealthWatch or Halis change, the value of the consideration received by Halis stockholder and paid by HealthWatch will change. For example, if the market price of HealthWatch common stock goes down, then the value received by Halis stockholders will also go

down. On March 8, 2000, the date of the merger announcement, HealthWatch's common stock had a closing price of $6.75 per share. Since that time, HealthWatch's common stock price has decreased significantly. On January 25, 2001, HealthWatch's common stock price closed at $1.25 per share. Based on that decrease, the merger consideration received by a Halis stockholder would decrease from $0.34 per share to $0.06 per share.

Our operating expenses are fixed in the short term; if our forecasted sales are delayed or do not occur, our operating results will fluctuate, which could cause our stock price to drop.

We expect that the combined company's operating results will fluctuate significantly in the future based upon a number of factors, many of which are not within our control. We have based our operating expenses on anticipated revenue growth and our operating expenses are relatively fixed in the short term. For example, our primary expenses are related to rent, overhead and personnel costs. As such, it is difficult to make changes to these costs quickly without affecting future operations. For the fiscal year ending June 30, 2001, we anticipate that the combined company will incur total rent, overhead and personnel costs of approximately $8,000,000, which represents 92% of our total costs for fiscal 2001. We may expend substantial funds and management resources during the development and sales cycle, but fail to make sufficient sales. Accordingly, our results of operations for a particular period may be adversely affected if the sales forecasted for that period are delayed or do not occur. If this occurs, the price of our common stock would likely decrease.

If the merger is completed, HealthWatch may be held responsible for Halis' outstanding lawsuits.

Halis is currently subject to four outstanding lawsuits, all of which arise out of breach of contract claims against Halis. The total of damages sought by the respective plaintiffs in these suits, including punitive damages and costs, aggregate to not less than $4.3 Million, the exact amount to be determined at trial. If HealthWatch loses or settles any of these claims after the merger, it will owe damages that may cause a reduction in available cash, a reduction in earnings, a drop in stock price and negative publicity.

If we do not integrate all aspects of our businesses successfully, we may not realize the potential benefits of the merger and the value of your investment may decrease significantly.

HealthWatch anticipates realizing cost savings, operating efficiencies and synergies from the merger of these two companies. HealthWatch will need to overcome significant issues in order to realize any benefits or synergies from the merger, including the timely, efficient and successful execution of a number of post-merger events. Key events include:

- integrating the accounting, operations and administrative functions of the two companies;
- retaining and assimilating the key technical and operational employees of each company;
- retaining the existing customers and business relationships of each company;
- developing uniform standards, controls, procedures and policies.

The successful execution of these post-merger events will involve considerable risk and may not be successful. These risks include:

- the potential disruption of the combined company's ongoing business and distraction of its management;
- unanticipated expenses related to delays in closing the merger;
- the impairment of relationships with employees and customers as a result of any integration of new management personnel; and
- potential unknown liabilities associated with the acquired business.

The combined company may not succeed in addressing these risks or any other problems encountered in connection with the merger, which could cause our stock price to drop.

16

If the costs of the merger exceed the cost savings realized from the merger, our combined financial results could be adversely affected.

If the benefits of the merger do not exceed the costs associated with the merger, including any dilution of HealthWatch stockholders resulting from issuing shares in connection with the merger, HealthWatch's financial results, including earnings per share, could be adversely affected. In connection with the merger, HealthWatch expects to incur estimated non-recurring transaction costs of $225,000 and Halis expects to incur estimated non-recurring transaction costs of $95,000. However, this is only an estimate and the costs could exceed this amount, particularly if we encounter delays. Halis and HealthWatch have already incurred many of these costs, and if the merger is not completed, HealthWatch and Halis will have incurred significant costs but will receive no benefits.

Halis' officers and directors have conflicts of interest that may influence them to support or approve the merger.

The directors and officers of Halis have continuing indemnification against liabilities that provide them with interests in the merger that are different from, or in addition to, yours. Paul W. Harrison, Chairman of the Board, CEO and President of both HealthWatch and Halis, has a conflict of interest as a result of his position with both companies. In addition, Mr. Harrison owns approximately 28% of HealthWatch's outstanding common stock, assuming the exercise of his stock options and the issuance of 250,800 shares of common stock if proposal 4 is approved by the HealthWatch stockholders to allow the conversion of Series P Preferred. Mr. Harrison also owns 12% of Halis' outstanding common stock, assuming the exercise of his stock options. Furthermore, HealthWatch owns approximately 25% of Halis' outstanding common stock, excluding the shares owned by Mr. Harrison directly. For these reasons, the directors and officers of Halis could be more likely to vote to approve the merger agreement than if they did not hold these interests. Halis stockholders should consider whether these interests may have influenced the directors and officers to support or recommend the merger.

Failure to complete the merger could negatively impact Halis' and/or HealthWatch's stock price, future business and operations.

If the merger is not completed for any reason, Halis and HealthWatch may be subject to a number of material risks, including the following:

- the price of Halis common stock and/or HealthWatch common stock may decline to the extent that the relevant current market price reflects a market assumption that the merger will be completed;

- Halis anticipates spending a total of $95,000 on costs related to the merger, such as legal and accounting and financial advisor fees, most of which have already been incurred and must be paid even if the merger is not completed;

- HealthWatch anticipates spending a total of $225,000 on costs related to the merger, such as legal, accounting fees, most of which have already been incurred and must be paid even if the merger is not completed; and

- the companies are dependent on each other's technology and potential customers may resist using either or both companies' products due to such reliance.

In response to the announcement of the merger, Halis' and/or HealthWatch's customers and strategic business relationships used in marketing and selling its products may delay or defer decisions concerning the relevant company. Any delay or deferral in those decisions by customers, resellers or suppliers could have a material adverse effect on business of the relevant company, regardless of whether the merger is ultimately completed. Similarly, current and prospective Halis and/or HealthWatch employees may experience uncertainty about their future roles with HealthWatch until HealthWatch's strategies with regard to Halis are announced or executed. This may adversely affect Halis' and/or HealthWatch's ability to attract and retain key management, sales, marketing and technical personnel.

Halis has experienced significant operating losses in the past and its auditors have given it a going concern opinion for the last two years.

Halis has experienced significant operating losses during the past several years and at December 31, 2000 had an accumulated deficit of $38,838,966. If the merger is not completed Halis will require additional debt or equity capital to sustain operations and continue its business. In addition, due to the limited resources available to it during the last two fiscal years it was unable to deploy its intended business strategy to any measurable degree. Its auditors have given it a going concern opinion for the last two years indicating that there is substantial doubt about its ability to continue as a going concern.

You may be subject to federal income tax on the HealthWatch shares you receive in the merger.

We have received opinions of legal counsel that the merger will constitute a tax-free reorganization for federal income tax purposes. However, neither HealthWatch nor Halis has requested or obtained a ruling from the Internal Revenue Service. Therefore, there is a risk that the merger may not constitute a tax-free reorganization, in which case, any gain you realize as a result of the merger may be subject to taxation. In addition, your individual financial situation may give rise to an obligation to pay taxes even if the merger is considered generally to be a tax-free transaction.

RISK FACTORS CONCERNING THE COMBINED COMPANY'S BUSINESS OPERATIONS

We are dependent on the healthcare industry's acceptance of our products.

We cannot guarantee that participants in the healthcare industry and in particular, physicians, will accept our HES System as a replacement for existing record keeping practices. Market acceptance of our product will depend upon continued growth in the use of the software products as a source of services for the healthcare industry. The acceptance of an electronic method of storing, managing and processing information by healthcare professionals will require a broad acceptance of new methods of conducting business and exchanging information. Our future financial success will depend upon our ability to attract and retain healthcare providers as customers. Our failure to achieve market acceptance would have a material adverse effect on our business, results of operations and financial condition.

We are dependent on the revenues derived from a single product.

Our primary products and services relate to the HES System. Our success is dependent on the healthcare industry's acceptance of the HES System. If the healthcare industry does not accept our HES System, our business, results of operations and financial condition would be adversely affected.

We are dependent on market acceptance of our Internet delivery method.

We are expecting that many of the smaller customers, i.e., company's with less than 100 users, of our HES System will access our products through the Internet. We cannot guarantee that participants in the healthcare industry will accept a software application accessed through the Internet as a replacement for traditional sources of these services, and to date, we have no customers using the HES System through the Internet. Market acceptance of our Internet product will depend upon continued growth in the use of the Internet generally and, in particular, as a source of services for the healthcare industry. The acceptance of the Internet for storing, managing and processing information by healthcare professionals will require a broad acceptance of new methods of conducting business and exchanging information. Our future financial success will depend upon our ability to attract and retain healthcare providers as customers. Our failure to achieve market acceptance of our Internet delivery method would have a material adverse effect on our business, results of operations and financial condition.

Halis has had limited success in marketing the HES System.

Halis first began marketing a pilot version of the HES System in 1998. However, to date it has had no sales from that effort. We believe the primary reasons for its limited success has been (i) a lack of financial resources needed to market the product and (ii) perception that Halis will not be able to service the product and customer due to such limited financial resources. However, we cannot guarantee you that we will be successful in marketing the HES System in the future. Our failure to gain market acceptance of the HES

System will have a significant adverse effect on our business, results of operations and financial condition.

Our management and major stockholders will retain substantial control, which could delay or prevent a change of control.

Our executive officers, directors and preferred stockholders have substantial control over matters requiring approval by our stockholders, such as the election of directors and approval of significant corporate transactions. This concentration of ownership might also have the effect of delaying or preventing a change in control. As of December 31, 2000, HealthWatch's executive officers and directors together beneficially owned approximately 29% of HealthWatch's outstanding common stock. Following the merger, they will beneficially own approximately 23% of HealthWatch's outstanding common stock, assuming we issue 2,300,000 shares of HealthWatch common stock to Halis stockholders in connection with the proposed merger. As of December 31, 2000, the holders of our Series C and D 8% Convertible Preferred Stock controlled approximately 52% of the total voting power of HealthWatch, excluding any unexercised options and warrants. Following the merger they will control approximately 34% of the total voting power of HealthWatch, excluding any unexercised options and warrants.

Paul Harrison, CEO and Chairman of the board of directors of HealthWatch and Halis, exercises control over approximately 544,503 shares of HealthWatch common stock, including currently exercisable options and warrants. Mr. Harrison also holds 25,080 shares of our Series P Preferred Stock, which he can convert into shares of HealthWatch common stock if proposal 4 is approved by the HealthWatch stockholders. If Mr. Harrison converts his Series P Preferred Stock, he will be issued approximately 250,800 shares of additional HealthWatch common stock. Assuming that he converts all of his Series P Preferred Stock, Mr. Harrison would control approximately 795,303 shares of HealthWatch common stock, or approximately 28% of the outstanding shares of HealthWatch common stock, prior to the merger and excluding from the total shares of HealthWatch common stock other HealthWatch securities convertible into HealthWatch common stock, including the Series A Preferred Stock, the Series C Preferred Stock, the Series D Preferred Stock, the Series P Preferred Stock not owned by Mr. Harrison, and other outstanding warrants and options of HealthWatch not owned by Mr. Harrison. Additionally, Mr. Harrison, as the designer of our technology and the HES System, is critical to the ongoing development and deployment of products utilizing our technology. As a result of such concentration of ownership and importance to the development of related software products, Mr. Harrison will have the ability to exert significant influence on the policies and affairs of HealthWatch and corporate actions requiring stockholder approval, including the election of the members of the board of directors.

HealthWatch officers and directors have conflicts of interest that may influence them to support the conversion feature of the Series P Preferred, which if approved could dilute your ownership.

In Proposal 4 contained in this joint proxy statement/prospectus, HealthWatch stockholders are being asked to approve the convertibility of the Series P Preferred into common stock at a ratio of ten shares of common stock to one share of Series P Preferred. Paul W. Harrison, Chairman, President and Chief Executive Officer of HealthWatch, owns 25,080 shares of the Series P Preferred and David M. Engert, Chief Operating Officer of HealthWatch, owns 3,177 shares of the Series P Preferred. If the proposal to allow Series P Preferred to convert to common stock is approved, Mr. Harrison will be entitled to convert his shares of Series P Preferred into 250,080 shares of HealthWatch common stock and Mr. Engert will be entitled to convert his shares of Series P Preferred into 31,770 shares of HealthWatch common stock. Other holders of Series P

Preferred may also be deemed affiliates of HealthWatch because of their family relationship with Mr. Harrison or their employment by HealthWatch. If all Series P Preferred held by all possible HealthWatch affiliates were converted as of December 31, 2000, such possible affiliates would beneficially hold 1,039,890 shares of HealthWatch common stock, or 34% of the outstanding HealthWatch common stock, including shares they currently hold and options and warrants exercisable within 60 days. This number does not include any shares of HealthWatch common stock that would be received in connection with the merger. Thus, if HealthWatch stockholders approve the conversion feature of the Series P Preferred, your ownership percentage would be diluted if such conversion feature was exercised.

If HealthWatch stockholders approve the anti-dilution provisions contained in the other HealthWatch proposals, your ownership could be diluted.

HealthWatch has submitted other proposals to its stockholders with regard to approval and ratification of certain anti-dilution provisions contained in outstanding preferred stock and related warrants (Proposals 3.A through 3.C beginning on page 121), which could dilute your ownership percentage. The anti-dilution provisions for the Series C and Series D Preferred and Bridge Warrants provide that in certain circumstances if HealthWatch issues common stock or securities convertible or exchangeable for HealthWatch common stock having a sale, conversion or exercise price less than the conversion or exercise price for the Series C and Series D Preferred and Bridge Warrants then in effect, then the conversion or exercise price of the Series C and Series D Preferred and Bridge Warrants will be automatically reset to that lower price. If HealthWatch's stockholders do not approve the Series C and Series D Preferred and Bridge Warrants anti-dilution provisions, the HealthWatch stockholders will experience no negative affect by voting against these Proposals.

The anti-dilution provisions in the Offering and Line of Credit Warrants could dilute your ownership.

HealthWatch has submitted other proposals to its stockholders with regard to approval and ratification of anti-dilution provisions contained in the outstanding Offering and Line of Credit Warrants (Proposals 3.D and 3.E). The anti-dilution provisions for the Offering and Line of Credit Warrants provide that in certain circumstances if HealthWatch issues common stock or securities convertible or exchangeable for HealthWatch common stock having a sale, conversion or exercise price less than the exercise price for the Offering and Line of Credit Warrants then in effect, then the exercise price of the Offering and Line of Credit Warrants will be automatically reset to that lower price. As such, your ownership percentage could be diluted if the anti-dilution provisions are triggered.

In addition, the Offering and Line of Credit Warrants contain provisions that if the anti-dilution provisions are not approved, the number of Offering and Line of Credit Warrants will be automatically doubled. As of December 31, 2000, if the Offering and Line of Credit Warrants were doubled, the holders would have the right to purchase 3,537,654 shares of HealthWatch common stock upon exercise of the Offering and Line of Credit Warrants. Thus, if stockholders do not approve the proposals related to the anti-dilution provisions in the Offering and Line of Credit Warrants, your ownership percentage would be diluted if the such warrants were exercised.

We hope to grow rapidly, and the failure to manage our growth could adversely affect our business.

As we continue to increase the scope of our operations, we may not have an effective planning and management process in place to implement our business plan successfully. Currently, HealthWatch is in its development stage, however, our software products are now ready for distribution and we have begun to increase the marketing and sales activities related to our products. This growth may strain our management systems and resources, which could adversely affect our operations. We will need to continue improving our financial and managerial controls and our reporting systems in order to manage such growth. In addition, we will need to expand, train and manage our growing work force. Our business, results of operations and financial condition will be materially and adversely affected if we are unable to manage and integrate our expanding operations effectively.

To grow our business, we may acquire other companies and raise capital by issuing shares of our stock, which may subject us to additional risks and will dilute your ownership.

HealthWatch's business plan contemplates the pursuit of strategic acquisitions necessary to gain market share. Specifically, HealthWatch will target companies which are currently performing management, billing and collection services for the healthcare industry. The integration of these acquired companies involves a number of special risks, as discussed above with respect to the merger. In addition, we may also sell additional shares of our stock to raise money for expanding operations. We cannot guarantee that we will be able to identify and acquire suitable candidates on acceptable terms. We also cannot promise that we will be able to arrange adequate financing, complete any transaction or successfully integrate the acquired business. In addition, HealthWatch may incur debt to finance future acquisitions, which would result in additional interest expenses and decrease net income or increase losses, as the case may be. Alternatively, or in addition to debt financing, HealthWatch may issue securities in connection with future acquisitions which would dilute the ownership of the current stockholders. Our growth strategies could be adversely affected if we are unable to successfully complete and integrate strategic acquisitions in a timely manner.

We Need to Expand our Sales and Customer Support Infrastructure.

HealthWatch and Halis are both development stage companies with relatively small sales and customer support functions. However, as we begin to market and sale our software products, we will need to expand these areas of the combined company. Competition for qualified personnel in these areas is intense. We may not be able to successfully expand our sales force, which would limit our ability to expand our customer base. As a result, any difficulties we may have in expanding our sales and marketing or customer support organizations will have a negative impact on our ability to successfully capitalize on any acquisitions we may complete.

There is no assurance that a public market for our common stock will continue to develop.

There has only been a limited public market for HealthWatch common stock with regard to trading volume and number of stockholders, resulting in fluctuations in trading prices during periods of high or low volume. HealthWatch currently has approximately 1,300 common stockholders and its daily trading volume averaged 24,275 shares for the month of December 2000. We cannot predict the extent to which investor interest in our common stock will lead to the development of an effective trading market or how liquid that market might become, especially if a large number of shares are introduced into the market upon conversion of the shares of HealthWatch's existing preferred stock.

HealthWatch is listed on the Nasdaq SmallCap Market which can be a volatile market.

HealthWatch common stock is quoted on the Nasdaq SmallCap Market and currently has a very low trading volume. Consequently, the trading of only a few shares may affect the market and may result in wide swings in price and volume. As of the record date, the 52-week high for HealthWatch common stock was $9.063 per share and the 52-week low was $0.37 per share. The market price of HealthWatch's common stock could fluctuate widely in response to the following particular factors:

- actual or anticipated variations in operating results;
- announcements by us or our competitors of new products, significant contracts, acquisitions, or relationships;
- additions or departures of key personnel;
- future equity or debt offerings or our announcements of these offerings; and
- economic conditions in the healthcare industry.

In addition, the stock market as a whole has experienced significant price and volume fluctuations, and the market prices of technology companies, particularly Internet-related companies, have been highly volatile.

21

These fluctuations have often been unrelated or disproportionate to the operating performance of individual companies. These broad market fluctuations may materially adversely affect our stock price, regardless of our operating results. HealthWatch stockholders, including Halis stockholders who receive HealthWatch common stock in the merger, may not be able to sell their shares at or above the current Nasdaq SmallCap Market price. Our results of operations during future fiscal periods might fail to meet the expectations of stock market analysts and investors. This failure could lead the market price of our common stock to decline and cause us to become the subject of securities class action lawsuits.

HealthWatch has been the subject of delisting proceedings relating to the Nasdaq SmallCap Market in the past and we cannot assure you that we will be able to maintain our listing in the future.

Our failure to continue to meet all of the Nasdaq's requirements for continued listing, compliance with which will be in part reliant on our ability to improve our business, increase revenues and improve our earnings, could result in the delisting of our common stock. In the past, Nasdaq has brought delisting proceedings against HealthWatch for violation of its continued listing policy with regard to the $1 minimum bid price per share and the $2 million net tangible asset requirements. These proceedings were ultimately dismissed because HealthWatch was able to bring itself back into compliance. However, we cannot assure you that we will be able to continue to meet Nasdaq's continued listing requirements. Delisting from the Nasdaq SmallCap Market could impact our stock price as well as make the development of a public market for our common stock less likely.

We do not intend to pay future cash dividends.

HealthWatch and Halis have never paid common stock dividends and we do not anticipate paying cash dividends on our common stock at any time in the near future. Any decision to pay dividends will depend upon our profitability at the time, cash availability and other factors. We may never pay cash dividends or distributions on our common stock. In addition, we have issued preferred stock with terms and conditions that restrict our ability to declare and pay common dividends unless all preferred stock dividends that are due and payable have been paid.

We have Broad Discretion in the Issuance of Additional Preferred Stock.

We are authorized to issue additional preferred stock. We may issue preferred stock in one or more series, the terms of which may be determined at the time of issuance by the board of directors, without further action by common stockholders. The issuance of any series of preferred stock could affect the rights of common stockholders, and therefore, reduce the value of the common stock and make it less likely that common stockholders would receive a premium for the sale of their common stock. In certain instances, existing preferred stockholders must consent to the issuance of new classes of preferred stock having rights senior to those of existing preferred stockholders or the rules of the Nasdaq SmallCap Market may require common stockholder approval for large issuances of convertible preferred stock. Preferred stock may include voting rights, preferences as to dividends and liquidation, conversion and redemption rights and sinking fund provisions. Currently, the HealthWatch Articles of Incorporation authorize the issuance of one million shares of Preferred Stock. Presently, there are 5,000 shares of 6% Series A Preferred Stock outstanding, 4,000 shares of Series C 8% Convertible Preferred Stock outstanding, 74,130 shares of Series D 8% Convertible Preferred Stock outstanding and 66,886 shares of Series P Preferred Stock outstanding. We are submitting a proposal in this joint proxy statement/prospectus to the HealthWatch stockholders to increase authorized preferred stock from one million to fifteen million shares (See proposal 2.B on page 118).

We will depend on the efficient operation of the Internet, other networks and systems of third parties; if they do not operate efficiently, we will not be able to effectively provide our products and services.

We will depend on the efficient operation of network connections from our customers and their data processing vendors to our systems. HealthWatch does not currently have any third parties under contract to

provide such network connections. Further, portions of our revenue are dependent on continued usage by end-users of Internet services and their connections to the Internet. For the fiscal year ending June 30, 2001, management forecasted that approximately 7% of our total revenue would be derived from our Internet applications, based on our sales models. However, to date HealthWatch has had no sales or earned any fees from use of the HES System through the Internet. Each of these connections, in turn, depends on the efficient operation of web browsers, Internet service providers and Internet backbone service providers, all of which have had periodic operational problems or have experienced outages. We would be unable to provide a real time connection to these systems if they experienced any operational problems or outages and we would be unable to process transactions for end-users, resulting in decreased revenues. In addition, any system delays, failures or loss of data, whatever the cause, could reduce customer satisfaction with our products and services and harm our sales.

Competition from third parties could reduce or eliminate demand for the combined company's products and services.

The market for Internet services is highly competitive, and we expect that competition will intensify in the future. We may not be able to compete successfully against our current or future competitors and, accordingly, we cannot be certain that we will be able to expand the number of our customers and end-users, or retain our current customers or third-party service providers. Many of our current and potential competitors have longer operating histories and may be in a better position to produce and market their services due to their greater financial, technical, marketing and other resources, as well as their significantly greater name recognition and larger installed customer bases.

Security breaches could damage our reputation and business.

The combined company's networks may be vulnerable to unauthorized access, computer viruses and other disruptive problems. We transmit confidential healthcare information in providing our services. Users of Internet and other electronic commerce services are concerned about the security of transmissions over public networks. Therefore, it is critical that our facilities and infrastructure remain secure and that our facilities and infrastructure are perceived by the marketplace to be secure. A material security breach affecting the combined company could damage our reputation, deter healthcare providers from purchasing our products or result in liability to us. Further, any material security breach affecting our competitors could affect the marketplace's perception of Internet services in general and have the same effects.

Concerns over security and the privacy of users may inhibit the growth of the Internet and other online services generally, especially as a means of conducting healthcare transactions. Any well-publicized compromise of security could deter people from using the Internet or using us to conduct transactions that involve transmitting confidential healthcare information. We may need to expend significant capital or other resources protecting against the threat of security breaches or alleviating problems caused by security breaches. Although we intend to continue implementing security measures, the measures that we implement may be circumvented in the future. Eliminating computer viruses and alleviating other security problems may result in interruptions, delays or cessation of service to users accessing web sites that deliver our services, any of which could harm our business. Our failure to respond to rapid changes in the market for Internet services could cause us to lose revenue and harm our business.

Newly introduced products may contain undetected or unresolved defects.

Our products are complex, integrated software programs that involve many different applications that must communicate with each other. As a result, any new or enhanced products we introduce may contain undetected or unresolved software or hardware defects when they are first introduced or as new versions are released. In the past, we have discovered minor errors in our products and it is possible that design defects will occur in new products. These defects could result in a loss of sales and additional costs, as well as damage to our reputation and the loss of relationships with our customers.

If we Fail to attract and retain experienced personnel and senior management, our ability to grow could be harmed.

We believe that our future success will depend in large part upon our continued ability to identify, hire, retain and motivate highly skilled employees, who are in great demand. In particular, we believe that the combined company must expand its research and development, marketing, sales and customer support capabilities in order to effectively serve the evolving needs of our present and future customers. Competition for these employees is intense and due to our operating losses in the past and the concern regarding Nasdaq technology companies in general, we may not be able to hire additional qualified personnel in a timely manner and on reasonable terms. In addition, our success depends on the continuing contributions of our senior management and technical personnel, all of whom would be difficult to replace. The loss of any one of them could adversely affect our ability to execute our business strategy. Most of our employees, including Paul W. Harrison, are not currently bound by an employment agreement. Furthermore, we do not yet have "key person" life insurance policies covering any of our employees.

Our limited ability to protect our proprietary technology may adversely affect our ability to compete, and we may be found to infringe on proprietary rights of others, which could harm our business.

Our future success and ability to compete depends in part upon our proprietary technology. None of our technology is currently patented. Instead, we rely on a combination of contractual rights and copyright, trademark and trade secret laws to establish and protect our proprietary technology. We generally enter into confidentiality agreements with our employees, consultants, resellers, customers and potential customers, limit access to and distribution of our source code, and further limit the disclosure and use of other proprietary information. We cannot assure you that the steps we take in this regard will be adequate to prevent misappropriation of our technology or that our competitors will not independently develop technologies that are substantially equivalent or superior to our technology. Despite our efforts to protect our proprietary rights, unauthorized parties may attempt to copy or otherwise obtain or use our products or technology. Monitoring unauthorized use of our products is difficult, and while we are unable to determine the extent to which piracy of our software products exists, we expect software piracy to be a persistent problem. In addition, the laws of some foreign countries do not protect our proprietary rights to the same extent as do the laws of the United States.

We are also subject to the risk of claims and litigation alleging infringement of the intellectual property rights of others. Third parties may assert infringement claims in the future with respect to our current or future products. Any assertion, regardless of its merit, could require us to pay damages or settlement amounts and could require us to develop non-infringing technology or pay for a license for the technology that is the subject of the asserted infringement. Any litigation or potential litigation could result in product delays, increased costs or both. In addition, the cost of litigation and the resulting distraction of our management resources could adversely affect our results of operations. We also cannot assure you that any licenses for technology necessary for our business will be available or, if available, that we can obtain these licenses on commercially reasonable terms.

RISK FACTORS CONCERNING THE COMBINED COMPANY'S INDUSTRY

Governmental regulation of healthcare privacy issues may result in additional expenditures and adversely affect our business.

The Federal Trade Commission and state governmental bodies have been investigating the confidentiality and privacy policies and practices of healthcare Internet companies and Internet companies in general, and may impose regulations. In addition, proposed privacy standards for handling individually identifiable health information that is transmitted or stored electronically were issued by the Department of Health and Human Services on November 3, 1999 and our platform and applications must comply with the final regulations. Finally, industry groups are also proposing various privacy and ethics standards in an effort to maintain self-regulation. We will likely incur additional expenses regarding privacy practices and policies. Any such policies and practices, whether self-imposed or imposed by government regulation, could affect the way in which we are allowed to conduct our business, especially those aspects that involve the collection, use and access to personal information and medical records, and could have a material adverse effect on our business, results of operations and financial condition.

The healthcare industry is subject to extensive government regulation.

Participants in the healthcare industry are subject to extensive and frequently changing regulation at the federal, state and local levels. Some of the laws and regulations relate to payment and other relationships with third party billing and collection agents as well as regulating computer software intended for use in the healthcare setting. The impact of regulatory developments in the healthcare industry is complex and difficult to predict. We cannot assure you that we will not be materially adversely affected by existing or new regulatory requirements or interpretations. These requirements or interpretations could also limit the effectiveness of the use of the Internet for the methods of healthcare e-commerce we are developing or even prohibit the sale of our products or services. Healthcare service providers, payors and plans are also subject to a wide variety of laws and regulations that could affect the nature and scope of their relationships with us. Laws regulating health insurance, health maintenance organizations and similar organizations, as well as employee benefit plans, cover a broad array of subjects, including confidentiality, financial relationships with vendors, mandated benefits, grievance and appeal procedures, and others. State and federal laws have also implemented so-called "fraud and abuse" rules that specifically restrict or prohibit certain types of financial relationships between us or our customers and healthcare service providers, including physicians and pharmacies. Laws governing healthcare providers, payors and plans are often not uniform between states, and could require us to undertake the expense and difficulty of tailoring our business procedures, information systems or financial relationships in order for our customers to be in compliance with applicable laws and regulations. Compliance with such laws could also interfere with the scope of our services, or make them less cost-effective for our customers.

The demand for the combined company's products and services could be negatively affected by reduced growth of Internet commerce or delays in the development of the Internet infrastructure.

Our future success depends heavily on the Internet being accepted and widely used for commerce in the healthcare industry. For the fiscal year ending June 30, 2001, we estimate that the combined company will derive 7% of its revenue from its applications that are accessed through the Internet. However, to date, HealthWatch has had no sales or earned any fees from use of the HES System through the Internet. If Internet commerce does not continue to grow or grows more slowly than expected, our business will suffer. There are a number of reasons that consumers and businesses may reject the Internet as a viable commercial medium for healthcare transactions in particular. These reasons include potentially inadequate network infrastructure, costs of implementing new systems, security concerns, reliability and quality problems, limited funds available for new spending due to healthcare cost reductions and investments already made in legacy systems. Even if we develop the required infrastructure, standards, protocols or complementary products, services or facilities, we may incur substantial expenses adapting our solutions to changing or emerging technologies.

THE SPECIAL MEETINGS

General

The special meeting of HealthWatch stockholders will be held at 10:00 a.m., local time, on March 29, 2001 at The W At Perimeter Center Hotel, 111 Perimeter Center West NE, Atlanta, Georgia 30346 for the purposes set forth in the Notice of the HealthWatch special meeting. The special meeting of Halis stockholders will be he