MDRANGER

Calculating Opportunity Cost in Physician Contracts

Calculating Opportunity Cost in Physician Contracts

Should a physician contractor be paid based on market benchmarks or on foregone clinical income, also called 'opportunity cost'? How influential should opportunity cost be when considering payment rates? Are there risks to opportunity-based payments? Should you pay a neurosurgeon the same as a pediatrician for the same work?

We've seen hospital administrators struggle to determine what is appropriate for their organization. The truth is that opportunity cost can be difficult to measure and document.

Defining Opportunity Cost

Opportunity cost is a determination of value based on the value of an alternate use of the same resources, which for our purposes is a physician's time. For physicians contracting with a hospital to take emergency coverage shifts or to spend hours a month on administrative tasks, the opportunity cost is generally considered to be the income lost from their private practice while on call or performing non-clinical duties.

When to Use Opportunity Cost

For call coverage and administrative services contracts, opportunity cost may be appropriate to consider if a physician's activities are restricted during a coverage shift or administrative duties are required during a time when she would typically be able to see patients. The physician's opportunity cost would be the net professional fees billed less the cost of overhead for the amount of time performing the contracted duties.

Opportunity cost shouldn't be factored into every situation—even if the physician's specialty is generally higher paid. A physician who has slowed down her practice because she is close to retirement should not get a higher hourly rate to serve as a medical director simply because she's a neurosurgeon.

Additionally, specialty may not be important for some administrative positions, such as directors of EMR implementation, quality initiatives, utilization review, or chief of staff. For these types of positions, opportunity cost generally isn't factored into contract rates because it's not necessary to have a physician of a high cost specialty in the role.

Potential Risks

The Office of the Inspector General advises in Opinion 07-10 to use caution when considering the opportunity cost:

> Moreover, depending on the circumstances, problematic compensation structures that might disguise kickback payments could include, by way of example: (i) 'lost opportunity' or similarly designed payments that do not reflect bona fide lost income…

As with other physician contracts, it is important to document the fair market value parameters used when opportunity cost has been factored. Include the calculations used to determine the value as well as why opportunity cost is important to the particular situation. Although the OIG opinion cited was written about an emergency call agreement in question, the OIG's guidelines can be reasonably applied to other types of physician contracts.

Despite the risks, it doesn't mean that you shouldn't consider opportunity cost when there is valid justification. However, exercise caution and don't forget to document all the steps taken in your decision-making process.

Want to discuss the use of opportunity cost in physician contracts with an expert? Email inquiries@mdranger.com or call the office at (650) 692-8873.