

# Understanding the Cost of Compliance: A Framework

by Austin Locke and Chelsea Barnes

In the Food and Beverage (F&B) industry, compliance to an ever-changing landscape of regulations is a minimum requirement to survive. Value chains span an increasing number of markets, uncertain geopolitical times obscure the impact of both existing and proposed regulation and increased consumer scrutiny brings transparency and compliance to the forefront of purchasing decisions. Furthermore, the number of food safety recalls continues to climb, seeing a 22% surge from 2015 to 2016<sup>1</sup>, resulting in billions of dollars in associated costs for the industry. Amongst all this complexity, how can large F&B organizations understand how much they're spending on regulatory compliance and whether that investment is sufficient and effectively allocated?

## Cost of Compliance: Definition

To perform this assessment, an organization must first understand that the cost of compliance (CoC) is the sum of costs to comply with existing regulation (Maintenance Cost), conform to new regulations and trends (Conformance Cost) and to make amends when regulations are not met (Non-conformance Cost). Many organizations are all too familiar with recalls and their immense cost, averaging \$10 million per incident<sup>2</sup>. However, as illustrated by this definition, the cost of compliance is far more expansive than the costs incurred when failing to adhere to existing laws.



Figure 1: Cost of Compliance Categories

## Cost of Compliance: Framework

To provide additional context and definition to this cost equation, we have developed the Cost of Compliance Framework. In this framework, we break down each cost category into one or more sub-categories which define the specific investments that companies can trace, assess and improve upon. For example, the cost to conform to new regulations and trends (Conformance Cost) is the sum of five costs – scanning, improvement initiatives, impact assessment, systems and processes and training – commonly incurred in F&B organizations. These sub-categories and their definitions are shown in Figure 2.

Cost Category	Definition
<b>Maintenance</b>	<b>Cost to maintain compliance to existing regulation</b>
Verification	Cost to ensure product meets regulatory standards (regulatory checks, testing and reporting)
Supplier Evaluation	Cost to assess, approve and audit suppliers
<b>Conformance</b>	<b>Cost to conform to new regulations and adjust to industry trends</b>
Scanning	Cost to proactively look for and understand future regulation
Improvement Initiatives	Cost of corporate improvement programs related to regulatory compliance
Impact Assessment	Cost to understand new regulation and its impact on the business
Systems and Process	Cost to implement systems or processes to conform to regulation
Training	Cost to train workforce on how to execute new regulations
<b>Non-Conformance</b>	<b>Costs assumed when the business fails to conform to regulations</b>
Recalls (Includes fines/fees)	Cost to remove product from market/satisfy penalties when it failed to meet regulatory requirements

Figure 2: Cost of Compliance Framework

As illustrated by the CoC framework, there are several costs that organizations need to monitor to truly understand what they are spending to comply to regulation. In subsequent parts of this series, we focus on each of the major cost categories, providing additional context and examples for each sub-category. We will also explore what a large F&B company might spend in each area and where industry leaders are investing for success.

### Works Cited

1. Maberry, Tiffany. A Look Back at 2016 Food Recalls. Food Safety Magazine. February 7, 2017.
2. Grocery Manufacturers Association. Recall Execution Effectiveness: Collaborative Approaches to Improving Consumer Safety and Confidence. May 2010.

Originally published on February 2nd, 2018

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