

## Inventory and Cost of Goods Sold

### Inventory

The value of goods held for resale. Reported as an asset on the Balance Sheet.

### Cost of Goods Sold

The value of goods sold during the reporting period. Reported as a deduction from Income on the Income Statement.

### Why record inventory and then move it to Cost of Goods Sold (COGS)?

There is no way to know if your business is making money if you immediately expense all your purchases. (Unless you sell all of your inventory every day.) Look at your Income Statement if you “expense” all your purchases immediately.

Fayetteville Computer Depot Income Statement For the Period 4/1/2022 - 4/30/2022	
<u>Revenue</u> Computers Sold (3 @ \$150)	\$450
<u>Cost of Goods Sold</u> Computers Purchased (10 @ \$75)	\$750
<u>Gross Margin</u>	<b>-\$350</b>

It appears that you made no money from selling your product. Because it ignores that you have 7 computers left to sell.

So let's record our purchases to Inventory and then move them to COGS when they are sold.

Fayetteville Computer Depot Income Statement For the Period 4/1/2022 - 4/30/2022	
<u>Revenue</u> Computers Sold (3 @ \$150)	\$450
<u>Cost of Goods Sold</u> Cost of Computers (3 @ \$75)	<b>\$225</b>
<u>Gross Margin</u>	\$225

Fayetteville Computer Depot Balance Sheet As of 4/30/2022	
<u>Current Assets</u>	
Cash	450
<u>Inventory (7 @ \$75)</u>	<b>525</b>
Total Current Assets	\$1,125

From this, you can determine that you made money (\$225) and you still have 7 computers left to sell.

## Determining Price of Product

You import apples and the price of the apples is only a small portion of the price of the product.

Description	Price per unit	Total price	Cost per Apple
Apples (40 per case)	20 cases @ \$52.75 per case	\$1,055	\$1.32
Shipping	\$60 per case	\$1,200	\$1.50
Duty	\$20 per case	\$400	\$0.50
Total		\$2,655	\$3.32

Imagine if you did not account for your shipping costs and duty-- you would assume your costs were \$1.32 per apple when they are actually \$2 more per apple.

Again, let's look at your Income Statement if you did not account for Inventory and "expensed" all your purchases and the related shipping costs.

Fayetteville Fruit Stand Income Statement For the Period 4/1/2022 - 4/30/2022	
<u>Revenue</u> Apples Sold (8 @ \$8)	\$64
<u>Cost of Goods Sold</u>	
Apples Purchased (20 Cases @ \$52.75 per case)	1,055
Shipping	1,200
Duty	400
<u>Total Cost of Goods Sold</u>	\$2,655
<u>Gross Margin</u>	<b>-\$2,591</b>

That result is not good. And it's not accurate. So let's account for Inventory.

Fayetteville Fruit Stand Income Statement For the Period 4/1/2022 - 4/30/2022	
<u>Revenue</u> Apples Sold (8 @ \$8)	\$64.00
<u>Cost of Goods Sold</u>	
<b>Cost of Apples Sold (8 @ \$3.32)</b>	<b>26.56</b>
<u>Total Cost of Goods Sold</u>	26.56
<u>Gross Margin</u>	\$37.44

Fayetteville Fruit Stand Balance Sheet As of 4/30/2022	
<u>Current Assets</u>	
Cash	64.00
<b>Inventory (792 @ \$3.32)</b>	<b>2,629.44</b>
Total Current Assets	\$2,693.44

This Income Statement looks much better and is a more accurate measure if you made money.

**WARNING:** Don't let Inventory sit on your Balance Sheet that is not sellable. What if those 792 apples rot? Does it help you understand how your business is performing if you keep the apples in Inventory on the Balance Sheet? NO! So you need to periodically count your inventory and write-off bad products. Let's look at the Income and Statement and Balance Sheet for that scenario.

<b>Fayetteville Fruit Stand Income Statement For the Period 4/1/2022 - 4/30/2022</b>	
<u>Revenue</u>	
Apples Sold (8 @ \$8)	\$64.00
<u>Cost of Goods Sold</u>	
Cost of Apples Sold (8 @ \$3.32)	26.56
Rotten Apples (Spoilage)	2,629.44
<u>Total Cost of Goods Sold</u>	2,656.00
<u>Gross Margin</u>	\$-2,592.00

<b>Fayetteville Fruit Stand Balance Sheet As of 4/30/2022</b>	
<u>Current Assets</u>	
Cash	64.00
Inventory	0.00
Total Current Assets	64.00

So don't let your Balance Sheet become a dumping ground of poor accounting that skews your Income Statement.