

FINANCE AT A GLANCE

Computing Cost of Goods Sold (4)

Lesson 25

The **Cost of Goods Sold** for a manufacturing business, just like for a trading business, is the cost of items sold to customers. However, since a manufacturer makes the products, the Cost of Goods Sold must include **Manufacturing Costs**.

A manufacturing business has three inventories:

1. raw materials inventory
2. good-in-process inventory (goods processed only up to a certain stage prior to completion)
3. finished goods inventory

For each of these inventories, the amount at the start of the period under consideration plus whatever is added to them, minus what is left at the end of the period is that what goes into the Cost of Goods Sold.

To the beginning inventory of raw materials, purchases are added. This becomes the amount available for production. At the end of the period, the ending inventory is determined. The amount available for production less the ending inventory becomes the **Direct Materials Used**.

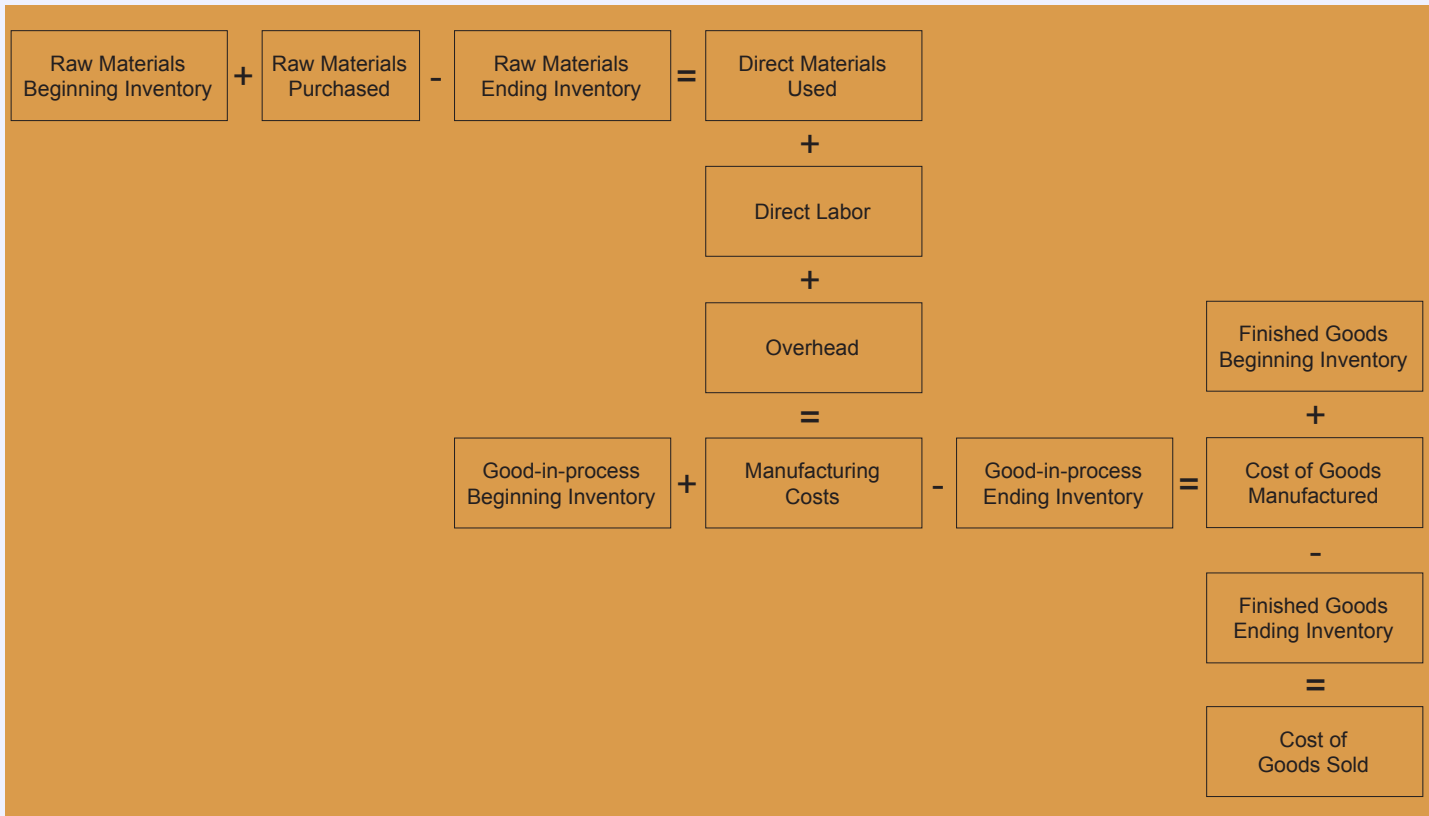
The manpower cost that is directly traceable to production is the **Direct Labor** cost.

Expenses on utilities and maintenance of factory facilities, as well as insurance and taxes of such facilities, and their depreciation make up the **Overhead** costs.

Direct Materials Used, Labor and Overhead comprise the Manufacturing Costs.

Manufacturing Costs are added to the beginning inventory of good-in-process. From this total, the ending value of good-in-process is deducted to arrive at **Cost of Goods Manufactured**.

The Cost of Goods Manufactured plus the beginning inventory of finished goods comprise the total cost of goods available for sale. The ending inventory of finished goods subtracted from the total cost of goods available for sale yields the Cost of Goods Sold.



There are different methods involved in the valuation of the three inventories. One method may be acceptable in one country, and unacceptable in another. There are also complex issues in the assignment of costs to the good-in-process and finished goods. A detailed discussion of these and other considerations is not necessary at this stage. However, it is hoped the foregoing discussion sheds light on what is involved in the Cost of Goods Sold for a manufacturing business.

Until then,

Info Solutions International