COGS vs SG&A

The cost of goods sold (COGS), and selling, general, and administrative (SG&A) expenses are completely separate sets of costs that a business incurs.

Quick links

COGS and SG&A values are recorded as separate items on the income statement.

Profit Frog is the leading financial planning and analysis (FP&A) software specifically designed to aid small businesses. We simplify COGS calculations and make them actionable so you can improve profitability.

What Is The Cost Of Goods Sold?

The cost of goods sold, sometimes termed cost of sales, are direct costs associated with producing goods or providing a service. They include raw materials and direct labor.

Generally accepted accounting principles (GAAP) defines COGS as the general cost of producing items sold during a selected period.

Our COGS definition: all direct costs involved in manufacturing a product or delivering a service.

COGS for Manufacturing Businesses

COGS, also referred to as cost of sales, measures the direct costs of producing goods. It includes all costs associated with manufacturing: transportation costs, direct material costs, and any other direct expenses.

COGS for Service Businesses

If you own a service business (for example a locksmith company), COGS will include business expenses involved in providing the service: direct labor, tools, and parts used, and transportation costs.

COGS for SaaS Companies

Since SaaS businesses provide their customers with software instead of physical goods, calculating COGS is quite different. Because SaaS companies have no "goods sold," some accountants refer to this metric as cost of sales or cost of revenue.

Tracking SaaS COGS accurately is important for accounting and modeling. Our SaaS business forecasting software includes a handy cost of goods sold calculator to make COGS—and all other aspects of budgeting and forecasting—much easier.

What is SG&A?

Selling, general and administrative, also known as SG&A, is a category for operating expenses that are not directly related to manufacturing the goods or delivering a service; non-COGS costs. SG&A is an essential part of increasing company profitability and calculating its breakeven point.

SG&A is never included in COGS; instead, it includes all non-production costs. It is listed in the expenses section of your financial statement.

Selling, general and administrative is one of the first places a manager will analyze when looking to reduce any redundancies.

What's Included in COGS vs SG&A?

COGS includes all costs associated with manufacturing or developing a product. For example, if a company is selling a physical product, the cost of goods sold will include transportation costs, direct material costs, and any other direct expenses.

Businesses should have these costs included in COGS:

1. Product storage costs
2. Product transport costs
3. Tools and parts used in production
4. Raw materials
5. Factory labor costs

If you own a service business, the cost of goods sold will include business expenses involved in providing the service; direct labor, tools and parts used, and transportation costs.

When it comes to selling, general and administrative expenses, here are three types of expenses listed under the SG&A category:

1. Indirect selling expenses
2. General expenses
3. Administrative costs

Sometimes, non-operating expenses can also be listed under SG&A.

Typical SG&A expenses include:

Selling expenses:

- Sales and marketing
- Advertising and promotional cost
- Distribution costs

General expenses:

- Rent, utilities
- Insurance
- Technology costs
- Office supplies
- Equipment costs

Administrative Expenses:

- Salaries of employees
- Consulting fees
- Accountants
- IT professionals
- Lawyers
- Administrative staff

The most common mistake business owners make is putting distribution costs under COGS. Distribution costs are not included in COGS, they are a part of SG&A.

COGS Formula vs SG&A Formula

Traditional COGS and SG&A formulas are backwards-looking. But there's a better, real-time, way: the Profit Frog way.

Traditional COGS Formula

The traditional, inventory-based COGS formula retrospectively calculates COGS after an accounting period has closed. This doesn't give much actionable insight to the entrepreneur trying to make real-time decisions.

COGS = Beginning Inventory + Purchases during the period – Ending Inventory

- Beginning inventory: a business's inventory at the beginning of an accounting period.

- Purchases: the cost incurred to produce a good or service during an accounting period.
- Ending inventory: the inventory remaining at the end of an accounting period.

All inventory that is sold will be shown as sales. The items that didn't get sold in the previous year become part of the beginning inventory for the upcoming year. If the business makes or purchases additional products, they will be added to the inventory.

There's a better way to track COGS (and SG&A too, for that matter).

Traditional SG&A Formula

SG&A Expense = Operating income (earnings before interest and taxes, or EBIT) – Gross profit

The SG&A expense figure should be negative, given that it is a debit on the income statement.

SG&A expenses are simple to calculate once you've classified them into the correct categories. SG&A is usually calculated when creating an income statement.

Calculating SG&A and COGS with Profit Frog

Profit Frog takes a real-time approach to COGS as well as SG&A. Business owners plug in all their costs, including SG&A, into their dashboard and see a current snapshot of their business's health.

No waiting until the end of an accounting period: they have up-to-the-moment visibility into the real drivers of their business. Then, they can forecast COGS, SG&A, profit margins, and more into the future by manipulating variables and creating different scenarios. This is known as scenario planning and it helps our customers stay ahead of the curve.

With Profit Frog, business owners don't need to stress about calculating costs. We give you a clear view of what's going on in your business and where you can increase profitability.

SG&A vs COGS Frequently Asked Questions

How to calculate SG&A sales ratios?

The SG&A ratio is the relationship between SG&A and revenue. The SG&A ratio measures the percentage of every earning a company makes that is impacted by SG&A.

SG&A Ratio = SG&A / Total Revenue

The SG&A ratio measures what percentage of each dollar earned by a company is impacted by SG&A.

Let's say that your company has $8 million in SG&A and $30 million in total revenue.

SG&A Ratio = $8,000 / $30,000 = 26%

Having a 26% ratio means that for every dollar of revenue incurred, $0.26 is spent on SG&A expenses.

How to calculate COGS percentage?

To calculate your COGS percentage, just divide the cost of goods sold by total revenue and then times the resultant number by 100.

COGS percentage formula:

(COGS / Total revenue) X 100

COGS Percentage Example

A glove store has spent $900 on inventory items during a fiscal quarter and had $300 worth of inventory on hand at the end of the quarter. He sold 100 gloves for $50 per pair during the quarter.

1. First, calculate COGS: 1000 + 900 – 300 = 1600
2. Calculate total sales: 100 x 50 = 5,000
3. Calculate the COGS percentage: 1600 / 5,000 = 0.32
4. Times by 100: 0.32 x 100 = 32

The glove maker has a COGS percentage of 32%.

What is the difference between operating expenses and SG&A?

Selling, general and administrative expenses include all costs that are non-production. SG&A is often used as a synonym for OPEX, yet they are sometimes shown as separate line items on income statements.

SG&A expenses are usually ones associated with overhead; they can't be directly tied to production. OPEX has the same parameters as SG&A.

What are the limitations of COGS?

Inventory-based COGS accounting systems are traditionally used in larger companies. Usually motivated by a desire to impress investors (or potential investors), accountants can manipulate cost of goods sold via any of the following:

- Not writing off obsolete inventory
- Fudging the amount of inventory at the end of an accounting period
- Overstating discounts
- Overstating returns to suppliers
- Valuing end-of-period inventory at more than the actual value

Because the value of inventory can be artificially inflated, the cost of goods sold can be under-reported, which can show artificially-inflated net income.

Profit Frog customers typically aren't subject to the same COGS limitations for the following reasons.

1. Our average customer is a bootstrapped Main Street business, not a VC-funded startup
2. We don't use backwards-looking inventory valuation systems for calculating COGS; instead, we use a real-time approach that helps you stay ahead of the curve

Get started with your free Profit Frog trial today.

Are COGS variable or fixed costs?

The COGS figure consists mostly of variable costs. Some companies consider the cost of goods to include all of their variable expenses, and put all fixed expenses under overhead costs (operating expenses).

Most common fixed costs included in the cost of goods sold are equipment depreciation costs and salaries for personnel responsible for product quality.

Together, variable and fixed costs make up the total expenses of running a business.

An administrative cost is commonly mistaken for a variable cost; it is a fixed cost, and a part of SG&A expenses, or OPEX.

Check our guide on the differences between COGS and OPEX.

Are SG&A expenses tax deductible?

As with any other business expense, SG&A expenses are tax deductible.

Is COGS included in operating expenses?

Cost of goods sold and operating expenses are completely separate categories of costs that companies incur. COGS and OPEX values are recorded as separate items on the income statement.

Operating expenses and COGS are mutually exclusive. If an expense is COGS it is not OPEX, and vice versa.

Operating expenses include:

1. Utilities
2. Rent
3. Legal costs
4. Insurance costs
5. Office supplies
6. Human resource costs
7. Interest paid on debt
8. Administrative expenses
9. Any other indirect cost (expense not directly related to revenue generation)

Selling, general, and administrative expenses (SG&A) are included in OPEX; SG&A are fixed costs. Operational costs are linked to the administration and maintenance of a business on a daily basis.

Operating expenses vs cost of goods sold calculations are difficult and confusing for most small business owners. Profit Frog also offers profit modeling software that guides you to optimize your profit.

Are marketing costs a part of COGS?

Business marketing refers to actions a business takes to attract more customers to the services or products they offer. Since marketing doesn't relate to product production or delivering a service, marketing can't be included in COGS.

What are the most important COGS metrics?

When it comes to tracking your businesses COGS metrics, the numbers that matter the most are:

- Production costs
- Direct labor
- Raw materials
- Inventory expenses

About Profit Frog

Profit Frog is the leading budgeting and forecasting software specifically designed to eliminate complexity for small businesses. Where other FP&A software solutions focus on complex forecasting of cash flows and other factors, Profit Frog strips forecasting down to the thing that matters most: profitability. Our profitability modeling solution allows you to quickly assess the health of your business, and look into the future to understand how all of your variables will affect future profitability as you adjust them. Armed with this knowledge, you can chart a path to maximum profit.

Get started with your free Profit Frog trial today!

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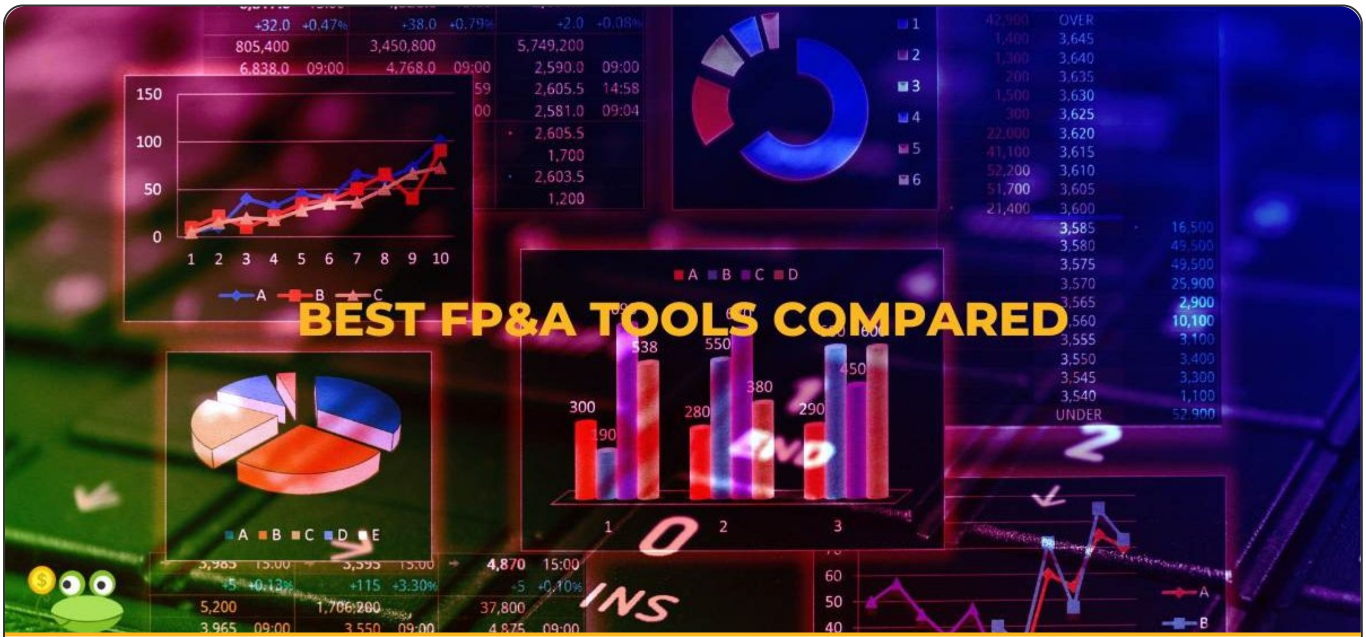

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