COST OF GOODS SOLD (SCHEDULE C, PART III)

Yellow cells are yours; lines 40 and 42, gross profit and margin follow by formula. Sample: the illustration in IRS Publication 334.

Line	Item	Amount	Form 1125-A line
35	Inventory at beginning of year	$37,845.00	1
36	Purchases less cost of items withdrawn for personal use	$283,250.00	2
37	Cost of labor (not amounts paid to yourself)	$0.00	3
38	Materials and supplies	$0.00	-
39	Other costs (containers, freight-in, manufacturing overhead)	$0.00	5 (4: section 263A)
40	Add lines 35 through 39: goods available for sale	**$321,095.00**	6
41	Inventory at end of year	$32,955.00	7
42	**COST OF GOODS SOLD: line 40 minus line 41**	**$288,140.00**	8

	Gross profit	Amount	
	Net sales (gross receipts minus returns and allowances)	$385,060.00	
	Gross profit: net sales minus cost of goods sold	**$96,920.00**	
	Gross margin: gross profit / net sales	**25.17%**	
	Cost of goods sold as a share of net sales	**74.83%**	

Pub. 334 example: $37,845 + $283,250 - $32,955 = $288,140; $385,060 - $288,140 = $96,920 gross profit (25.17%). Line descriptions: IRS Publication 334, chapter 6, and Form 1125-A (Rev. November 2024).

Small business taxpayers (26 U.S.C. 471(c)) need not keep inventories if average annual gross receipts of the 3 prior years are $32,000,000 or less for tax years beginning in 2026 (Rev. Proc. 2025-32) or $33,000,000 for 2027 (Rev. Proc. 2026-35) and they are not tax shelters.

FIFO, LIFO AND AVERAGE COST

Enter the units sold and up to five lots in the order bought, beginning inventory first. Single-period illustration; tax LIFO keeps yearly layers.

Units sold in the period	300

Lot (oldest first)	Units	Cost per unit	Lot cost	FIFO units sold	LIFO units sold
1: beginning inventory	100	$10.00	$1,000.00	100	0
2: purchase	200	$11.00	$2,200.00	200	150
3: purchase	150	$12.00	$1,800.00	0	150
4: purchase			$0.00	0	0
5: purchase			$0.00	0	0
Available for sale	**450**		**$5,000.00**	**300**	**300**

Method		Cost of goods sold	Ending inventory		
FIFO (first in, first out)		**$3,200.00**	$1,800.00		
LIFO (last in, first out)		**$3,450.00**	$1,550.00		
Average cost		**$3,333.33**	$1,666.67		

Check: units sold are within units available

IRS Publication 538: FIFO assumes the items bought first are sold first; LIFO assumes the items bought last are sold first; in times of rising prices LIFO gives a larger cost of goods sold and a lower closing inventory. LIFO is adopted on Form 970 with the timely filed return for the first LIFO year.

Average cost = total cost / total units x units sold. Sample: 300 units sold give FIFO $3,200.00, LIFO $3,450.00, average $3,333.33 (computed).