

## Pricing Decisions and Borrowing Costs under International Accounting Standard 23 in Jordanian Industrial Corporations

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### Abstract

This study investigates how corporations borrowing costs (BC) under IAS 23 will be impacted on pricing decisions (PD) in industrial corporations, Study population of Jordanian industrial corporations, listed on the Amman Stock Exchange for the year 2015 is made up, the number of these corporations stood at 92 industrial corporations, study sample including all corporations availability information to calculate the variables of study during the study period, the number 70 industrial corporation, used three, depending variables, that is pricing decisions, cost-plus price (CPP), contribution margin Price (CMP), and target costing price (TCP), the independent variable is (BC), this, the variables because the increase of dependence on the borrowing lead to increase the cost of finance and loading of corporations for expenses, that effect on net profit realize and loading the service or product for (BC), thus impact on service or product price. Hilton (2005). The simple regression used to test hypotheses. This study indicated to an impact on profit when the capitalization of (BC) for using (CPP) and (CMP) method. There is no impact on profit for using the (TCP) method, but leading to increase competitive advantage a to product, increase the team ability and benefits of the product.

**Keywords:** Pricing decision making, Cost-Plus Price, Contribution Margin Price, Target Costing Price, Borrowing Costs.

### INTRODUCTION:

Many major factor effects on the (PD), the final price for a product or service may be influenced by two categorized costs main groups, first costs group are internal, and second group is external, the cost of the product is internal including cost of development, testing, and packaging required when making (PD), this leads to address the standards of (BC) No (23) which effects on the production costs, (BC) don't require from corporations to capitalize (BC) rather it is enjoined to make a uniform policy in capitalized or not capitalized (BC). The (BC) required specific rules in case of capitalizing and requests the standard 23 disclose the procedures are clear.

The borrowing is financing methods adopted in Jordan, the majority of corporations resort to debt financing with the exception of corporations that refuse to banks licensed lending due to lack of solvency, irregular income or corporations that appear abstaining from borrowing is a well known fact, that the availability of credit conditions, closely rely on the age of the corporations, this is due to the short life of the corporations, provide less information about it. Petersen and Raian (1995) The increasing reliability of projects on loan financing will cause the bearing corporations (BC) are relatively high, compared to a net profit return on Investment, need to focus on how to address the costs of borrowing? and the state of its impact on revenue or net income, as is determining the price of the service or the product of the most difficult decisions or the most crucial for managers, must take many factors affecting (PD) as demand, competitors, cost and environmental issues.

The Hilton (2005), then deducting the (PD) is important because it relates to the goals of the corporations, either directly or indirectly. Monroe (2003), therefore, the need to reduce costs and maximize profitability an important factor in the corporations, whether its small or large, simple or complex, private or public, requires them to offer competitive prices. Ayozie (2008). Higher cost of capital and lower (BC) reason for borrowing the corporations and increase financial borrowing, because the investors' expectations higher return than the available interest rate in the market, as a result of the risks investors is endure. The second reason to made borrowing lower the tax burden and recognized by the expenses, while dividends to shareholders are granted distribution of income and the lack of competitiveness. Anthony, (1975).

The contribution this study is to demonstrate the impact of (BC) on (PD) in the long term to clarify, the differences in the results with borrowing or without borrowing, giving relationships within the limits of efficiency reasonable, when assuming an average return of investment equivalent to 20%, reliance on the information contained in the financial statements published in the Amman Financial Market from 2010 to 2014.

### RELATED LITERATURE

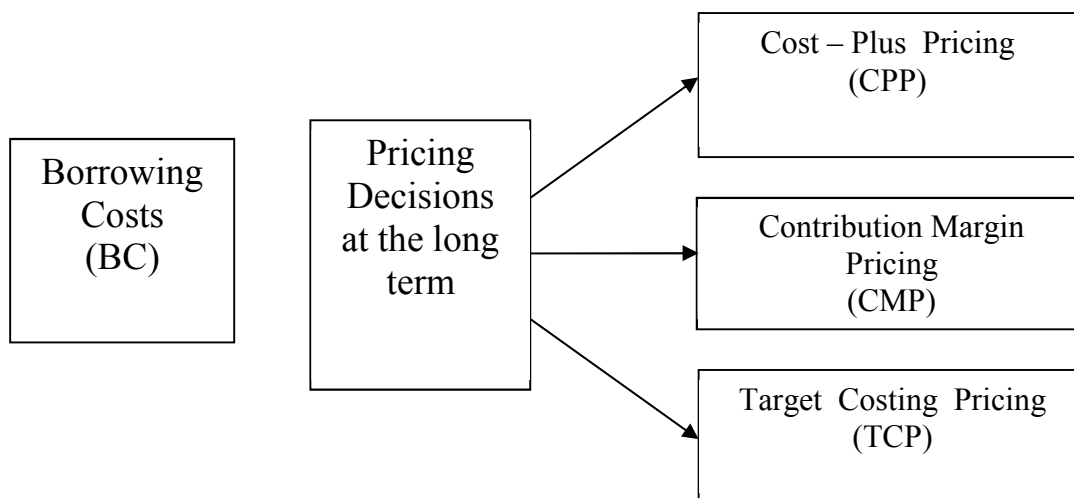
Conducted several studies on the (BC), these studies have been associated with many of the research topics, used by many methodologies, it studies done on the (BC) and (PD) on the other hand as follows:

Study; Ratnatunga (1985) manufacturing corporations in British public fin Ruth prices and profit targets vary to a greater extent and more systematically corporations size than with a number of competitors;

study Noreen and Burgstahler (1997), full-cost pricing imposes restrictions on product prices that may prevent corporations from making a (PD) that leads to satisfactory profits when satisfactory profits and derecognition; study Balakrishnan and Sivaramakrishnan, ( 2001)The corporations used the full-cost method on a large scale in managerial accounting decisions, study Lucas (2003) reached on recommends by using the full cost method in (PD) or (CPP); Buchheit (2004) it turns out the absence of the effect of fixed cost on (PD) in the short term, and increasing fixed cost lead to lower prices and increased competition prices; Cardinaels, et. al (2004) proposed revision of the costing system to play an important role in (PD), the reverse and information on the market, especially ABC system because it provides, the benefit of its cost and volume the sector of the market, Boyd and cox, (2010) the cost accounting systems by providing information is being to make (PD) ideal condition, there be evidence about the constraints of production and non-use of allocated cost, Martin and Stevens (2011) Investment in cost Accounting Systems is costing and analysis, it is focusing on benefit – cost found in that in some cases traditional ways, there is a perfect economic decision, Peter and Chris (2013) the role of the cost information system and accounting costs in (PD) within tourism organizations. Frantz and Instejford, (2013) reached a correlation between improvement of corporate government and reduce the cost of debt, Christopher. J. G et.al, (2012) existence of an important role for the reputation and experience of borrowers in reducing the spread of loans and increase their wealth; Avlonitis and Indounas, (2005) Managers might gain a lot by placing their emphasis on an integrated pricing approach and implement pricing methods, that are in line with the pricing objectives that have been initially set; Guerreiro, et. al (2012) pricing model based on the contribution margin per hour offers stronger adherence for optimizing global earnings if compared to contribution margin in percentage terms.

**HYPOTHESES:**

The model for study put on the basis impact of the independent variable is (BC) under IAS 23 on the (PD) at long term, three methods for pricing at long term cost-plus pricing (CPP), contribution margin pricing (CMP) and target costing pricing (TCP) methods are dependent variables as follow:



Prepared by the researcher

Based on the objectives and the problem of the study model, the formulation of hypotheses of the study as follows:

*H01:* There were no impact for borrowing costs (BC) under IAS 23 for pricing decisions (OD) in Jordanian industrial corporations by using the cost-plus pricing (CPP) method on profitability.

*H02:* There were no impact for borrowing costs (BC) under IAS 23 for pricing decisions (PD) in Jordanian industrial corporations by using contribution margin pricing (CMP) method on profitability.

*H03:* There were no impact for borrowing costs (BC) under IAS 23 for pricing decisions (PD) in Jordanian industrial corporations by using target costing pricing (TCP) method on profitability.

**RESEARCH DESIGN:**

Use the descriptive form and analytical standards with respect to previous studies, prepares to test the impact of (BC) under IAS 23 on (PD), relied on secondary sources to show the theoretical aspect of the study, used the financial statements published in the stock exchange during the time period of 2011-2015.

**Borrowing Costs (BC):**

The (BC) are costs incurred by entity related to (BC) of money, that includes interest, and financial fees on the overdraft account, short-term and long-term borrowing, Standards 23 identify (BC) for costs directly to

acquisition, construction or production of a qualifying asset that needs a long period of time to get ready for use or sale, these costs included costs of assets, but the other costs are included as expenses. Standards 23 related by amortized discounts or premiums related by (BC), arrangements, and financing related by contract lease rent under the international accounting standard 17 and currency exchange differences Kieso et.al (2015).

(BC) basic treatment as an expense in the income statement close, considers as period expenses incurred it, regardless of how it is used? the disclosure requirements form entity about accounting policies used for treatment (BC).

The accounting treatment alternative in accordance with international standard 23 relates to qualifying assets, qualifying assets require long-time to become ready for intended use or sale, such as industrial facilities, assets that require long- time to be ready, and power generation facilities. The (BC) for qualifying assets must be capitalized as a part of the cost of an asset under IAS 23 the (BC) as part of the cost of an asset, if it is probable to achieve the future economic benefit of an entity, and measured reliably, but (BC) of other recognized as an expense for the period incurred it IASC (1984).

#### **Pricing decisions (PD):**

The use of primary and secondary sources plays an important role in the (PD), there is a relationship between (PD) and management of entities must use pricing experts when making (PD), Obigbemi (2010), many factors influence on the (PD) are demanding, competitors cost, political, environmental, legal, and image-related issues, Horngren, et.al, (2006). The best method to maximize their profit and a chive the goals is through the development of competitive price based on accurate data that take into account factors affecting the decisions. product or service, as may be defined price that the only market which leads to revenue and profit variable depending on the thinking and study, does not need to invest and expenses, while the price can also be defined as the process of developing a cash or in-kind value of a good and service, it can be defined as the price that the only market which leads to revenue and profit based on reflection and study variable, and does not need to invest and expenses while the price can also be defined as the process of developing a monetary, in addition to the profit margin specified by the market or the product of a commodity or service, price is meant success or the way in which an entity can make a profit, through pricing achieved established goals direct and indirect, the most important of these objectives to obtain profitability, which share in which all treaty departments, which is a strong indicator of the growth of established in the long term, it is available for installation flexibility in adjusting their price, Monroe (2003).

The profit target first goal, that most be an influence on (PD), seeking facilities to maximize their profits by (PD) sound to maintain profit margins, reduce costs, and achieve the rate of return on investment target is linked to profits, depends on the entity in its products and services pricing, because the yield the appropriate investment governs the (PD) to reach the required or adequate return, and expresses the return on investment Basal dividing any profits realized the net profit ratio on net assets invested (invested capital) despite the fact that income is only used as an indicator of when pricing.

The facility used (PD) in achieving objectives survive in the market, and the challenge of fierce competition, meet the needs and desires of customers, become obsessed survive is desired ambition behind the pricing, has established resort to low-pricing policy in order to increase its sales to the point of reducing the price to cover the costs college or less of them in order to survive, (PD) may be used to stabilize the current situation, without getting involved in pricing policies and engage in a price war, (PD) also be used in cash forecast sales to increase cash sales and lower future sales, especially in the goods that characterized the life cycle short.

#### **Product competitive position in price:**

The face of competition strategy with other corporations, earned may experience the process of reducing the price, due to the impact of competition, either directly or indirectly on the prices of products with varying from corporation to other, depending on the nature and the corporation's work environment, despite the fact that the competition is not the only determining factor in determining the product prices, the size of the corporation affects the pricing policy, Dockner and Fruchter (2004).

#### **Pricing decisions at short-term**

Relationship between (PD) in the short term strongest operational process for a year or less, (PD) require in the short term to focus on the exploitation of surplus production capacity, and linked operation production capacity to exploit fully, the price is lower in the short about it long in the long term the (PD) in the short term relationship request of the client, subject to conditions, including: first to be mainly targeted at long-pricing decisions forward, secondly to exceed the pricing in the short-term variable cost coverage to cover part of the fixed cost, and thirdly that do not order special effect on the expected volume of sales, Leonard, (2005).

#### **Pricing decisions at long-term**

The (PD) in the long term associated with the operation of a term beginning from one year to five years, up to ten years, her relationship with the continuity of the corporation and planning for the long term, a result of the understanding of the costs, customers and competition, a corporation must cover all costs, and taking into account that the average price more than the average total cost of the product or service, so that the corporation

achieved satisfactory profits, enabling them to survive and continue Competitive prices reflect the reaction of competitors to the pricing strategy, lead to increased Benchmarking (Benchmark) in exchange for the customer compared to the price, it is an expression of the reaction of competitors, that's what made there are many considerations required and questions to answer? when developing price? Horngren and Rajan, (2012); Gorchels, (2003).

**Cost- Plus based Pricing**

(CPP) method on a long term pricing forward to determine the total cost of the product or service basis, addition to target profit, which sets a target rate of return on capital investment, that is requires a fixed and variable cost coverage in addition to the profit target Leonard, (2005); Nick (200)5 and Horngren, (2009). The cost-plus pricing method was three cases.

The (CPP) method is method for pricing of a product or service based on cost basis, including direct materials, cost of direct labor and overhead costs, add a markup percentage that represents the profitability of the entity. This method is easy to apply, there is guaranteed to achieve profitability, not to risk the contractual agreement, and justification for the high price due to the high cost, but disadvantage kill the spirit of competition, lack of attention for design, the high cost, lack of attention to the reduction of cost and increase the cost for increase profitability, this is based on historical cost although the replacement costs to be more representative.

$$S P = C (1+ Markup) \dots\dots\dots(1)$$

$$1+ Markup = (SP/ C)\dots\dots\dots(2)$$

$$Markup = (S P/C) - 1 \dots\dots\dots(3)$$

Where as:

Markup = Percentage of profit

SP = Sale price

C = Costs

Effect the borrowing costs

$$Markup = (S P/ C - BC) - 1 \dots\dots\dots(4)$$

Where as:

Borrowing Costs = B C

There are third steps to determine the price based on the (CPP) method.

**Step1:** Determine the total cost of product on the basis of the following equation:

$$TC = VC + FC \dots\dots\dots(5)$$

Where as:

Total costs = TC

Variable costs = VC

Fixed costs = FC

**Step2:** Divide the total costs by the number of units of producing or expected output to determine the cost per unit of product or service.

$$SP = (VC + FC) / X \dots\dots\dots(6)$$

Where as:

X = Number of produced or expected units

**Step3:** Multiply the units of cost by the markup percentage to determine the sale price for unit.

So the equation of determining the price as follows:

$$SP = (VC + FC) * (1+markup)\dots\dots\dots(7)$$

When using costs for the purposes of continuously and systematically pricing, the corporation must take care of two basic.

1. fixed costs become a favorable pricing in the long term.
2. must be proportional to the desired yield in the long term with the investments and risks in the market, not to exceed the revenue limit ourselves only to the cost of changing. Don't finding apposite relationships between the size of the corporation and the(CPP) method, Guilding, et. al, (2005).

**Contribution Margin based Pricing**

Contribution margin based pricing (CMP) is a pricing method which works based on the difference between the product price and variable costs (the products contribution margin per unit), assumptions regarding the relationship between the product's price and the number of units that can be sold at that price. The product's contribution to total firm profit is maximized when a price is chosen that maximizes the 'Contribution Margin Per Unit X Number of Units Sold'.

$$SP - VC = CM \dots\dots\dots(8)$$

$$\text{Break even point} = FC / CM \dots\dots\dots(9)$$

$$\text{Break even point} = FC/ SP - VC \dots\dots\dots(10)$$

With profit

$$\text{Break even point} = FC + P / SP - V \dots\dots\dots(11)$$

Where as:

CM = Contribution Margin

P = profit

Contribution margin used in (PD) to cover the fixed costs, that are sunk costs, if the contribution margin of a low this is method is not profitable, but be useful in two cases, first case when different products, second case if the limited by available resources to directed to the many products profitable.

Characterized the method signs pricing contribution margin by forecasting figures sales, analysis a cost and size, classified as cost to variable cost and fixed costs.

Disadvantage its depend on real figures for sales, the sales price decision change and lock of a problem in big orders the profit doesn't change with the change of prices, even product mix and the corporation sell and produce the same number of units.

The contribution margin equal sales price minus its variable costs, that means the contribution margin determine for sales amount after adjusting variable cost of selling, becomes the income of the corporation is revenue minus expenses, the expenses include fixed costs and plus variable costs.

### **Target costing based Pricing**

Target costing developed in both USA and Japan, Burrows and Chanhall (2012) pricing based on market, estimated for the product or service price which potential and the customers be willing to pay this price, the estimate price is based on an understanding of the customer, the value which return on the customer from the product or service, and how the competitors put pricing for their products or services? understanding customers and competitors very important increasingly, for three reasons:

- 1- Competitors products at the lowest cost, and observance that continues prices.
- 2- Products on the market for short periods, leaving less time and a chance to recover from the pricing errors.
- 3- Customers more knowledgeable and demanding a high quality products at lower prices Horngren. et. al (2012).

There are five steps in the development of target prices and target costing Horngren, et. al, (2012) as follows:

First step: develop products for the meet the needs of potential customers, customers requirements and product features offered by competitors is taking it, the design modifications through market research and add features required from customers is sold at a lower price than competitors.

Second step: Choose a target pricing against the expected benefits of the product based on the volume of sales.

Third step: Derivation of target cost per unit of less the target operating income per unit from target pricing as the target cost represents the estimated cost of long term enable the corporation to achieve the target unit operating income.

Fourth step: Perform cost analysis and reduction of costs that are to focus on the tasks performed by the product of current costs of the various components and focus on providing by different product features.

Fifth step: Engineering performance of Value Engineering to achieve the target cost, a methodology to evaluate all aspects of the value chain in order to reduce costs, achieve the level of quality of satisfied customers, including improving product design, adherence to the specifications, materials, and changes in the operating methods.

The (TCP) method replaced, (CPP) method of pricing the product and service, it objective of maximizing customer benefit, satisfaction with acceptable quality and lowest cost Hibbets et. al (2005), target costing developed in the United States and Japan to improve and reduce costs Burrows, (2012), there is a relationship between pricing methods for target costing and the success of Japanese corporations Cooper (1992).

$$TC = TP - P \dots\dots\dots(12)$$

$$TP = TC + P \dots\dots\dots(13)$$

Where as:

TC = Target costing

TP = Target Price

P = Profit

### **Value Engineering**

Engineering Value EV applied in 1947 in the USA, built on the basis of the production process, aimed at the elimination of unnecessary costs that do not add their values, VE led to raising the level of performance, not confined to the industrial field and entered the service field Ramli et. al (2012), the task of VE team, analysis the new product, VE require the skill and capability of specialists Rich (2000).

VE effort given away and organized to design build the system and equipment, the method of selection of materials, the goal designed to achieve lower costs and better performance through the product life cycle, expected to reach the high quality by raising ideas, improve the product, reducing life cycle costs is done using

the tear effort, the team suggestions in order to make changes lead to lower costs, and maintain the quality Miles (2015).

### CHARACTERISTICS OF SAMPLE

To achieve goals and test hypotheses, for the impact of borrowing costs under IAS 23 on the pricing decisions in the Jordanian corporation, were as follows:

The study population is a Jordanian Corporations Industrial of the Amman Stock Exchange. Founding ratio of borrowing to total equity during five years from 2011- 2015 average rate 23.75%. according to the table (1) this is percent a high proportion of importance.

**Table (1)**  
**Rate Of The Debt Financing In The Industrial Sector**

Year	2010	2011	2012	2013	2014	Average
Finance Rate	24.2	23.46	22.34	23.85	24.03	23.75

The study sample was subjected, according to the data available on the Amman Stock Exchange, Focusing the industrial corporations to the high proportion of debt financing to percent 23.75%, average funding size annual during the study period of 3952 million dinars, and the average earnings annually during the study period 308 million dinars. Table (2) shows the size of the sample of 70 Corporations to the average 76% of the study population.

**Table (2)**  
**The Study Sample Corporations**

Industrial corporations listed	Number	Rate
Corporations excluded	92	100%
The study sample	70	76%

Financial statements published industrial corporations Jordanian during the study period from 2011-2015 was used, Financial statements on the basic accounting treatment of the (BC) adjusted considered an expense as voluntarily expense to be regarded interest expense as a capitalist expense, and extracted profitability compare it with the lists is adjusted.

The study procedures, the researcher access to financial statements published in the sample during the study period, measuring profitability indicators, adjusting the financial statements using the alternative accounting treatment as allowed expense capitalist, measuring profitability indicators after adjustment, measuring the differences between treatment of allow to an alternative treatment, and use of the differences to reach boiling results prove or reject hypotheses.

### RESULTS

The discuss of results in this part of the research, prove or deny the research hypotheses by statistics measure the paired sample test by focusing on alternative treatment for (BC) as contained in the IAS of the effect of this treatment on the revenue using linear equations used in the (PD) of the product or service end to shed light on the (PD) after alternative treatment allowed in the IAS No 23.

### TESTING HYPOTHESES

The statistical guide (t) (Paired sample test) used to test the degree of moral and degree of difference between the value of (t) indexed and (t) calculated for the interpretation of the analytical results of the study.

**H01: There were no impact for ((BC) under IAS 23 for (PD) in Jordanian industrial corporations by using the (CPP) method on profitability.**

**Table (3)**

Paired samples test		
Axis	Value "t"	Sig.
Net profit with capitalization – Net profit without capitulation	2.111	0.038

Table (3) shows value of sig equal 0.038, this is less than 0.05 it rejects the null hypothesis or accept the alternative hypothesis, there is the materiality of a difference in net profit between the treatment of (BC) consider capitalist and treatment the (BC) consider expense revenue from during timing chain from 2011 to 2015.

#### The impact capitalization of (BC) on revenue

SP without capitalize of (BC)

$$SP = C (1 + \text{markup}) \dots\dots\dots(3)$$

But the S. P with capitalize B. C

$$SP = C - BC (1 + \text{markup}) \dots\dots\dots(4)$$

If the (BC) > 0

SP Without capitalizing (BC) > SP with capitalizing (BC)

So that: markup without capitalizing (BC) > markup with capitalizing (BC)

Capitalization for (BC) is not interest of the (CPP) method, because it reduces profits, this method makes the corporation's the interest with increase expenses for increase profitability, if the requirement and the contracts incompatibility with that.

**H02: There were no impact for (BC) under IAS 23 for (PD) in Jordanian industrial corporations by using (CMP) method on profitability.**

**Table (4)**

Paired Samples Test		
Axis	Value "t"	Sig.
Net profit with capitalization – Net profit without capitulation	2.685	.022

Table (4) shows value of sig equal 0.022, this is less than 0.05 it rejects the null hypothesis or accept the alternative hypothesis, there is the materiality of a difference in net profit between the treatment of (BC) consider capitalist and treatment the (BC) consider expense revenue from during timing chain from 2011 to 2015.

**The impact capitalization of (BC) on revenue**

The breakeven point (BEP) without capitalize of (BC) is:

$$\text{Breakeven point} = FC + P / SP - VC \dots\dots\dots(10)$$

The breakeven point with the capitalize of (BC) is:

$$\text{Breakeven point} = FC + P / SP - (VC + BC) \dots\dots\dots(11)$$

So that:

$$\text{CM without capitalizing (BC)} = SP - VC \dots\dots\dots(13)$$

$$\text{CM with capitalize (BC)} = SP - (VC + BC) \dots\dots\dots(14)$$

From equation (13) and (14) found:

CM without (BC) > CM with (BC) and  
 (BEP) with (BC) < (BEP) without (BC) or  
 SP without (BC) < SP with (BC)

The capitalization of (BC) as an alternative treatment with a negative impact on the (BEP) or at the sale price, as evidenced by the former, the capitalization (BC) will lead to increased (BEP). (BEP) without (BC) > (BEP) with (BC), while the second option increase the sales price as in SP with (BC) > SP without (BC), So that first or second case, it will affect the competitive advantage of the entity and weakening the competitive advantage ability of the entity.

**H03: There were no impact for (BC) under IAS 23 for (PD) in Jordanian industrial corporations by using (TCP) method on profitability.**

$$T.C = TP - P \dots\dots\dots(12)$$

$$TP = TC + P \dots\dots\dots(15)$$

TC .... determine from market

RC ... determine from life cycle cost

where as:

RC = Real cost

$$R.C = VRC + FRC$$

**Effect (BC)**

$$\text{RC with (BC)} = VC + FC$$

$$\text{RC Without (BC)} = VC - BC + FC$$

$$\text{RC Without (BC)} < \text{RC with (BC)}$$

The concluding from the foregoing that the alternative to (BC) of treatment (capitalization of borrowing costs) lead to a reduction of the actual production costs, lead to of facilitate the effort VE team to reach the target costing , because the cost of a product life cycle in the case of non capitalized (BC) higher than the cost of product life cycle in case of capitalized production costs, facilitates which the work of the team to get appoint equal to the target cost with the requirement.

**CONCLUSION**

Showing the test result of this research which examines the impact of (BC) under IAS 23 on (PD) at the Jordanian Public Industrial Corporations at long- term pricing having to deal with the impact of alternative (PD) on (BC) used (CPP) a manner where the results indicated, the presence of adverse impact on the pricing for (CPP) method, increase production costs lead to increased profitability in a manner (CPP) method, increased profitability associated with the cost of production, agreements and contracts must be respected.

The other result under treatment alternative (BC) of (PD) for (CMP) method, found negatively impact, because the capitalization of (BC) will lead to higher (BEP), higher sales price alternative to high (BEP), this is impacting on the competitive advantage or lower for profitability. Alternative treatment for (BC) using (TCP) method lead to decline actual cost, facilitate the work of VE team, increased competitive advantage and

increased quality, thus provides a treatment alternative to (BC) when pricing a method that the (TCP).

Not appropriate to capitalize (BC) for pricing (CPP) and (CMP) method, so as to influence bad on profitability when pricing at (CPP) method, (CMP) method increases the (BEP) at short time, that required great effort to reach to (BEP), but the (TCP) methodical treatment alternative to (BC) is best, because it reduces the production costs in a short time.

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