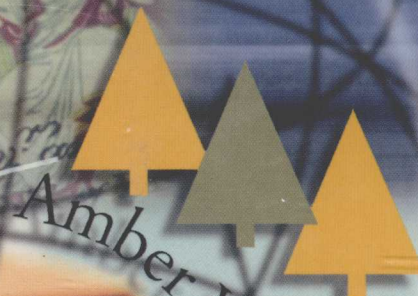
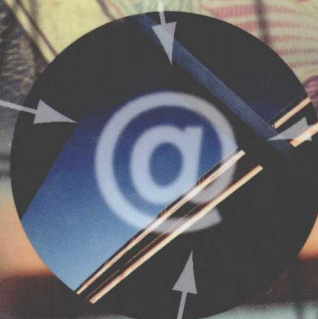


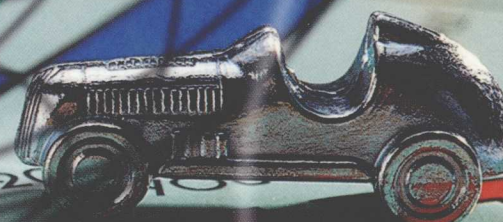


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MANAGERIAL ACCOUNTING

A Focus on Decision Making

STEVE JACKSON

ROBY SAWYERS



MANAGERIAL ACCOUNTING

A FOCUS ON DECISION MAKING



STEVE JACKSON

University of Tennessee

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*To those who influence our decisions:
Cheryl, Christina, Kent and Ben
Amber and Robyn*

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PREFACE

AN INTRODUCTION TO THIS TEXT

"If by education we mean the cramming of a pupil's mind with facts or rules, without any real conception of their meaning or of the relations in which they stand to each other, it is perfectly safe to say that it is a waste of time. This kind of education fits a man for a certain groove, in which he moves in a routine way, a mere piece of mechanical machinery, incapable of independent thought or action. *If confronted with a new condition, to which his rules do not apply, he is helpless, and is liable to make mistakes that are disastrous, because his action is based on insufficient knowledge of the foundation principles . . .*"

Walton, 1917, Journal of Accountancy

In the above statement lies the primary motivation for our writing a new textbook for the study of Managerial Accounting: *a desire to encourage a transition away from a purely third-person delivery by classroom instructors toward a first-person discovery by students both within and outside of the classroom.*

To encourage *discovery learning*, this textbook links **discussion** and **assignments** to needed student skills in managerial decision making. It further illustrates the discussion through use of realistic and interesting companies in every chapter. While educators should expose students to structured uses of tools and information (which aid in good management decisions), accounting education at the turn of *this* century also demands preparation for a world of unstructured problem solving.

The ever-expanding body of knowledge needed in this information age requires that students take responsibility for **life-long** discovery learning. Our approach encourages students to exploit the material presented by allowing its contents to awaken in them a curiosity about how managers solve some of the complex problems and what judgment processes are inherent in today's highly competitive global environment.

Accounting itself has always been referred to as the *language of business*. Business does not exist because of accounting, but accounting exists because businesses need a way to communicate. Accounting information is used for decision-making, planning and controlling activities. Today's competitive global environment requires that accounting information systems have a customer focus so as to provide quantitative and qualitative information useful for decision-making. This requires accounting information to be relevant and reliable in order to be useful to that end. Therefore, managers must learn to be active participants in the design of the information systems used and the reports that are generated from those systems. They must not be passive users of accounting information.

This textbook does provide the background accounting information and tools for using that information that are vital for success in the management environment. However, here the emphasis is on the analysis and interpretation of information rather than on its preparation. This enables us to teach students to think not only "how" but also "why" and to make informed decisions.

We present an approach that we eagerly invite you to explore—an approach which allows both instructor and student to discover an understanding of decision-making in business and will prepare the student for success in all areas.

INTENDED AUDIENCE

In the past, management accountants were traditionally thought of as the recorders and preparers of accounting information. They were typically separated from the rest of the management team and were rarely involved in the major decision-making process. In

"This is truly a managerial accounting approach."

SHEILA AMMONS, AUSTIN COMMUNITY COLLEGE

today's very competitive, global economy, management accountants *have* become part of the management team, actively participating in formulating and implementing the businesses' strategy.

Our textbook and supporting package is intended for all business majors: accounting, management, marketing, finance, human resources, and general business, indeed it is intended for all who will *use* accounting information to make business decisions. Non-business majors will also find this text useful, as the real-world focus and use of accounting information in decision-making are important skills in all areas of life and work. We teach without the use of journal entries or other accounting procedures since our focus is on using accounting information by managers in an organization.

We anticipate that all students in your managerial courses have had at least one term of financial accounting. This text is designed to stand alone and work well in succession to any of the popular financial accounting texts currently on the market.

KEY FEATURES

While the contents of the book are similar to other managerial accounting textbooks, it is truly focused on decision-making and using accounting information for analysis of business problems. We introduce a basic, four-step decision-making model in Chapter 1.



The most important element in the decision-making emphasis of this text is providing students with the structure of the decision-making model. The decision-making model is incorporated throughout the text to reinforce learning. The book integrates material on current issues such as technological advances, global competition, ethics, total quality management, cross-functional teams, activity based costing and the value chain throughout the text. Finally, it would be practically impossible to properly address current issues in managerial accounting without addressing changes in knowledge management and accounting information systems. Chapter 13 focuses on developments in knowledge management and accounting information systems for improved managerial decision-making.

The end of chapter assignment material differs from other texts in that a significant proportion of the longer problems and cases will, through the use of the decision model, require the student to analyze, predict, and extend the solution to make business decisions. These problems/cases require the student to work with unstructured situations, which have more than one defensible decision. The text *and* assignment materials both include extensive use of qualitative information. End-of-chapter assignment material also includes a few problems/cases that focus on group learning or outside research requiring short written solutions. Each chapter also includes a continuing case designed around a computerized business simulation.

PEDAGOGY

This textbook is designed to capture and maintain student focus and interest. The textbook is designed in full-color, with a very visual format to stimulate student interest in the text material.

The text has several types of critical thinking questions in the text designed to alert students to any lack of understanding of material covered before moving on to subsequent areas.



Concept Questions are answered in the text immediately following the question.

Pause and Reflect questions are inserted where needed to alert the student to stop and reflect on what they have learned so far, applying ideas to various situations. Due to the nature of the questions, Pause and Reflect questions do not have answers in the text. Our intent is to teach students to think critically, and to evaluate more than one possible solution to business problems.



Key Concepts and definitions are also highlighted in the text and reference is made, where appropriate, to the decision model.

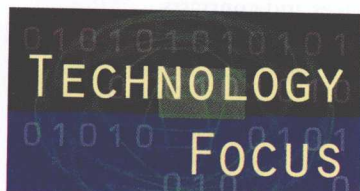
Key Formulas are highlighted where presented in the text.

In The News features, are real world stories, to help students grasp and apply the real-world significance of many of the topics discussed.

Management Actions and Decisions are interviews with managers and users of accounting information in today's business environment. These enhance the learning of concepts by allowing the student to see how decisions are made in the "real world."



Cross Functional Applications highlight the use of accounting information by managers in all areas of business. Our hope is to spark the interest of business students, to emphasize the reasons accounting information is important to understand.



Finally, due to the rapid development of technology available to organizations to conduct their businesses, we have incorporated **Technology Focus** features, which correlate to chapter topics on such issues as Electronic Commerce and Electronic Data Interchange (EDI).

Liberal use of photos further illustrates topics and enhances the understanding of the text material. End-of-chapter assignment material as well as the text material has been classroom tested to minimize errors and misstatements.

Each chapter features a variety of fictional, yet interesting and realistic companies as an example(s) of chapter concepts. We also feature a **Continuing Case** on "Big Al's Pizza Inc." This case builds on lessons and solutions from preceding chapters. It provides a dynamic setting for students to grasp the impact their decisions make upon a business, and promises to be fun as well. The Continuing Case dovetails with **Templates** in MS Excel providing students the dynamic tools to explore possible outcomes by working with numbers on interactive spreadsheets. Three to five Excel templates for end-of-chapter problems are also available to provide students with the opportunity for more analysis and experience with modern applications in business.



SPECIFIC CHAPTER COVERAGE

We have written a 16-chapter text designed for a one-semester course. The book is divided into five sections:

- The Costing of Products and Services.
- The Nature of Costs in Decision-Making.
- Planning, Performance Evaluation and Control.
- Contemporary Topics in Management Decision-Making.
- Other Topics of Interest.

"This chapter presents a good overview of management accounting and its users. New acronyms, such as ERP are also used—good! The role of managers is good, and adequately explained. . . . The human resource aspect is a role frequently overlooked or minimized. The decision model is a good addition. I have not seen it before in a management accounting text."

JAMES MAKOSKE, FRESNO CITY COLLEGE

CHAPTER 1

ACCOUNTING INFORMATION AND MANAGERIAL DECISIONS

This chapter defines accounting information and its uses by both external and internal users. The chapter then describes the decision-making role of management in planning, operating and controlling and provides a framework for assessing decisions that commonly face managers of organizations.



CHAPTER 2

THE PRODUCTION PROCESS AND PRODUCT (SERVICE) COSTING

Chapter 2 begins with a description of the production process for both traditional manufacturing companies with inventory and manufacturing companies with little or no inventory. The chapter also provides an introduction into basic cost terminology applicable to manufacturing companies, merchandising companies and service providers and concludes with a description of cost flows in each type of company.

CHAPTER 3

PRODUCT COSTING MEASUREMENT DECISIONS

Chapter 3 begins with a discussion of the basic systems that companies use to accumulate, track and assign costs to products and services and contrasts and compares job costing, process costing and operations costing. Chapter 3 introduces the concept of cost pools and cost drivers and how they are used to allocate overhead using plant-wide and departmental overhead rates. The chapter includes a discussion of the use of overhead estimates (predetermined overhead rates) in product costing and the treatment of over or under-applied overhead. The appendix of the chapter introduces backflush costing (a costing system that is appropriate for companies employing just-in-time (JIT) manufacturing techniques) and discusses process costing in more detail.



"...The TopSail [Construction Co. in Chapter 4] example was a very clear, concise and comprehensive illustration of the application of ABC. Sometimes explaining the concepts of ABC is very difficult, as students often have a difficult time relating to the types of activities in many manufacturing environments..."

DANIEL R. BRICKNER, UNIVERSITY OF AKRON

CHAPTER 4

PRODUCT COSTING FOR MANAGEMENT DECISIONS: ACTIVITY BASED COSTING AND ACTIVITY BASED MANAGEMENT

In this chapter, we revisit the problems of overhead application and discuss the use of an alternative product costing system called activity based costing (ABC). The benefits and limitations of ABC are discussed, as is the application of ABC to selling and administrative activities and in a JIT environment. The last part of the chapter discusses the use of activity information in controlling and managing costs (activity-based management).



CHAPTER 5



THE NATURE OF COSTS

This chapter introduces concepts and tools that will be used in Chapters 6 through 8. Chapter 5 begins with a definition of cost behavior and illustrates the concepts of fixed costs, variable costs and mixed costs. Next, the chapter revisits the concept of relevant costs as they apply to variable and fixed costs. The chapter also describes the impact of income taxes on costs and introduces the concept of the time value of money and its impact on costs incurred in different time periods.



CHAPTER 6

COST BEHAVIOR AND DECISION MAKING: COST, VOLUME, PROFIT ANALYSIS



In this chapter, we focus on one aspect of the nature of costs (cost behavior) and develop a set of tools that focus on the distinction between fixed and variable costs. These tools include measures of a company's contribution margin, contribution margin ratio and operating leverage - the cornerstones of cost-volume-profit (CVP) analysis. The effect of income taxes on CVP analysis is also discussed.



"The authors did a thorough job [in Ch. 6] of explaining CVP analysis and related topics—contribution margin, breakeven, target profit, operating leverage, income tax effects, and variable costing. Break-even analysis utilizing ABC is also discussed. The reinforcement of the decision model was a good inclusion."

JEANNE YANAMURA, UNIVERSITY OF NEVADA-RENO

CHAPTER 7

ACCOUNTING INFORMATION, RELEVANT COSTS, AND DECISION MAKING

In Chapter 5, we emphasized that only relevant costs and factors should be considered by managers when making decisions. Following the decision-making framework developed in Chapter 1 and building on what we know about the nature of costs from Chapter 5, we analyze a variety of decisions affecting managers in Chapter 7. These decisions include an examination of general pricing issues and the pricing of special orders. The chapter also examines decisions to outsource labor, whether to make or buy a component used to manufacture a product, whether to add or drop a product or service, and how to utilize limited resources to maximize profit. We also consider the impact of ABC on these decisions.

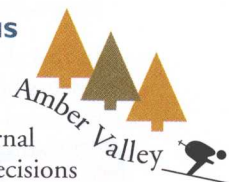


CHAPTER 8

LONG-TERM (CAPITAL INVESTMENT) DECISION ANALYSIS



In this chapter, we develop tools that aid managers in making long-term decisions to purchase new property, plant and equipment (capital investment decisions). The use of net present value and internal rate of return methods in both screening decisions and preference decisions is discussed, as is the impact of income taxes on the analysis. The impact of new manufacturing techniques on capital investment decisions and the importance of qualitative factors in the analysis are also discussed. An approach to long term purchasing decisions that does not take into consideration the time value of money, the payback method, is also mentioned.



CHAPTER 9

THE USE OF BUDGETS IN PLANNING AND DECISION MAKING



In this chapter we introduce the concept of budgeting and discuss how budgets assist managers in planning and decision making. We discuss and demonstrate the preparation of operational budgets for a traditional manufacturing company with inventory as well as for a company operating in a JIT environment. The chapter also covers the use of operational budgets in merchandising and service companies. We pay special attention to the preparation and use of the

"This is the best coverage [in Ch. 9] of the use of Budgeting that I have seen in a Principles of Management Accounting textbook. It is thorough, straightforward, and has good examples."

LYNETTE CHAPMAN, SOUTHWEST TEXAS STATE UNIVERSITY

cash budget for managerial decision making and tie it into the preparation of the statement of cash flows used extensively by external users. Finally, we discuss static and flexible budgets with particular emphasis on the impact of ABC on flexible budgets, and the preparation and use of non-financial budgets.

CHAPTER 10



THE USE OF BUDGETS FOR COST CONTROL AND PERFORMANCE EVALUATION

In this chapter, we expand the discussion of flexible budgeting, and introduce the concept of standard costs and variance analysis as tools to help managers “manage by exception” and evaluate performance in their control function. The chapter ends with a discussion of budgeting culture and the various behavioral issues involved in the budgeting process.

“[Chapter 11 is a] good combination of objectives: responsibility accounting, decentralized operations, cost, profit and investment centers, segment margins and departmental income statements ... right place for performance evaluations and transfer pricing.”

JACQUELINE SANDERS, MERCER COUNTY COMMUNITY COLLEGE

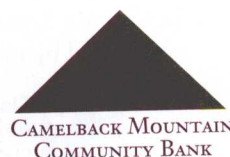
CHAPTER 11



GARCIA & BUFFET CPAS

OTHER TOOLS FOR COST CONTROL AND PERFORMANCE EVALUATION

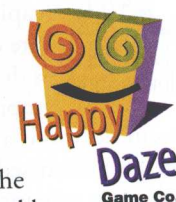
In this chapter we discuss decentralized organizations with an emphasis on the different decisions that must be addressed in a decentralized environment. We also discuss the impact of responsibility accounting and segment reporting on decision making in decentralized organizations. We discuss performance evaluation in cost, revenue, profit and investment centers and introduce measures of performance such as return on investment (ROI), residual income and economic value added (EVA) commonly used in investment centers. We conclude the chapter with a discussion of segment performance and transfer pricing issues between segments.



CHAPTER 12

NON-FINANCIAL MEASURES OF PERFORMANCE

In this chapter we introduce the concept of the balanced scorecard and discuss how the balanced scorecard integrates financial and non-financial measures of performance. We discuss the four perspectives of the balanced scorecard approach: the financial perspective, the customer perspective, the internal business perspective and the learning and growth perspective. We relate measures of quality, timeliness, marketing effectiveness and productivity to each perspective of the balanced scorecard. We conclude the chapter by referring to previous examples in the text to highlight the variety of non-financial measures of performance used by companies.



“I think this [Ch. 13] is a great topic. Accounting has always been an information system, but now its role is being broadened into information for financial and non-financial data. It's not the debits and credits anymore, but efficiency factors, module relationships and sharing information. It's decision-making based on customer orientation along with the bottom line results. It is a merging of technology, marketing, human resources, accounting, finance and management.”

JIM MEIR, CLEVELAND STATE COMMUNITY COLLEGE

CHAPTER 13

THE MANAGEMENT OF INFORMATION AND KNOWLEDGE FOR BETTER DECISIONS

In this chapter we introduce the reader to the concept of knowledge management—the process of formally managing information and knowledge resources in order to facilitate access and reuse of that information and knowledge. Information and knowledge resources may vary for each company, but include traditional sources of data provided by the accounting information system as well as such things as internal memos, training manuals, customer information, and of course the biggest knowledge resource of them

all—a company's employees. Just as information and knowledge resources vary among companies, knowledge management systems may vary as well. Typical knowledge management tools include knowledge warehouses and enterprise resource planning (ERP) systems. Knowledge management tools facilitate supply-chain management, customer relationship management, and internal decision making.

CHAPTER 14

MANAGEMENT FRAUD AND INTERNAL CONTROL



In this chapter we discuss the importance of good internal control and its affect on the reliability of accounting information used in decision making. We discuss the internal control function from a management perspective and from the perspective of the external auditor or CPA. We discuss the most common types of fraud (including inventory theft, price fixing, phantom vendors, kickbacks and financial statement fraud) and show how internal control systems can prevent or uncover these abuses. Finally the chapter looks at the role of the accounting managers and external auditors in providing assurance that the reported financial information is fairly presented and reliable.

**Cher Lee
Financial**

CHAPTER 15

THE STATEMENT OF CASH FLOWS



In the previous fourteen chapters of this textbook we have concentrated on using internally generated accounting information for managerial decision making. In this chapter we present an in-depth discussion of the preparation and use of the cash flow statement. While this statement is primarily used by parties external to the organization, we discuss its importance to managerial decision making and its links to the cash budget produced for internal purposes.

CHAPTER 16

FINANCIAL STATEMENT ANALYSIS



In this chapter we concentrate on another typical financial accounting topic with emphasis on preparing ratios used by stockholders, creditors and other user groups. We also relate some of the ratios to internal uses in decision making. The ratios covered are related to the decision making process of internal management as well as the outside users mentioned above.

"The chapters [15 and 16] compare quite favorably [to other books available]. These are extremely difficult chapters to write and for students to comprehend, due to the nature of the material. I am quite pleased with the approach taken and the examples given."

GEORGE VIOLETTE, UNIVERSITY OF
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FOR INSTRUCTORS

Solutions Manual with checklist of Key Figures *Written by Steve Jackson and Roby Sawyers* A comprehensive manual, written by the authors, containing all the solutions to the end-of-chapter items. Open ended discussion questions have several possible answers listed, with none being the absolute correct answer.

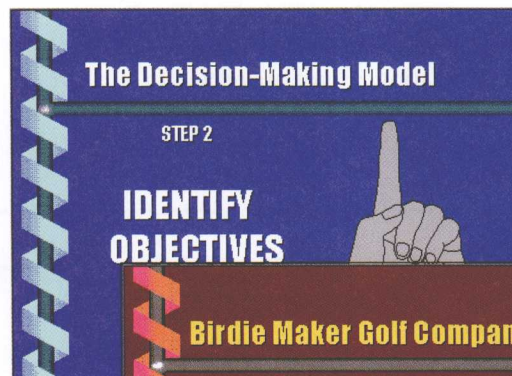
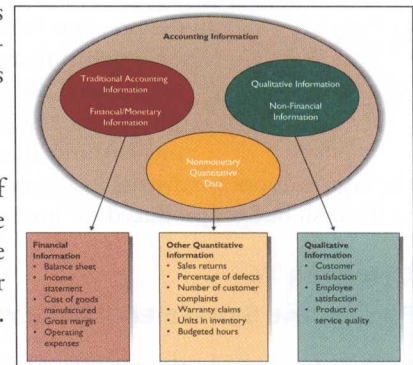
Instructor's Manual *Written by Steve Jackson and Roby Sawyers* A comprehensive resource for instructors, this manual was written by the authors to provide additional teaching tips, outlines, tips for finding guest speakers, instructional outlines for using the videos with classes. This manual has been created closely with the PowerPoint lecture slides to provide a cohesive and seamless teaching package.

Test Bank *Written by Suzanne H. Lowensohn, Barry University* Sue Lowensohn was a colleague of Steve Jackson's at the University of Southern Maine and has been closely involved with this project since its inception. The test bank is fully compatible with the approach of the authors. The test bank contains over 1,500 questions to evaluate students' progress through the course material. Continuing with the text's vision of teaching decision-making and critical thinking skills, it contains questions which require students to evaluate accounting information. A selection of various formats is available including multiple choice, short answer, problems and short cases.

Computerized Test Bank Available in Windows format, the computerized version of the printed test bank enables instructors to preview and edit test questions, as well as add their own. The tests and answer keys can also be printed in "scrambled" formats.

Request Test Service Harcourt College Publishers makes test planning quicker and easier than ever with this program. Instructors can order test masters by question number and criteria over a toll-free telephone number. Test masters will be mailed or faxed within 48 hours.

Overhead Transparencies A selection of textbook illustrations and examples are available in transparency acetate form. Also included are solution acetates for all numerical end-of-chapter concept application exercises, problems and cases.



Lecture Software in Microsoft PowerPoint *Created by Kristine Palmer, Longwood College* An asset to any instructor, the lectures in PowerPoint provide outlines of chapters, graphics of illustrations and examples from the text. Selected end-of-chapter exercises will be included in a clear, crisp fashion to enhance the presentation.

Custom Videos In partnership with successful, well-known companies such as IBM, Lycos, Stride Rite and Pizzeria Uno's, this exciting and innovative video package was developed to find out how managers use accounting information to make decisions. Topics illustrated include break-even analysis, pricing decisions, process controls, and the use of accounting information systems in organizations.

Accounting

Managerial Accounting: A Focus on Decision Making, 1/e by Steve Jackson and Roby Sawyers

ISBN: 0-03-021092-5 [About the Book](#)

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Stock Market Game

Managerial Accounting has a **Companion Web site** www.harcourtcollege.com providing additional instructor and student resources including managerial accounting links and an accounting resource library of articles with applications to text lessons, student Internet activities, and tutorials to enhance the classroom experience. Harcourt College Publishers has also collaborated with Eric Sandburg and Crystal Barkley Corporation to develop a Web Site especially for accounting. This site contains a wealth of accounting resources and student exercises to aid instructors and students in obtaining company information, annual reports, current news, links to SEC filings, and stock quotes. These resources can be located at www.harcourtcollege.com/accounting/.

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For professors interested in supplementing classroom presentations with online content or who are interested in setting up a distance learning course, Harcourt College Publishers, along with WebCT and Blackboard, can provide you with the industry's leading on-line courses.



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If you are using WebCT in your class but not a Harcourt Online Course or textbook, you may adopt the *Student's Guide to the World Wide Web and WebCT* (ISBN 0-03-045503-0). This manual gives step-by-step instructions on using WebCT tools and features.

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FOR STUDENTS

Study Guide Written by Steve Jackson, Roby Sawyers, and James Makofske of Fresno City College A true study aid, this manual lists learning objectives with key concepts to aid students with the fundamentals of the course. In addition, it provides students with self-test questions, exercises and problems that actively engage students in applying what they have learned as well as preparing them for exams.

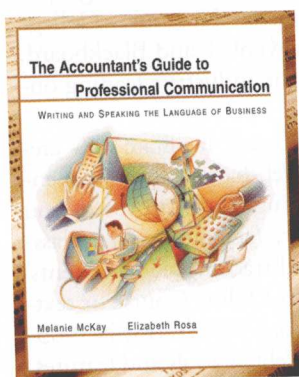
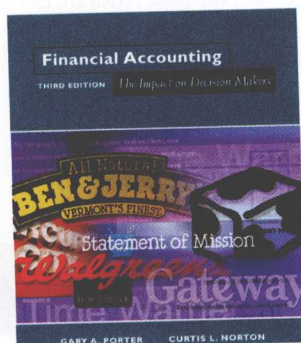
Student PowerPoint Notes We have provided a complete set of student notes in a manual so that all topics within the chapters are covered and less pressure is placed upon instructors to cover all topics in class. Students can spend more time focusing their attention on class discussions rather than rushing to write down all the information being provided. Therefore, students can simply add to the lecture information in the space provided next to every corresponding slide.



Big Al's Pizza Inc. Continuing Case Templates *Created by Steve Jackson and Roby Sawyers* The continuing case has corresponding MS Excel spreadsheets providing dynamic tools to explore possible outcomes by working with numbers on interactive spreadsheets.

Interactive MS Excel templates are provided for Chapters 8 and 9 and selected end-of-chapter exercises throughout the text on our Web site to aid students in “what-if” analysis using time value of money tools and interactive budgets.

Managerial Accounting has a **Companion Web site** www.harcourtcollege.com providing additional activities and resources including managerial accounting links and an accounting resource library of articles with applications to text lessons, Internet activities, and tutorials to enhance the classroom experience.



NEW FROM HARCOURT COLLEGE PUBLISHERS

A Great Companion to *Managerial Accounting* is **Financial Accounting: The Impact on Decision Makers, Third Edition** by Gary Porter and Curt Norton. The first edition of Porter/Norton was the most successful new entry into the financial accounting market in 20 years. This third edition holds true to the original vision of teaching the subject from both the preparer and user perspective, but with a revision focused on greater accessibility to the variety of students taught. Two annual reports (Gateway and Ben & Jerry's) and an annual update program with price stability guarantee highlight the third edition package.

The Accountant's Guide to Professional Communication: Writing and Speaking the Language of Business by Melanie McKay and Elizabeth Rosa. This stand-alone text handbook is a great addition to a student and young professional's accounting reference library, fitting perfectly with the goals of the AECC for enhancing accounting communication skills. It gives a comprehensive, real-world look at all forms of communication used by accounting professionals. Users are taught to write and speak more effectively as preparation for entering the accounting profession. This text, which virtually “teaches itself”, can be used independently in an accounting communication course or as a supplement to enhance any course covering financial reporting, managerial accounting, auditing, or tax accounting topics. Both accounting and non-accounting business majors alike will find this book to be an indispensable reference tool they will want to keep on their office shelves upon entering the “real world”.

REVIEWER FEEDBACK

We would love to list all the great feedback we have received from students and faculty who have aided us with writing *Managerial Accounting*, yet it would be impossible to thank everybody. We hope our thanks is manifested and evidenced through the incorporation of their suggestions in the final product. However, we do list a few comments that assure us—and hopefully you—that we are on-target:

“Overall, I am impressed by the clarity and pedagogy of this [text]. It seems to provide good foundation materials for a Managerial Accounting course. It is fairly aggressive in including complex problems, but compensates by providing a clear understandable description of the problem solving process. Using this text should help students to become better users of accounting information and better decision makers.” Douglas Johnson, Arizona State University.

“I especially like the ‘In the News’ features... the authors have used examples that relate well to the students. [Also] I love having the Contribution Model covered along with Break/Even and Taxes. Currently this is the only text I have seen where Break/Even and ABC are explained together.” Lynette Chapman, Southwest Texas State University.

“The examples and illustrations were outstanding... the illustration of flows of manufacturing costs is one of the clearest I've seen.” Mark Comstock, Missouri Southern State College.

ACKNOWLEDGEMENTS

No book can ever be developed without the help of others who teach the course. We want to give our thanks to the individuals involved in the development of *Managerial Accounting: A Focus on Decision Making*.

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