

BEFORE THE WASHINGTON STATE
UTILITIES AND TRANSPORTATION COMMISSION

In re Application No. GA-079331 of
SURE-WAY SYSTEMS, INC.
For A Certificate of Public Convenience and
Necessity to Operate Motor Vehicles in
Furnishing Solid Waste Collection Service

DOCKET NO. TG-042089
PREFILED TESTIMONY OF
DAVID SULLIVAN

I, David Sullivan, declare under penalty of perjury of the laws of the State of Washington, that the following is true and correct:

1. I have reviewed the prefiled testimony of Nanette Walker and discussed the proposed operations of Sure-Way Systems, Inc. ("Sure-Way Systems") with Gary Chilcott and have the following comments. Although I generally reaffirm the cost expectations used in my proformas and stand behind those estimates, I have revised our proforma financial statements in light of Ms. Walker's comments. See attached Exhibit DS-6
2. Despite Ms. Walker's claims to the contrary, Sure-Way Systems can profitably and effectively serve customers in the proposed Eastern Washington counties on a nondiscriminate basis at 25% market share. Stericycle's actual costs referenced in its replies are excessive, a probable result of a monopoly environment where costs are passed through to captive customers. Allowing Sure-Way Systems to compete in the Eastern Washington market will give the Washington Utilities and Transportation Commission (the "Commission") and Eastern Washington customers an opportunity to demand cost reduction via competition in the marketplace.
3. Stericycle repeatedly uses its actual costs to refute Sure-Way Systems estimates, and states its costs are much higher than Sure-Way Systems lists in the proformas. This suggests on the surface that Stericycle costs are too high. One of the primary reasons to allow competition is to let other providers challenge each other and achieve cost reductions through competition. Smaller companies survive and prosper because they can operate more efficiently at lower costs. Smaller company owners are typically much more conscientious of costs because it comes out of their pocket directly, unlike public companies with mostly outside shareholders.
4. Ms. Walker's loss estimates are substantially predicated upon route mileage she estimates at 9,685 miles per month. The erroneous mileage she proposes results in significantly higher vehicle and

1 additional labor/driver costs. Our own route analysis suggests we can cover the twelve counties once
2 a month in 1,824 miles. See attached Exhibit DS-7.

3 5. Ms. Walker's proposed transportation costs are almost equivalent to Stericycle's actual costs
4 for 100% of customers even though she acknowledges only 25% of the market will be served by
5 Sure-Way Systems. Ms. Walker claims "Sure-Way would have to travel approximately the same
6 distances to serve 25% of Stericycle's existing customer base." Clearly common sense would suggest
7 this is a flawed premise. Obviously the volume of waste generated by 100% of the customers greatly
exceeds waste from 25% of the customers. The key point her argument excludes is frequency of
pickups and the additional distances with more customers causing significantly more mileage driven to
cover all the customers Stericycle serves.

8 6. Sure-Way Systems seeks to provide service in only twelve of the twenty Eastern Washington
9 counties. Those twelve counties comprise only half of the geographic area of Eastern Washington
10 (20,551 square miles of 41,823 square miles). See attached Exhibit DS-8. Thus, Sure-Way Systems
11 will be covering only half of the area of Stericycle in Eastern Washington. Serving the customers in
all of Eastern Washington obviously requires more trips and more mileage than serving only those
customers in an area half the size.

12 7. The exhibits to Mr. Philpott's testimony show weekly and bi-weekly pickups. Sure-Way
13 Systems hopes to be able to provide its rural service once a month for the first nine months, adding a
14 second southern route run in the tenth month and possibly a second northern route run in the second
year.

15 8. Ms. Walker's application of the time Stericycle's drivers spend on driving, customer service
16 and other is not applicable to Sure-Way Systems. Unlike Stericycle, Sure-Way System's drivers will
17 not weigh every container picked up. Nor will it take Sure-Way Systems 75% of the yard time to
serve 25% of the customer base. It simply does not take $\frac{3}{4}$ of the time to handle $\frac{1}{4}$ of the waste.

18 9. Based on routes outside of Spokane County of approximately 1,824 miles, Sure-Way Systems
19 believes it can cover that territory and all of Spokane County with one route driver at 75% (an
20 increase from our original estimate of 70%). That driver will work four ten-hour days. This would
21 include two rural runs, one north of approximately 698 miles and one south of approximately 1,126
22 miles. We estimate three travel days per month initially, with five by the end of the year. The rest of
the time would likely be spent in Spokane County. Given the fact that Stericycle uses four drivers to
cover all of Eastern Washington, it does not seem unreasonable for Sure-Way Systems to plan on
using 75% of one driver for 25% of the market in half the territory.

23 10. These mileage numbers are different from my originally submitted proforma and are based on
24 actual mileage calculated by MapQuest with estimates of additional mileage that might be needed and
25 increasing those miles as we feel our customer base will increase.
26

1 11. I reduced the number of miles for the long-haul because I forgot to share those miles with our
2 Idaho operations.

3 12. I added a \$50 per diem travel allowance for the route driver, which was not previously
4 included.

5 13. The pickup vehicle cost was increased to account for the increased route mileage.

6 14. The plant processing expense was reduced to account for an error in my calculation of the
7 ratio of the 12 Eastern Washington county population as 25% of that of the entire Montana
8 population, when in fact the ratio is only 21%.

9 15. I added sales route mileage of 1,047, representing half the basic route distance of 2,094, based
10 on our estimate that our sales manager will cover the routes once every two months. We reduced the
11 allocation of the sales manager's salary from 80% to 50%, determining that he will only need to spend
12 half his time in Washington, with the other half spent in Idaho. I added amounts for travel per diem
13 and vehicle expense for the sales manager.

14 16. The revised proforma net loss after year one is \$34,394, with a second year profit of \$9,995,
15 meaning we should be able to recover our investment in less than three and one-half years.

16 17. Contrary to Ms. Walker's assertion, there is no need to add an annual cost of \$1,433 for
17 general liability and property insurance. Sure-Way Systems' Washington operations will be covered
18 by its existing general liability coverage of \$2Million and \$1Million for pollution, for which there has
19 never been a claim. See attached Exhibit DS-9. Sure-Way will use vehicles it already owns and
20 insures, so property insurance is not added.

21 18. Similarly, there is no need to add another \$1,000 expense in the second year for "other
22 equipment" because that is for startup equipment that will not need to be replaced.

23 19. Sure-Way Systems does in fact generate positive Cash Flow From Operations (1st section of
24 standards based cash flow statements) as demonstrated on the financial statement submitted with my
25 first prefiled testimony. See Exhibit DS-2. Sure-Way Systems has directed its positive cash flow
26 toward investment in other areas of expansion, resulting in a negative bottom line cash flow that was
financed. Every growing company must use sources of outside capital as its growth opportunities
exceed internally generated cash. The Washington expansion will necessitate Sure-Way Systems
direct its positive cash flow from operations to fund expenses necessary to serve the Washington
customers during the startup phase.

20. Ms. Walker erroneously claims the suspense account called "Holding" of Sure-Way Systems
has a negative effect on the Company's cash position. This wouldn't even be true if the suspense
account reduction were treated as an expense entry. If it were an expense it would actually reduce

1 taxes and improve cash because of additional expense thereby reducing income and income taxes.
2 However, it will not be an expense as I explain below.

3 21. The reduction of the holding balance will in fact be a prior period adjustment and not effect
4 reported 2004 net income. This is recommended action from Sure-Way System's auditors, because
5 the cause of the balance is from 2002. A prior period adjustment means the amounts are shown as
6 reducing retained earnings or income from periods prior to the report time. Accounting treatment
7 does this to maintain the integrity of net income for the period (typically year(s)) covered by the
8 report. Obviously showing a large adjustment in 2004 that was from an earlier period would
9 significantly skew and erroneously present the 2004 results. A prior period adjustment is generally
10 accompanied by a footnote to describe the nature of the transaction so a report reader can be fully
11 informed on a reported value that could affect any decisions based on reported financial information.

12 22. I explained the nature of the account on a telephone call with Ms. Walker. It was represented
13 to her the account was a suspense account, or simply a category used to accumulate transactions for
14 proper clearing or accounting treatment. I represented the account will go to zero. I did not say it
15 would be expensed. At that time we didn't have a full explanation from Sure-Way System's auditors,
16 and we represented to Ms. Walker we were waiting for the auditors response for more details. In this
17 case the balance is caused by an error in fixed assets related to audit schedules. Further the amounts
18 apply to periods before 2004. Therefore, Sure-Way Systems will record a prior-period adjustment on
19 the 2004 financial statement. Since the item does not in any way relate to 2004, Sure-Way System's
20 auditors have recommended for proper reporting the amount be classified as a prior period
21 adjustment on the 2002 financial statements.

22 23. In any case this particular item does not affect Sure-Way System's cash balance or reported
23 cash flow. An entry on a journal record does not affect a Company's bank account or cash balance
24 because it is not a cash payment or receipt. Ms. Walker's analysis erroneously reports the affect of
25 her proposed expense adjustment as affecting cash. On an indirect method Cash Flow Statement the
26 reduction of the current asset holding is an offsetting adjustment, properly showing zero effect on
cash even though net income would decrease by an expense amount. Lastly this is a reporting
difference as a prior period adjustment and only effects amounts reported on paper. A subsequent
cost would actually benefit a Company's cash position by lowering its tax obligation because of more
expense on its income tax return.

27 24. Ms. Walker's testimony that "Sure-Way's financial statements for 2004 indicate that Sure-
28 Way's existing business is cash flow negative" is a highly misleading statement using a bottom line
29 number on the cash flow statement to refute what I had accurately represented as Cash Flow From
30 Operations of existing businesses. If her statement were factual the Company would be bankrupt,
31 and not spending money pursuing a WA Permit Application. Sure-Way Systems is a going concern
32 with proven industry experience. Sure-Way Systems does in fact generate positive Cash Flow From
33 Operations of 2002=\$480,455; 2003=\$673,803; 2004=\$102,212 (1st section of standards based cash
34 flow statements). See Exhibits DS-10, GC-4, and DS-2.

1 25. Sure-Way Systems made a decision to save costs on CPA tax return filing when it elected to
2 delay filing its 2003 tax return. Sure-Way Systems knew the 2003 return would have to be amended
3 after its audit and hence filed twice. Sure-Way Systems expects to and will certainly comply with
4 penalties and interest imposed by the IRS as a result. In light of the ways people can potentially
5 misconstrue and suggest negativity pointing to this action, Sure-Way Systems would certainly file the
6 return with information available at the time even if it meant doubling the cost of filing. This situation
7 is a lesson learned by Sure-Way Systems, and it certainly will not repeat this mistake.

8 26. The 2004 tax return will be filed on time, and work is progressing in that direction at this time.
9 Sure-Way Systems can remit proof of 2004 timely filing to the Commission if requested, in addition
10 to demonstrating 2003 filing. The 2003 filing is expected to be complete by mid-August. The fact
11 that Sure-Way Systems audits its records, a big expense to a small company, demonstrates its
12 commitment to financial integrity and fair representation to counterparties.

13 27. Sure-Way Systems has learned a lesson regarding non-payment of a bill such as the audit bill,
14 and how this kind of situation can create perception problems or look worse than it is. At this time
15 Sure-Way Systems makes regular payments to its auditors to prevent any concerns from any parties
16 about non-payment.

17 28. In fact Sure-Way Systems did not pay its audit bill for some time. Differences between Sure-
18 Way Systems and the CPA firm about the monies owed caused the total bill to sit idle for some time.
19 This situation was more of a stalemate with neither party taking action. Sure-Way believed by paying
20 the bill and trying to get credit later it would by the payment indicate their agreement with the bill and
21 prevent recovery later. The audit period was before my time providing services to Sure-Way
22 Systems, therefore I had no direct contact with the audit work or reasons why the bill was considered
23 excessive. I did request another firm to provide an estimate of what they would charge to do the
24 audit, so Sure-Way Systems could consider other auditors and attempt to bring the audit costs down.
25 The other CPA firm did provide some verbal estimates that were a little lower than the current CPA
26 Firm, but not much lower. The other firm's estimates did give Sure-Way Systems management
assurance the bill was at least competitive even though they still considered the bill excessively
expensive. Sure-Way Systems' current CPA firm later credited charges to Sure-Way Systems as a
compromise to retain the account. Sure-Way Systems elected to continue to work with its current
CPA firm because of the compromise, its long relationship with them, and their locality in the Deer
Lodge community and economy.

27 29. After the billing issues were resolved Sure-Way Systems encountered scheduling delays in the
28 fall of 2004 and the CPA individual tax season, approximately January-April 2005. During tax
29 season the CPAs devote all their energies to individual taxes, and were not able to schedule any time
30 for a multi-year audit project until after tax season. Audit planning stages did start in May 2005, and
31 the work started in June 2005.

32 30. With audit clients, the auditors prudently prefer to complete the audit work before filing the
33 tax return. Most audits result in at least minor adjusting entries. Their goal is to use the most

1 accurate numbers possible prior to filing the return thereby minimizing amendment of returns filed, a
2 potentially costly mistake for clients.

3 DATED this 1st day of August, 2005 at Salt Lake City, Utah.

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David Sullivan

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