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APQC CASE STUDY

Kansas City Southern Case Study

PLANNING, BUDGETING, AND FORECASTING

Quick Facts

This case study is about the integrated entity Kansas City Southern.

Kansas City Southern is composed of Kansas City Southern Railway (KCSR) in the United States and Kansas City Southern de Mexico (KCSM) in Mexico.

Headquarters: Kansas City, MO

2007 Sales (mil.)	$1,742.8
2007 Net Income (mil.)	$153.8
2007 Employees	6,485

Source: Hoovers.com, retrieved November 11, 2008

Riding the Rails to Financial Process Excellence

For a railroad that has been around since 1887, Kansas City Southern (KCS) has shown incredible forward thinking when it comes to improving the performance of its financial operations. Since 2006, KCS' quarterly month-end closing process has decreased from more than 30 calendar days to five business days. In the words of Michael Borrows, Senior Vice President and Chief Accounting Officer, "Five days to income statement, sixth day balance sheet, seventh day cash flow. Done. It's a wrap."

At the same time, KCS has worked to "stop the leakage" across accounting functions. The accounting group has reduced the Days Sales Outstanding (DSO) metric by 32 days, from 70 down to 38 days. DSO is a measure used to report the average number of days it takes to collect cash after a sale has been made. Given the high importance of cash in running a capital-intensive business like a railroad, it is in the company's best interest to collect outstanding receivables in a timely manner. By quickly turning sales into cash-in-hand, KCS has the chance to reinvest and drive more revenue. For KCS, this improvement in DSO represents more than $100 million.

HOW DID KCS DO IT?

In leading this transformation, "the two keys to KCS' success are leveraging technology and employing talented people in value-added activities," Borrows said. Leveraging technology required KCS to begin taking advantage of its systems environment after addressing the underpinning processes. All of its business processes are geared toward SAP (with the exception of planning and forecasting and related reporting that uses TM1, originally from Applix, now a part of Cognos, an IBM Company.) TM1 is managed within the accounting organization at Kansas City Southern and is commonly referred to as "My VIA."

"The two keys to the kingdom are talented people and leveraging technology."

— Michael Borrows, Senior Vice President and Chief Accounting Officer

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The winning name in an internal contest, "My VIA" was selected because "via" means "track" in Spanish and because it can stand for Vision, Insight, and Accountability. The "My VIA" adoption has been so successful that the organization plans to continue to enhance it and fully utilize its capabilities in the foreseeable future.

In the past, finance employees had been over-burdened with manual work, resulting in high levels of attrition, so while the company was bringing in new technology, it was also making significant changes in its human capital. These simultaneous changes enabled KCS to shift the culture within finance and continue to build on the "stop the leakage" mind-set. People worked smarter and more efficiently, not longer, thus allowing the team to use improved technology to focus on value-added tasks.

"Gold-plated technology is not always the best choice; technology that is well implemented based on thoughtful business requirements which meet the business's most critical needs is often a better choice," noted Rob Stilley, General Director, Financial Process Design and Technology Management. KCS' success resulted from a winning combination of the proper implementation and the right technology.

To understand the significance of today's improved financial accounting operational performance, it is important to look at the journey that Kansas City Southern has taken over time.

In mid-2006, KCS brought in Michael Borrows to its financial accounting group. The environment at the time was plagued with process- and system-related difficulties, causing problems with timeliness and accuracy of internal reporting. KCS had just fully acquired its Mexican railroad subsidiary as of April 1, 2005, and struggled with resolving lingering coordination issues between the two entities. The former (pre-acquisition) accounting organization in Mexico had implemented a version of Oracle; however, this implementation was rushed and lacked business definition, so the group reverted back to a legacy version of SAP. As a result of the system turnover as well as other issues, the Domestic and Mexico teams had to manually create a consolidated view at month's end. With the implementation of TM1 by the current accounting team, KCS was able to bring the two companies together from a reporting perspective and greatly improve the efficiency of the consolidation process and significantly improve its internal reporting.

From this transformation, KCS learned that the underpinning internal processes must be well developed before technology can be implemented successfully. KCS learned this firsthand after its implementation of SAP in January 2006. For accounting end users or from a business process perspective, some of the functional details were not properly addressed prior to taking SAP live. In a dramatic example, accounts payable was implemented with no vendor terms. This meant every invoice entered into the system was paid the following day, resulting in significantly reduced cash flow, inability to correct vendor errors within the supply chain, and other fundamental problems. Since then, the company has improved its days payable outstanding (DPO) to about 38 days. Prior to and throughout the implementation of TM1, KCS was much more attentive to the details and the underlying fundamentals of a successful implementation.

There were several reasons why Kansas City Southern selected TM1 as the most effective tool to meet its needs:

- TM1 provides the vehicle for the financial accounting organization to pull and consolidate information from multiple sources (since KCS does not have a single source of data or a data warehouse).
- TM1's end-user interface is very similar to fully functioning Microsoft Excel. In general, KCS resources are familiar with Excel, minimizing the need for specific end-user training.
- TM1 is a scalable end-user tool that does not require significant resource investments to implement and maintain the data. TM1 does not require significant IT overhead such as a database administrator, which other competitive products do. Borrows said, "You don't have to be a pseudo-programmer in the accounting organization to use TM1, and that was important to me. KCS, as a $2 billion company, is not going to have the staff to support that type of specific skill set, so it was important to the organization to implement a tool that was easy to use and required only minimal training."
- In addition to the front-end flexibility, KCS leaders noticed other benefits of the tool, including the ability to store both text and numerical data (which differs from one major competitor).
- The time needed to implement TM1 is reasonable.

From an organizational perspective, KCS transformed the financial accounting culture. The chief accounting officer turned about one-third of the domestic workforce by bringing in talented individuals and identified top performers from the existing talent in Mexico to relocate to Kansas City or assume more prominent leadership roles in Mexico. With this new, highly qualified team and a vision for a new culture, the accounting team became more flexible with a focus on leadership and quality, not just on simply completing the work. The organization has embraced the concept of "work smarter, not harder" and is constantly striving for a "work-life blend." Management does not want employees to be working in the office into the early hours of the morning, so there has been a consistent effort to improve efficiencies and processes.

Another key shift has been to refocus talented employees on analytics as more of the work becomes automated. "As a data-rich company, KCS is now able to gather insight into its data through reporting formats that tell a story or influence business issues from a cost control perspective," said Scott Mylin, AVP Internal Reporting and Control. Prior to the transformation, they were often searching for "the needle in the haystack."

RESULTS

How do you know when your planning and forecasting processes are successful? According to KCS, it comes when you exceed your expectations about the number of users who would want access. KCS had to buy more licenses to be able to meet demand for access to TM1. Finance leadership received requests for access to the TM1 tool from people in parts of the company beyond accounting and financial support (such as the operations team) that it had not anticipated. These teams requesting access had not been trained, but they felt that access to important aspects of the company's financial performance could be a valuable tool. One regular, but unexpected, user of the system is the U.S. vice president of transportation. Borrows said this is a testament to how well designed the tool is, how it has evolved over time, and how the users can all benefit in their own unique way. KCS' leadership has taken the approach of giving people access and not discouraging their use of the product.

Another benefit of the significantly redesigned business processes and automation is that KCS' external auditor has significantly reduced its fees to the railroad. Many of the underlying process improvements and increased efficiencies have occurred around the TM1 product. This product has also allowed the company to begin investigating other areas that could benefit from using the TM1 tool. "Not only is KCS using My VIA for greater visibility into the operating results of the company, KCS is also beginning to use the tool for capital reporting and forecasting," said Ed Scott, Vice President of Capital Investment Accounting.

In 2007, Kansas City Southern won a Vision award from *Business Finance Magazine* based on how the organization was able to move from controlled chaos internally to fluid business processes. The TM1 implementation played a major role in determining KCS as a "best-practice" example and is another testament to the positive results achieved from the transformation.

A final indicator of success for KCS is senior management's willingness to provide capital for technology within the finance organization. Considering that the alternative to investing in finance operations in this asset-intensive company is additional track structure, it is important to note that the positive results achieved have made it easier to get support for necessary capital and provide an environment for continuous improvement. These ideas and the earlier example of significantly reducing the DSO have gone a long way toward demonstrating to management the payoff for their financial accounting investments.

WHO IS BEHIND THIS TRANSFORMATION?

The financial accounting group is lead by Michael Borrows, Sr. Vice President and Chief Accounting Officer. The entire team has worked diligently to transform the department into a top-tier accounting organization able to generate significant value as a business partner contributing to the execution of the company vision. The leaders below, including members of the financial process and design group also in the financial accounting department, have ownership of the planning and forecasting processes and oversee the TM1 module. These individuals, including the leader of the financial process and design team, are the direct reports within the chief accounting officer's organization and oversee the domestic and Mexico finance and accounting operations:

1. **Jim Byrd**—Vice President of International Tax
2. **Suzie Grafton**—AVP Financial Reporting, focusing on external reporting and Sarbanes-Oxley compliance. In October 2008 she was named one of the "Top 40 under 40 Accounting Professionals" in the U.S. by *Treasury and Risk* magazine
3. **Scott Mylin**—AVP Internal Reporting and Control
4. **Ed Scott**—Vice President, Capital Investment Accounting
5. **Rob Stilley**—General Director, Financial Processes and Design. His role is to function as the "grease" between the accounting organization and IT. He helps ensure that KCS' technology footprint continues to evolve as envisioned.
6. **Julio Quintero**—Vice President, Revenue and Disbursements Accounting

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WHAT'S NEXT?

Kansas City Southern's accounting organization has shifted its focus from sprinting quickly to achieve compliance to more of a marathon pace for fine-tuning and continuous improvement. The new goal for the accounting organization is not closing faster but rather fine-tuning its efforts and closing better at a steady pace. The top leaders believe the company is making progress, but they want to do better. Moving forward, KCS looks to perform more-detailed analysis on costs enterprise-wide as it aligns financials in the U.S. and Mexico.

Kansas City Southern is also changing the frequency with which it plans and forecasts. While the company still does a five-year strategic plan, it is moving away from an annual plan and instead focusing on a five-quarter rolling forecast with monthly projections. The organization completes a thorough forecast analysis once per quarter; for the interim months, it only updates the significant or meaningful changes that could impact business decisions. Although the process is not quite "push-button" automated, the linkages are tighter and there is greater ownership of forecasts across the organization. It is no longer viewed as "accounting's plan," handed down to terrorize people in a monthly operations review meeting.

In addition, leadership is driving toward a culture of key performance indicators, metrics and measures, and understanding of costs. The organization is taking simple steps such as minimizing disconnects and ensuring "good hygiene" when completing a financial plan through linkages among revenue projections, capital plans, and operating expenses.

The future for Kansas City Southern includes insight into information that is important to its growth and the ability to execute on its vision. Throughout 2008, management has seen greater buy-in for its revamped financial planning and forecasting models than anticipated. KCS will strive for continuous improvement to enhance its processes and stay on track for 2009. •