KANSAS CITY SOUTHERN
Form 10-K
February 12, 2010

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-K

þ	**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the fiscal year ended December 31, 2009**
	or
o	**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934** **For the transition period from to**

Commission file number: 1-4717

KANSAS CITY SOUTHERN
(Exact name of registrant as specified in its charter)

Delaware *(State or other jurisdiction of incorporation or organization)*	**44-0663509** *(I.R.S. Employer Identification No.)*
427 West 12th Street, Kansas City, Missouri *(Address of principal executive offices)*	**64105** *(Zip Code)*

816.983.1303
(Registrant s telephone number, including area code)
None
(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Preferred Stock, Par Value $25 Per Share, 4%, Noncumulative	New York Stock Exchange
Common Stock, $.01 Per Share Par Value	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes þ No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes o   No þ

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ   No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o   No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer,   accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o   No þ

The aggregate market value of common stock held by non-affiliates of the registrant was $1.49 billion at June 30, 2009. There were 96,519,854 shares of $.01 par common stock outstanding at February 4, 2010.

DOCUMENTS INCORPORATED BY REFERENCE

Kansas City Southern s Definitive Proxy Statement for the 2010 Annual Meeting of Stockholders which will be filed no later than 120 days after December 31, 2009, is incorporated by reference in Parts I and III.

KANSAS CITY SOUTHERN
2009 FORM 10-K ANNUAL REPORT

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Item 1. ***Business***

COMPANY OVERVIEW

Kansas City Southern, a Delaware corporation, is a holding company with domestic and international rail operations in North America that are strategically focused on the growing north/south freight corridor connecting key commercial and industrial markets in the central United States with major industrial cities in Mexico. As used herein, KCS or the Company may refer to Kansas City Southern or, as the context requires, to one or more subsidiaries of Kansas City Southern. KCS and its subsidiaries had approximately 6,100 employees on December 31, 2009. The Kansas City Southern Railway Company (KCSR), which was founded in 1887, is a U.S. Class I railroad. KCSR serves a ten-state region in the midwest and southeast regions of the United States and has the shortest north/south rail route between Kansas City, Missouri and several key ports along the Gulf of Mexico in Alabama, Louisiana, Mississippi, and Texas.

KCS controls and owns all of the stock of Kansas City Southern de México, S.A. de C.V. (KCSM). KCS previously owned this stock through its wholly-owned subsidiary, Grupo KCSM, S.A. de C.V. (Grupo KCSM), formerly known as Grupo Transportación Ferroviaria Mexicana, S.A. de C.V., or Grupo TFM. Effective May 8, 2007, Grupo KCSM was merged into KCSM. Through its 50-year concession from the Mexican government (the Concession), which could expire in 2047 unless extended, KCSM operates a key commercial corridor of the Mexican railroad system and has as its core route the most strategic portion of the shortest, most direct rail passageway between Mexico City and Laredo, Texas. KCSM serves most of Mexico s principal industrial cities and three of its major seaports. KCSM s rail lines provide exclusive rail access to the United States and Mexico border crossing at Nuevo Laredo, Tamaulipas, the largest rail freight interchange point between the United States and Mexico. Under the Concession, KCSM has the right to control and operate the southern half of the rail bridge at Laredo, Texas, which spans the Rio Grande River between the United States and Mexico.

KCSM provides exclusive rail access to the Port of Lazaro Cardenas on the Pacific Ocean. The Mexican government is developing the port at Lazaro Cardenas principally to serve Mexican markets and as an alternative to the congested U.S. west coast ports of Long Beach and Los Angeles. KCSM is the sole provider of rail service to this port, which provides an alternate route for Asian traffic bound for the eastern, southern and midwestern United States. Traffic at Lazaro Cardenas is both domestic and import traffic, consisting of intermodal containers, minerals, iron, steel slabs, wire rods, and fertilizers.

The Company wholly owns, directly and indirectly through its wholly-owned subsidiaries, Mexrail, Inc. (Mexrail) which, in turn, wholly owns The Texas Mexican Railway Company (Tex-Mex). Tex-Mex owns a 157-mile rail line extending from Laredo, Texas to the port city of Corpus Christi, Texas, which connects the operations of KCSR with KCSM. Through its ownership of Mexrail, the Company owns the northern half of the rail bridge at Laredo, Texas. Laredo is a principal international gateway through which more than half of all rail and truck traffic between the United States and Mexico crosses the border. The Company also controls the southern half of this bridge through its ownership of KCSM.

The KCS coordinated rail network (KCSR, KCSM and Tex-Mex) comprises approximately 6,000 miles of main and branch lines extending from the midwest and southeast portions of the United States south into Mexico and connects with other Class I railroads, providing shippers with an effective alternative to other railroad routes and giving direct access to Mexico and the southeast and southwest United States through less congested interchange hubs.

Panama Canal Railway Company (PCRC), an unconsolidated joint venture company owned equally by KCS and Mi-Jack Products, Inc. (Mi-Jack), was awarded a concession from the Republic of Panama to reconstruct and operate the Panama Canal Railway, a 47-mile railroad located adjacent to the Panama Canal that provides international container shipping companies with a railway transportation option in lieu of the Panama Canal. The concession was awarded in 1998 for an initial term of 25 years with an automatic renewal for an additional 25 year term. The Panama Canal Railway is a north-south railroad traversing the Isthmus of Panama between the Atlantic and Pacific Oceans. PCRC s wholly-owned subsidiary, Panarail Tourism

Company (Panarail), operates and promotes commuter and tourist passenger service over the Panama Canal Railway.

Other subsidiaries and affiliates of KCS include the following:

Meridian Speedway, LLC (MSLLC), a seventy-two percent owned consolidated affiliate that owns the former KCSR rail line between Meridian, Mississippi and Shreveport, Louisiana, which is the portion of the KCSR rail line between Dallas, Texas and Meridian known as the Meridian Speedway. Norfolk Southern Corporation (NS) through its wholly-owned subsidiary, The Alabama Great Southern Railroad Company, owns the remaining twenty-eight percent of MSLLC. Ultimately KCS will own seventy percent and NS will own thirty percent of MSLLC upon the contribution of additional capital by NS to MSLLC;

Pabtex, Inc., a wholly-owned and consolidated owner of a bulk materials handling facility with deep-water access to the Gulf of Mexico at Port Arthur, Texas that stores and transfers petroleum coke from rail cars to ships, primarily for export;

Trans-Serve, Inc. (doing business as Superior Tie and Timber), a wholly-owned and consolidated operator of a railroad wood tie treatment facility;

Transfin Insurance, Ltd., a wholly-owned and consolidated captive insurance company, providing property, general liability and certain other insurance coverage to KCS and its subsidiaries and affiliates;

Southern Capital Corporation, LLC (Southern Capital), a fifty percent owned unconsolidated affiliate that leases locomotives and other equipment; and

Ferrocarril y Terminal del Valle de México, S.A. de C.V. (FTVM), a twenty-five percent owned unconsolidated affiliate that provides railroad services as well as ancillary services in the greater Mexico City area.

2009 Revenues
Business Mix

MARKETS SERVED

Chemical and petroleum. This sector includes products such as petroleum, rubber, plastics and miscellaneous chemicals. KCS transports these products to markets in the southeast and northeast United States and throughout Mexico through interchanges with other rail carriers. The products within the chemicals and plastics channels are used in the automotive, housing and packaging industries as well as in the production of other chemicals and plastic products. KCS hauls petroleum products across its network and as petroleum refineries have continued to increase their refining capacity, they have coordinated with KCS to develop additional long-term storage opportunities which complement a fluid freight railroad operation.

Industrial and consumer products. KCS rail lines run through the heart of the southeast United States timber-producing region. The Company believes that forest products made from trees in this region are generally less expensive than those from other regions due to lower production costs. As a result, southern yellow pine products from the southeast are increasingly being used at the expense of western producers that have experienced capacity reductions because of environmental and public policy considerations. KCS serves paper mills directly and indirectly through its various short-line connections.

This sector also includes metals and ores such as iron, steel, zinc and copper. The majority of metals, minerals and ores mined, and steel produced in Mexico are consumed within Mexico. The volume of Mexican steel exports fluctuates based on global market prices. Higher-end finished products such as steel coils are used by Mexican manufacturers in automobiles, household appliances and other consumer goods which are imported to the United States through Nuevo Laredo and through the seaports served by KCS rail network.

Agriculture and minerals. The agriculture and minerals sector consists primarily of grain and food products. Shipper demand for agriculture products is affected by competition among sources of grain and grain products, as well as price fluctuations in international markets for key commodities. In the United States, KCS rail lines receive and originate shipments of grain and grain products for delivery to feed mills serving the poultry industry. KCS currently serves feed mills along its rail lines throughout the midwest and southeast United States and through its marketing agreements, KCS has access to sources of corn and other grain in the Midwest. United States export grain shipments and Mexico import grain shipments include primarily corn, wheat, and soybeans transported to Mexico via Laredo and to the Gulf of Mexico for overseas destinations. Over the long term, export grain shipments to Mexico are expected to increase as a result of Mexico s reliance on grain imports and KCS coordinated rail network is well positioned to meet these increases in demand. Food products consists mainly of soybean meal, grain meal, oils, canned goods, and sugar. Other shipments consist of a variety of products including ores, minerals, clay and glass used across North America.

Intermodal. The intermodal freight business consists primarily of hauling freight containers or truck trailers on behalf of steamship lines, motor carriers, and intermodal marketing companies with rail carriers serving as long-distance haulers. KCS serves and supports the U.S. and Mexican markets, as well as cross border traffic between the U.S. and Mexico. In light of the importance of trade between Asia and North America, the Company believes the Port of Lazaro Cardenas continues to be a strategically beneficial location for ocean carriers, manufacturers and retailers. The Asia/Mexico commerce is handled through the Port of Lazaro Cardenas in conjunction with cross border movement on the single coordinated rail network into markets in the U.S. The Company also provides premium service to customers over its line from Dallas through the Meridian Speedway a critical link in creating the most direct transcontinental line between the southwest and southeast U.S.

Automotive. KCS provides rail transportation to every facet of the automotive industry supply chain, including automotive manufacturers, assembly plants and distribution centers throughout North America. Several U.S. automakers have moved assembly plants into central Mexico to take advantage of access to lower costs, which has driven a shift in production and distribution patterns from the U.S. to Mexico. In addition, KCS transports finished vehicles imported from Asia through a distribution facility at the Port of Lazaro Cardenas. As the automotive industry shifts production and distribution patterns, KCS is poised to serve as a key partner with the automakers, with the technology and rail network to quickly adapt to the automotive industry s evolving transportation requirements.

Coal. KCS hauls unit trains (trains transporting a single commodity from one source to one destination) of coal for eight electric generating plants in the central United States. The coal originates from the Powder River Basin in Wyoming and is interchanged to KCS at Kansas City, Missouri. Coal mined in the midwest United States is transported in non-unit trains to industrial consumers such as paper mills, steel mills, and cement companies. Petroleum coke is also included in the coal sector, which KCS transports from refineries in the United States to cement companies in Mexico as well as to vessels for international distribution through the Pabtex export terminal located in Port Arthur, Texas.

GOVERNMENT REGULATION

The Company s United States operations are subject to federal, state and local laws and regulations generally applicable to all businesses. Rail operations are also subject to the regulatory jurisdiction of the Surface Transportation Board (STB) of the U.S. Department of Transportation (DOT), the Federal Railroad Administration of the DOT, the Occupational Safety and Health Administration (OSHA), as well as other federal and state regulatory agencies. The STB has jurisdiction over disputes and complaints involving certain rates, routes and services, the sale or abandonment of rail lines, applications for line extensions and construction, and consolidation or merger with, or acquisition of control of, rail common carriers. DOT and OSHA each has jurisdiction under several federal statutes over a number of safety and health aspects of rail operations, including the transportation of hazardous materials. In the fourth quarter of 2008, the President of the United States signed the Rail Safety Improvement Act of 2008 into law, which, among other things, revises hours of service rules for train and certain other railroad employees, mandates implementation of positive train control (a technology designed to help prevent train-to-train collisions, overspeed derailments, incursions into rail work zones, and entry into main line track if a switch is misaligned) at certain locations (including main

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line track where toxic inhalation hazard or poison inhalation hazard movements occur or where passenger operations occur) by the end of 2015, addresses safety at rail crossings, increases the number of safety related employees of the Federal Railroad Administration, and increases fines that may be levied against railroads for safety violations. State agencies regulate some aspects of rail operations with respect to health and safety in areas not otherwise regulated by federal law.

KCS subsidiaries are subject to extensive federal, state and local environmental regulations. These laws cover discharges to water, air emissions, toxic substances, and the generation, handling, storage, transportation and disposal of waste and hazardous materials. These regulations have the effect of increasing the costs, risks and liabilities associated with rail operations. Environmental risks are also inherent in rail operations, which frequently involve transporting chemicals and other hazardous materials.

Primary regulatory jurisdiction for the Company s Mexican operations is overseen by the Secretary of Communications and Transportation (SCT). The SCT establishes regulations concerning railway safety and operations, and is responsible for resolving disputes between railways and between railways and customers. In addition, KCSM must register its maximum rates with the SCT and make regular reports to the SCT on investment and traffic volumes. See Note 1 to the Consolidated Financial Statements in Item 8 of this Form 10-K Description of the Business *The KCSM Concession*.

The Mexican operations are subject to Mexican federal and state laws and regulations relating to the protection of the environment through the establishment of standards for water discharge, water supply, emissions, noise pollution, hazardous substances and transportation and handling of hazardous and solid waste. The Mexican government may bring administrative and criminal proceedings and impose economic sanctions against companies that violate environmental laws, and temporarily or even permanently close non-complying facilities.

Noncompliance with applicable legal provisions may result in the imposition of fines, temporary or permanent shutdown of operations or other injunctive relief, criminal prosecution or the termination of the Concession. KCS believes that facilities which it operates are in substantial compliance with applicable environmental laws, regulations and agency agreements. KCS maintains environmental reserves which are believed by management to be appropriate with respect to known and existing environmental contamination of its properties which KCS may be responsible to remedy. In addition, KCS s subsidiaries are party to contracts and other legally binding obligations by which previous owners of certain facilities now owned by KCS are responsible to remedy contamination of such sites remaining from their previous ownership. There are currently no material legal or administrative proceedings pending against the Company with respect to any environmental matters and management does not believe that continued compliance with environmental laws will have any material adverse effect on the Company s financial condition. KCS cannot predict the effect, if any, that unidentified environmental matters or the adoption of additional or more stringent environmental laws and regulations would have on the Company s results of operations, cash flows or financial condition.

COMPETITION

The Company competes against other railroads, many of which are much larger and have significantly greater financial and other resources. The railroad industry is dominated by a few very large carriers. The larger western railroads (BNSF Railway Company and Union Pacific Railroad Company), in particular, are significant competitors of KCS because of their substantial resources and competitive routes. The ongoing impact of past and future rail consolidation is uncertain. However, KCS believes that its investments and strategic alliances continue to competitively position the Company to attract additional rail traffic throughout its rail network.

In November 2005, Ferrocarril Mexicano, S.A. de C.V. (Ferromex) acquired control of and merged with Ferrosur S.A. de C.V. (Ferrosur), creating Mexico s largest railway. These merged operations are much larger than KCSM, and they serve most of the major ports and cities in Mexico and together own fifty percent of FTVM, which serves industries located within Mexico City. The merger between Ferromex and Ferrosur has been rejected by the *Comisión Federal de Competencia* (Mexican Antitrust Commission, or COFECO). Both Ferromex and Ferrosur challenged COFECO s decision.

The Company is subject to competition from motor carriers, barge lines and other maritime shipping, which compete across certain routes in KCS operating areas. In the past, truck carriers have generally eroded the railroad industry s share of total transportation revenues. Intermodal traffic and certain other traffic face highly price sensitive competition, particularly from motor carriers. However, rail carriers, including KCS, have placed an emphasis on competing in the intermodal marketplace and working with motor carriers to provide end-to-end transportation of products.

While deregulation of U.S. freight rates has enhanced the ability of railroads to compete with each other and with alternative modes of transportation, this increased competition has generally resulted in downward pressure on freight rates. Competition with other railroads and other modes of transportation is generally based on the rates charged, the quality and reliability of the service provided and the quality of the carrier s equipment for certain commodities.

EMPLOYEES AND LABOR RELATIONS

Labor relations in the U.S. railroad industry are subject to extensive governmental regulation under the Railway Labor Act (RLA). Under the RLA, national labor agreements are renegotiated on an industry-wide scale when they become open for modification, but their terms remain in effect until new agreements are reached or the RLA s procedures (which include mediation, cooling-off periods, and the possibility of presidential intervention) are exhausted. Contract negotiations with the various unions generally take place over an extended period of time and the Company rarely experiences work stoppages during negotiations. Wages, health and welfare benefits, work rules and other issues have traditionally been addressed during these negotiations.

Approximately 80% of KCSR employees are covered by various collective bargaining agreements. KCSR participates in industry-wide bargaining as a member of the National Carriers Conference Committee. A negotiating process for new, major collective bargaining agreements covering all of KCSR s union employees has been underway since the bargaining round was initiated in November of 2009. Long term settlement agreements were reached during 2007 and 2008 covering all of KCSR s unionized work force through January 1, 2010. The union labor negotiation has not historically resulted in any strike, boycott, or other disruption in the Company s business operations. The Company does not believe the expected settlements will have a material impact to the consolidated financial statements.

KCSM union employees are covered by one labor agreement, which was signed on June 23, 1997, between KCSM and the *Sindicato de Trabajadores Ferrocarrileros de la República Mexicana* (Mexican Railroad Union), for a term of 50 years, for the purpose of regulating the relationship between the parties and improving conditions for the union employees. Approximately 80% of KCSM employees are covered by this labor agreement. The compensation terms under this labor agreement are subject to renegotiation on an annual basis and all other terms are subject to negotiation every two years. In June of 2009, the negotiation of the compensation terms and all other benefits was started with the Mexican Railroad Union. The union labor negotiation with the Mexican Railroad Union has not historically resulted in any strike, boycott, or other disruption in KCSM s business operations. KCSM does not believe the expected settlements will have a material impact to the consolidated financial statements.

RAIL SECURITY

The Company and its rail subsidiaries have made a concentrated, multi-disciplinary effort since the terrorist attacks on the United States on September 11, 2001, to continue securing the Company s assets and personnel against the risk of terrorism and other security risks. Many of the specific measures the Company utilizes for these efforts are required to be kept confidential through arrangements with government agencies, such as the Department of Homeland Security (DHS), or through jointly-developed and implemented strategies and plans with connecting carriers. To protect the confidentiality and sensitivity of the efforts the Company has made to safeguard against terrorism and other security incidents, the following paragraphs will provide only a general overview of some of these efforts. KCSR and KCSM utilize a security plan based on an industry wide security plan developed by Association of American Railroads (AAR) members which focuses on comprehensive risk assessments in five areas hazardous materials; train operations; critical physical assets; military traffic; and information technology and communications. The security plan is kept confidential, with access to the plan tightly limited to members of management with direct security and anti-terrorism implementation responsibilities. KCSR and KCSM participate with other AAR members in periodic drills under the industry plan to test and refine its various provisions.

The Company s security activities range from periodically mailing each employee a security awareness brochure (which is also posted under the Employees tab on the Company s internet website, www.kcsouthern.com) to its ongoing development and implementation of security plans for rail facilities in areas labeled by the DHS as High Threat Urban Areas (HTUAs). The Company s other activities to bolster security against terrorism include, but are not limited to, the following:

Conferring regularly with other railroads security personnel and with industry experts on security issues;

Analyzing routing alternatives and other strategies to reduce the distances that certain chemicals, which might be toxic if inhaled, are transported;

Initiating a series of over 20 voluntary action items agreed to between AAR and DHS as enhancing security in the rail industry; and

Including periodic security training as part of the scheduled training for operating employees and managers.

In addition, in 2008 the Company created a new leadership role titled Director of Homeland Security to oversee the ongoing and increasingly complex security efforts of the Company in both the United States and Mexico. The Company identified and retained an individual to fill the position who has an extensive law enforcement background, including being formerly employed as an analyst with the Federal Bureau of Investigation (FBI) for 12 years. This member of management remains a member of the FBI s Joint Terrorism Task Force and is a valuable asset to the Company in implementing and developing anti-terrorism and other security initiatives.

During 2008, KCSR worked toward implementation of DHS s Transport Worker Identification Card program for those employees requiring unescorted access to secure areas of port facilities, and during 2009, began implementing a contractor background check program for contractor employees having access to certain Company facilities.

While the risk of theft and vandalism is higher in Mexico, KCSM remains among the safest transportation for freight shipments in Mexico. KCSM s record in rail safety is due in large part to the implementation of a multi-layered, safety and security process throughout the KCSM network. In addition to having its own internal system of checks and balances, the process is connected to, and supported by a high level of federal, state and local law enforcement. A primary focus of this effort involves maintaining train velocity, which reduces the likelihood for incidents to occur. By moving customers shipments more efficiently, KCSM is keeping the cargo secure.

AVAILABLE INFORMATION

KCS website (www.kcsouthern.com) provides at no cost KCS Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, and Current Reports on Form 8-K, and amendments to those reports, as soon as reasonably practicable after the electronic filing of these reports is made with the Securities and Exchange Commission. In addition, KCS corporate governance guidelines, ethics and legal compliance policy, and the charters of the Audit Committee, the Finance Committee, the Nominating and Corporate Governance Committee and the Compensation and Organization Committee of the Board of Directors are available on KCS website. These guidelines, policies and charters are available in print without charge to any stockholder requesting them. Written requests for these materials may be made to the Corporate Secretary, P.O. Box 219335, Kansas City, Missouri 64121-9335 (or if by express delivery to 427 West 12th Street, Kansas City, Missouri 64105).

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See Item 8, Financial Statements and Supplementary Data Note 1 Description of the Business and Note 17 Geographic Information for more information on the description and general development of the Company s business and financial information about geographic areas.

Item 1A. *Risk Factors*

Risks Related to an Investment in KCS Common Stock

The price of KCS common stock may fluctuate significantly, which may make it difficult for investors to resell common stock when they want to or at prices they find attractive.

The price of KCS common stock on the New York Stock Exchange (NYSE), listed under the ticker symbol KSU , constantly changes. The Company expects that the market price of its common stock will continue to fluctuate.

The Company s stock price can fluctuate as a result of a variety of factors, many of which are beyond KCS control. These factors include, but are not limited to:

- quarterly variations in operating results;
- operating results that vary from the expectations of management, securities analysts, ratings agencies and investors;
- changes in expectations as to future financial performance, including financial estimates by securities analysts, ratings agencies and investors;
- developments generally affecting the railroad industry;
- announcements by KCS or its competitors of significant contracts, acquisitions, joint marketing relationships, joint ventures or capital commitments;
- the assertion or resolution of significant claims or proceedings against KCS;
- KCS dividend policy and restrictions on the payment of dividends;
- future sales of KCS equity or equity-linked securities;
- the issuance of common stock in payment of dividends on preferred stock or upon conversion of preferred stock or convertible debt; and
- general domestic and international economic conditions including the availability of short- and long-term financing.

In addition, from time to time the stock market in general has experienced extreme volatility that has often been unrelated to the operating performance of a particular company. These broad market fluctuations may adversely affect the market price of KCS common stock.

KCS ability to pay cash dividends on its common stock is currently prohibited and KCS does not anticipate paying cash dividends on its common stock in the foreseeable future.

KCS has agreed, and may agree in the future, to restrictions on its ability to pay cash dividends on its common stock. In addition, to maintain its credit ratings, the Company may be limited in its ability to pay cash dividends on its common stock so that it can maintain an appropriate level of debt. During the first quarter of 2000, the Board of Directors suspended common stock dividends. KCS does not anticipate making any cash dividend payments to its common stockholders in the foreseeable future.

Holders of the Series D Preferred Stock may have special voting rights if KCS fails to pay dividends on that preferred stock over a stated number of quarters.

If dividends on the Series D Preferred Stock are in arrears for six consecutive quarters (or an equivalent number of days in the aggregate, whether or not consecutive), holders of the Series D Preferred Stock will be entitled to elect two of the authorized number of directors at the next annual stockholders meeting at which directors are elected and at each subsequent stockholders meeting until such time as all accumulated dividends are paid on the Series D Preferred Stock or set aside for payment. In addition, so long as dividends on the Series D Preferred Stock remain unpaid and for a period thereafter, KCS will not be eligible to register future offerings of securities on Form S-3 or to avail itself of the other benefits available to companies that qualify as well-known seasoned issuers under SEC rules, which could adversely affect KCS ability to access capital markets and increase the cost of accessing capital markets.

Sales of substantial amounts of KCS common stock in the public market could adversely affect the prevailing market price of the common stock.

As of December 31, 2009, there were 8,763,107 shares of common stock issued or reserved for issuance under the 1991 Amended and Restated Stock Option and Performance Award Plan, the 2008 Stock Option and Performance Award Plan and the Employee Stock Purchase Plan, 2,117,095 shares of common stock held by executive officers and directors outside those plans, and 6,999,826 shares of common stock reserved for issuance upon conversion of the outstanding shares of convertible preferred stock. Sales of common stock by employees upon exercise of their options, sales by executive officers and directors subject to compliance with Rule 144 under the Securities Act, and sales of common stock that may be issued upon conversion of the outstanding preferred stock, or the perception that such sales could occur, may adversely affect the market price of KCS common stock.

KCS has provisions in its charter, bylaws and Rights Agreement that could deter, delay or prevent a third party from acquiring a controlling interest in KCS and that could deprive an investor of an opportunity to obtain a takeover premium for shares of KCS common stock.

KCS has provisions in its charter and bylaws that may delay or prevent unsolicited takeover bids from third parties, including provisions providing for a classified board and supermajority stockholder approval requirements in order to increase the size of the board of directors, abolish cumulative voting, abolish the classification of the Board, or effect certain merger, consolidation or sale transactions. The bylaws provide that a stockholder must give the Company advance written notice of its intent to nominate a director or raise a matter at an annual meeting. In addition, the Company has adopted a Rights Agreement which under certain circumstances would significantly impair the ability of third parties to acquire control of KCS without prior approval of the Board of Directors. These provisions may deprive KCS stockholders of an opportunity to sell their shares at a premium over prevailing market prices.

The failure of a bank to fund a request (or any portion of such request) by KCS to borrow money under its existing revolving credit facility could reduce KCS ability to fund capital expenditures or otherwise properly fund its operations.

The Company and its subsidiaries are in an industry that requires continuing infrastructure improvements and acquisitions of capital assets, necessitating substantial expenditure of cash. KCSR has an existing revolving credit facility with multiple banking institutions to provide additional liquidity. If any of the banking institutions that are a party to such credit facility fails to fund a request (or any portion of such request) by KCSR to borrow money under its credit facility, KCS ability to fund capital expenditures, fund its operations and pay debt service could be reduced, each of which could result in a decline in the value of a stockholder s investment in the Company.

The failure of any bank in which the Company deposits funds could reduce the amount of cash the Company has available to pay distributions and make additional investments.

Given the developments in the subprime mortgage and other financial markets, financial institutions have additional capital risks. The Company has diversified cash and cash equivalents among several banking institutions in an attempt to minimize exposure to any one of these entities. However, the Federal Deposit Insurance Corporation, or FDIC, only insures amounts up to $250,000 per depositor per insured bank. KCS currently has cash and cash equivalents and restricted cash deposited in certain financial institutions in excess of federally insured levels. If any of the banking institutions in which KCS has deposited funds ultimately fails, the Company may lose its deposits to the extent they are in excess of $250,000. The loss of the Company s deposits could reduce the amount of cash the Company has available to distribute or invest and could result in a decline in the value of each stockholder s investment in the Company.

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Risks Related to KCS Business

KCS competes against other railroads and other transportation providers.

The Company s domestic and international operations are subject to competition from other railroads, particularly the Union Pacific Railroad Company (UP) and BNSF Railway Company (BNSF) in the United States and Ferromex in Mexico, as well as from truck carriers, barge lines, and other maritime shippers. Many of KCS rail competitors are much larger and have significantly greater financial and other resources than KCS, which may enable rail competitors to reduce rates and make KCS freight services less competitive. KCS ability to respond to competitive pressures by matching rate reductions and decreasing rates without adversely affecting gross margins and operating results will depend on, among other things, the ability to reduce operating costs. KCS failure to respond to competitive pressures, and particularly rate competition, in a timely manner could have a material adverse effect on the Company s results of operation and financial condition.

The railroad industry is dominated by a few large carriers. These larger railroads could attempt to use their size and pricing power to block other railroads access to efficient gateways and routing options that are currently and have historically been available. In addition, if there is future consolidation in the railroad industry in the United States or Mexico, there can be no assurance that it will not have an adverse effect on operations.

Trucking, maritime, and barge competitors, while able to provide rate and service competition to the railroad industry, are able to use public rights-of-way, require substantially smaller capital investment and maintenance expenditures than railroads and allow for more frequent and flexible scheduling. Continuing competitive pressures, any reduction in margins due to competitive pressures, future improvements that increase the quality of alternative modes of transportation in the locations in which the Company operates, or legislation or regulations that provide motor carriers with additional advantages, such as increased size of vehicles and reduced weight restrictions, could result in downward pressure on freight rates, which in turn could have a material adverse effect on results of operations, financial condition and liquidity.

A central part of KCS growth strategy is based upon the conversion of truck traffic to rail. There can be no assurance the Company will succeed in its efforts to convert traffic from truck to rail transport or that the customers already converted will be retained. If the railroad industry in general is unable to preserve its competitive advantages vis-à-vis the trucking industry, projected revenue growth could be adversely affected. Additionally, revenue growth could be affected by, among other factors, an expansion in the availability, or an improvement in the quality, of the trucking services offered by carriers resulting from regulatory and administrative interpretations and implementation of certain provisions of the North American Free Trade Agreement (NAFTA), and KCS inability to grow its existing customer base and capture additional cargo transport market share because of competition from the shipping industry and other railroads.

KCS business strategy, operations and growth rely significantly on agreements with other railroads and third parties.

Operation of KCS rail network and its plans for growth and expansion rely significantly on agreements with other railroads and third parties, including joint ventures and other strategic alliances, as well as interchange, trackage rights, haulage rights and marketing agreements with other railroads and third parties that enable KCS to exchange traffic and utilize trackage the Company does not own. KCS ability to provide comprehensive rail service to its customers depends in large part upon its ability to maintain these agreements with other railroads and third parties. The termination of, or the failure to renew, these agreements could adversely affect KCS business, financial condition and results of operations. KCS is also dependent in part upon the financial health and efficient performance of other railroads. For example, some of KCSR s traffic moves over the UP s lines via trackage rights, a significant portion of KCSR s grain shipments originate with another rail carrier pursuant to marketing agreements with that carrier, and the UP is KCS largest partner in the interchange of total rail traffic. There can be no assurance that KCS will not be materially adversely affected by operational or financial difficulties of other railroads.

KCSM s operations are subject to certain trackage rights, haulage rights and interline service agreements with another Mexican rail carrier, some of which are in dispute.

Through KCSM s Concession from the Mexican government, KCSM is required to grant short and long distance trackage rights to Ferromex. Applicable law stipulates that Ferromex similarly is required to grant to KCSM rights to use portions of their tracks. Although all of these trackage rights have been granted under the Concession, KCSM and Ferromex have not actually operated under the long distance trackage rights because, other than the rates to be charged pursuant to the Trackage Rights Agreement, dated February 9, 2010, between KCSM and Ferromex, the rates that may be charged for the right to use the tracks have not been agreed upon between KCSM and Ferromex for the periods beginning in 1998 through December 31, 2008.

If KCSM cannot reach an agreement with Ferromex for rates applicable for services prior to January 1, 2009 which are not subject to the Trackage Rights Agreement, the SCT is entitled to set the rates in accordance with Mexican law and regulations, which rates may not adequately compensate KCSM. KCSM is currently involved in judicial, civil and administrative proceedings and negotiations with Ferromex regarding the rates payable to each other for trackage rights, interline services and haulage rights for periods prior to January 1, 2009. Certain of these disputes continue under litigation. Any resolution of such procedures adverse to KCSM could have a negative impact on its results of operations in a particular quarter or fiscal year.

KCS debt capitalization ratio (total debt as a percentage of total debt plus equity) is 45.8%. KCS leverage could adversely affect its ability to fulfill obligations under various debt instruments and operate its business.

KCS level of debt could make it more difficult for it to borrow money in the future, may reduce the amount of money available to finance operations and other business activities, exposes the Company to the risk of increased interest rates, makes it more vulnerable to general economic downturns and adverse industry conditions, and could reduce flexibility in planning for, or responding to, changing business and economic conditions. KCS failure to comply with the financial and other restrictive covenants in its debt instruments, which, among other things, require KCS to maintain specified financial ratios and limit its ability to incur debt and sell assets, could result in an event of default that, if not cured or waived, could have a material adverse effect on the Company s business or prospects. If the Company does not have enough cash to service its debt, meet other obligations and fund other liquidity needs, KCS may be required to take actions such as requesting a waiver from lenders, reducing or delaying capital expenditures, selling assets, restructuring or refinancing all or part of the existing debt, or seeking additional equity capital. KCS cannot assure that any of these remedies can be effected on commercially reasonable terms or at all. In addition, the terms of existing or future debt agreements may restrict the Company from adopting some of these alternatives.

The indebtedness of KCSM exposes it to risks of exchange rate fluctuations because any devaluation of the peso would cause the cost of KCSM s dollar-denominated debt to increase and could place the Company at a competitive disadvantage in Mexico, compared to Mexican competitors that have less dollar-denominated debt and greater operating and financial flexibility than KCSM.

A downturn in the debt capital markets may increase the cost of borrowing and make financing difficult to obtain, each of which may have a material adverse effect on the Company s results of operations and business.

Events in the financial markets may have an adverse impact on the debt capital markets and, as a result, credit may become more expensive and difficult to obtain. Lenders may impose more stringent restrictions on the terms of credit and there may be a general reduction in the amount of credit available in the markets in which KCS conducts business. The negative impact of tightening credit markets and adverse changes in the debt capital markets generally may have a material adverse effect on KCS business and results of operations resulting from, but not limited to, an inability to finance capital expansion on favorable terms, if at all, increased financing costs or financial terms with increasingly restrictive covenants.

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KCS business is capital intensive.

The Company s business is capital intensive and requires substantial ongoing expenditures for, among other things, additions and improvements to roadway, structures and technology, acquisitions, and maintenance and repair of equipment and the rail system. KCS failure to make necessary capital expenditures to maintain its operations could impair its ability to serve existing customers or accommodate increases in traffic volumes.

KCSM s Concession from the Mexican government requires KCSM to make investments and undertake capital projects. If KCSM fails to make such capital investments, KCSM s business plan commitments with the Mexican government may be at risk, requiring KCSM to seek waivers of its business plan. There is no assurance that such waivers, if requested, would be granted by the SCT. KCSM may defer capital expenditures under its business plan with the permission of the SCT. However, the SCT might not grant this permission, and any failure by KCSM to comply with the capital investment commitments in its business plan could result in sanctions imposed by the SCT, and could result in revocation of the Concession if sanctions are imposed on five distinct occasions. The Company cannot assure that the Mexican government would grant any such permission or waiver. If such permission or waiver is not obtained in any instance and KCSM is sanctioned, its Concession might be at risk of revocation, which would materially adversely affect KCS financial condition and results of operations. See KCSM s Mexican Concession is subject to revocation or termination in certain circumstances below.

KCS has funded, and expects to continue to fund capital expenditures with funds from operating cash flows, equipment leases, and debt financing. KCS may not be able to generate sufficient cash flows from its operations or obtain sufficient funds from external sources to fund capital expenditure requirements. Even if financing is available, it may not be obtainable on acceptable terms and within the limitations contained in the indentures and other agreements relating to KCS existing debt.

KCS depends on the stability and availability of its information technology systems to operate its business.

KCS relies on information technology in all aspects of its business. A significant disruption or failure of its information technology systems, including its computer hardware, software and communications equipment, could result in service interruptions, safety failures, security violations, regulatory compliance failures and the inability to protect corporate information assets against intruders or other operational difficulties. Although KCS has taken steps to mitigate these risks, a significant disruption could adversely affect KCS results of operations, financial condition, liquidity and ability to compete effectively. Additionally, if KCS is unable to acquire or implement new technology, it may suffer a competitive disadvantage, which could also have an adverse effect on KCS results of operations, financial condition or liquidity.

KCS business may be adversely affected by changes in general economic, weather or other conditions.

KCS operations may be adversely affected by changes in the economic conditions of the industries and geographic areas that produce and consume the freight that KCS transports. The relative strength or weakness of the United States and Mexican economies affect the businesses served by KCS. Prolonged negative changes in domestic and global economic conditions or disruptions of either or both of the financial and credit markets, including the availability of short and long-term debt financing, may affect KCS, as well as the producers and consumers of the commodities that KCS transports and may have a material adverse effect on KCS results of operations, financial condition, and liquidity.

PCRC is directly affected by the world economy and trans-Pacific trade flows. In addition, KCS investments in Mexico and Panama expose the Company to risks associated with operating in Mexico and Panama, including, among others, cultural differences, varying labor, regulatory and operating practices, political risk and differences between the United States, Mexican and Panamanian economies. Historically, a stronger economy has resulted in improved results for KCS rail transportation operations. Conversely, when the economy has slowed, results have been less favorable. If an economic slowdown or recession occurs in key markets, the volume of rail shipments is likely to be reduced, which could have a material adverse effect on KCS business and financial condition.

The transportation industry is highly cyclical, generally tracking the cycles of the world economy. Although transportation markets are affected by general economic conditions, there are numerous specific factors within each particular market that may influence operating results. Some of KCS customers do business in industries that are highly cyclical, including the oil and gas, automotive, housing and agriculture industries. Any downturn in these industries could have a material adverse effect on operating results. Also, some of the products transported have had a historical pattern of price cyclicality which has typically been influenced by the general economic environment and by industry capacity and demand. For example, global steel and petrochemical prices have decreased in the past, and reduced demand for automotive vehicles and related shipments may result in decreased prices. KCS cannot assure that prices and demand for these products will not decline in the future, adversely affecting those industries and, in turn, the Company s financial condition or results.

The Company s operations may also be affected by natural disasters or adverse weather conditions. The Company operates in and along the Gulf Coast of the United States, and its facilities may be adversely affected by hurricanes, floods and other extreme weather conditions that adversely affect KCS shipping, agricultural, chemical and other customers. Many of the goods and commodities transported by KCS experience cyclical demand. KCS results of operations can be expected to reflect this cyclical demand because of the significant fixed costs inherent in railroad operations. Significant reductions in the volume of rail shipments due to economic, weather, or other conditions could have a material adverse effect on KCS business, financial condition, results of operations, and cash flows.

KCS business may be affected by market and regulatory responses to climate change.

KCS operations may be adversely affected by restrictions, caps, taxes, or other controls on emissions of greenhouse gases, including diesel exhaust. Restrictions on emissions could also affect KCS customers that use commodities that KCS transports to produce energy, use significant amounts of energy in producing or delivering the commodities KCS transports, or manufacture or produce goods that consume significant amounts of energy or burn fossil fuels, including coal-fired power plants, chemical producers, farmers and food producers, and automakers and other manufacturers. Significant cost increases, government regulation, or changes of consumer preferences for goods or services relating to alternative sources of energy or emissions reductions could materially affect the markets for the commodities KCS transports, which in turn could have a material adverse effect on KCS results of operations, financial condition and liquidity. Government incentives encouraging the use of alternative sources of energy could also affect certain customers and their respective markets for certain commodities KCS transports in an unpredictable manner that could alter traffic patterns, including, for example, the impacts of ethanol incentives on farming and ethanol producers. Any of these factors, individually or in conjunction with one or more of the other factors, or other unforeseen impacts of climate change could have a material adverse effect on KCS business, results of operations, financial condition and liquidity.

KCS is exposed to the credit risk of its customers and counterparties and their failure to meet their financial obligations could adversely affect KCS business.

KCS business is subject to credit risk including the risk that a customer or counterparty will fail to meet its obligations when due. Customers and counterparties that owe the Company money may default on their obligations to the Company due to bankruptcy, lack of liquidity, operational failure or other reasons. Although the Company has procedures for reviewing its receivables and credit exposures to specific customers and counterparties to address present credit concerns, default risk may arise from events or circumstances that are difficult to detect or foresee. Some of the Company s risk management methods depend upon the evaluation of information regarding markets, clients or other matters that are publicly available or otherwise accessible by the Company. That information may not, in all cases, be accurate, complete, up-to-date or properly evaluated. In addition, concerns about, or a default by, one customer or counterparty could lead to significant liquidity problems, losses or defaults by other customers or counterparties, which in turn could adversely affect the Company. The Company may be materially and adversely affected in the event of a significant default by its customers and counterparties.

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KCS business is subject to regulation by international, federal, state and local regulatory agencies, including tax, environmental, health, and safety laws and regulations that could require KCS to incur material costs or liabilities relating to tax, environmental, health, or safety compliance or remediation. KCS failure to comply with these regulations could have a material adverse effect on its operations.

KCS is subject to income taxes as well as non-income based taxes, in both the United States and Mexico. Significant judgment is required in determining the provision for income taxes and other tax liabilities. Changes in tax rates, enactment of new tax laws, and revisions of tax regulations could have a material adverse affect on the Company s financial condition and operating results. Although KCS believes the tax estimates are reasonable, the final determination of tax audits, claims, or litigation could differ from what is reflected in KCS income tax provisions and accruals.

KCS is subject to governmental regulation by international, federal, state and local regulatory agencies with respect to its railroad operations, including the Department of Transportation and the Department of Homeland Security in the United States and the Secretary of Communications and Transportation in Mexico, as well as a variety of health, safety, labor, environmental, and other matters. Government regulation of the railroad industry is a significant determinant of the competitiveness and profitability of railroads. As part of the Rail Safety Improvement Act of 2008 in the United States, Class I railroad carriers and passenger and commuter rail operators must implement positive train control (a technology designed to help prevent train-to-train collisions, overspeed derailments, incursions into rail work zones, and entry into main line track if a switch is misaligned) at certain locations (including main line track where toxic inhalation hazard or poison inhalation hazard movements occur or where passenger operations occur) by the end of 2015, which will add to operating costs, increase the number of employees the Company employs and require KCS to invest significant amounts of money into new safety technology. KCS inadvertent failure or inability to comply with applicable laws and regulations could have a material adverse effect on our financial condition, liquidity and operations, including limitations on operating activities until compliance with applicable requirements is achieved. These government agencies may change the legislative or regulatory framework within which the Company operates without providing any recourse for any adverse effects on its business that occur as a result of such change. Additionally, some of the regulations require KCS to obtain and maintain various licenses, permits and other authorizations. Any failure to maintain these licenses, permits, and other authorizations could adversely affect KCS business.

From time to time, certain KCS facilities have not been in compliance with environmental, health and safety laws and regulations and there can be no assurance that KCS will always be in compliance with such laws and regulations in the future. Environmental liability under federal and state law in the United States can also extend to previously owned or operated properties, leased properties and properties owned by third parties, as well as to properties currently owned and used by the Company. Environmental liabilities may also arise from claims asserted by adjacent landowners or other third parties. Given the nature of its business, the Company incurs, and expects to continue to incur, environmental compliance costs, including, in particular, costs necessary to maintain compliance with requirements governing chemical and hazardous material shipping operations, refueling operations and repair facilities. KCS presently has environmental investigation and remediation obligations at certain sites, and will likely incur such obligations at additional sites in the future. Liabilities accrued for environmental costs represent the Company s best estimate of the probable future obligation for the remediation and settlement of these sites. Although the recorded liability is the best estimate of all probable costs, clean-up costs cannot be predicted with absolute certainty, and may exceed such estimates, due to various factors such as evolving environmental laws and regulations, changes in technology, the extent of other parties participation, developments in environmental surveys and studies, and the extent of corrective action that may ultimately be required. New laws and regulations, stricter enforcement of existing requirements, accidental spills, releases or violations or the discovery of previously unknown contamination could require KCS to incur costs or subject KCS to liabilities that could have a material adverse effect on KCS business, results of operations, financial condition, and cash flows.

The Company s Mexican operations are subject to Mexican federal and state laws and regulations relating to the protection of the environment, including standards for, among other things, water discharge, water supply, emissions, noise pollution, hazardous substances and transportation and handling of hazardous and solid waste. Under applicable Mexican law and regulations, administrative and criminal proceedings may be brought and economic sanctions imposed against companies that violate environmental laws, and non-complying facilities may be temporarily or permanently closed. KCSM is also subject to the laws of various jurisdictions and international conferences with respect to the discharge of materials into the environment and to environmental laws and regulations issued by the governments of each of the Mexican states in which KCSM s facilities are located. The terms of KCSM s Concession from the Mexican government also impose environmental compliance obligations on KCSM. The Company cannot predict the effect, if any, that unidentified environmental matters or the adoption of additional or more stringent environmental laws and regulations would have on KCSM s results of operations, cash flows or financial condition. Failure to comply with any environmental laws or regulations may result in the termination of KCSM s Concession or in fines or penalties that may affect profitability.

KCS, as a common carrier by rail, is required by United States and Mexican laws to transport hazardous materials, which could expose KCS to significant costs and claims.

Under United States federal statutes and Mexican applicable laws, KCS s common carrier responsibility requires it to transport hazardous materials. Any rail accident or other incident or accident on KCS s network, facilities, or at the facilities of KCS s customers involving the release of hazardous materials, including toxic inhalation hazard (or TIH) materials, could involve significant costs and claims for personal injury, property damage, and environmental penalties and remediation, which could have a material adverse effect on KCS s results of operations, financial condition, and liquidity.

KCS business is vulnerable to rising fuel costs and disruptions in fuel supplies. Any significant increase in the cost of fuel that is not adequately covered by fuel surcharges, or severe disruption of fuel supplies, would have a material adverse effect on KCS business, results of operations and financial condition.

KCS incurs substantial fuel costs in its railroad operations and these costs represent a significant portion of its transportation expenses. Significant price increases for fuel may have a material adverse effect on operating results. During periods of rising fuel prices, KCS has been able to pass the majority of these fuel cost increases on to customers in the form of fuel surcharges applied either in the form of an increase in the freight rate or direct customer billings. If KCS is unable to recapture its costs of fuel from its customers, operating results could be materially adversely affected. In addition, a severe disruption of fuel supplies resulting from supply shortages, political unrest, a disruption of oil imports, weather events, war, or otherwise, and the resulting impact on fuel prices could materially adversely affect KCS operating results, financial condition, and cash flows.

KCS currently meets, and expects to continue to meet, fuel requirements for its Mexican operations almost exclusively through purchases at market prices from PEMEX Refinanción (PEMEX), the national oil company of Mexico, a government-owned entity exclusively responsible for the distribution and sale of diesel fuel in Mexico. KCSM is party to a fuel supply contract with PEMEX of indefinite duration. Either party may terminate the contract upon 30 days written notice to the other at any time. If the fuel contract is terminated and KCSM is unable to acquire diesel fuel from alternate sources on acceptable terms, the Mexican operations could be materially adversely affected.

Market fluctuations could adversely impact KCS s operating results as it hedges certain transactions.

From time to time, KCS may use various financial instruments to reduce its exposure to various market risks, including interest rates and fuel prices. While these financial instruments reduce the Company s exposure to changes in market risks, the use of such instruments may ultimately limit the Company s ability to benefit from lower fuel prices or interest rates due to amounts fixed at the time of entering into the hedge agreement.

The loss of key personnel could negatively affect business.

KCS success substantially depends on its ability to attract and retain key members of the senior management team and the principals of its foreign subsidiaries. Recruiting, motivating, and retaining qualified management personnel, particularly those with expertise in the railroad industry, are vital to operations and success. There is substantial competition for qualified management personnel and there can be no assurance that KCS will always be able to attract or retain qualified personnel. Employment agreements with senior management are terminable at any time by either party. If KCS loses one or more of these key executives or principals, its ability to successfully implement its business plans and the value of its common stock could be materially adversely affected.

A majority of KCS employees belong to labor unions. Strikes or work stoppages could adversely affect operations.

The Company is a party to collective bargaining agreements with various labor unions in the United States and Mexico. As of December 31, 2009, approximately 80% of KCSR s and KCSM s employees were covered by labor contracts subject to collective bargaining. The Company may be subject to, among other things, strikes, work stoppages or work slowdowns as a result of disputes under these collective bargaining agreements and labor contracts or KCS potential inability to negotiate acceptable contracts with these unions. In the United States, because such agreements are generally negotiated on an industry-wide basis, determination of the terms and conditions of labor agreements have been and could continue to be beyond KCS control. KCS may, therefore, be subject to terms and conditions in industry-wide labor agreements that could have a material adverse effect on its results of operations, financial condition and cash flows. If the unionized workers in the United States or Mexico were to engage in a strike, work stoppage or other slowdown, if other employees were to become unionized, or if the terms and conditions in future labor agreements were renegotiated, KCS could experience a significant disruption of its operations and higher ongoing labor costs. Although the U.S. Railway Labor Act imposes restrictions on the right of United States railway workers to strike, there is no law in Mexico imposing similar restrictions on the right of railway workers in that country to strike.

KCS faces possible catastrophic loss and liability and its insurance may not be sufficient to cover its damages or damages to others.

The operation of any railroad carries with it an inherent risk of catastrophe, mechanical failure, collision, and property loss. In the course of KCS operations, spills or other environmental mishaps, cargo loss or damage, business interruption due to political developments, as well as labor disputes, strikes and adverse weather conditions, could result in a loss of revenues or increased liabilities and costs. Collisions, environmental mishaps, or other accidents can cause serious bodily injury, death, and extensive property damage, particularly when such accidents occur in heavily populated areas. Additionally, KCS operations may be affected from time to time by natural disasters such as earthquakes, volcanoes, floods, hurricanes or other storms. The occurrence of a major natural disaster could have a material adverse effect on KCS operations and financial condition. The Company maintains insurance that is consistent with industry practice against the accident-related risks involved in the conduct of its business and business interruption due to natural disaster. However, this insurance is subject to a number of limitations on coverage, depending on the nature of the risk insured against. This insurance may not be sufficient to cover KCS damages or damages to others and this insurance may not continue to be available at commercially reasonable rates. In addition, KCS is subject to the risk that one or more of its insurers may become insolvent and would be unable to pay a claim that may be made in the future. Even with insurance, if any catastrophic interruption of service occurs, KCS may not be able to restore service without a significant interruption to operations which could have an adverse effect on KCS financial condition.

KCS business may be affected by future acts of terrorism war or other acts of violence or crime.

Terrorist attacks, such as an attack on the Company s chemical transportation activities, any government response thereto and war or risk of war may adversely affect KCS results of operations, financial condition, and cash flows. These acts may also impact the Company s ability to raise capital or its future business opportunities. KCS rail lines and facilities could be direct targets or indirect casualties of acts of terror, which could cause significant business interruption and damage to KCS property. In recent years, there have been

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reported incidents of train cargo robberies in the United States and Mexico. Other acts of violence or crime could also adversely affect the Company s business.

As a result, acts of terrorism or war or acts of crime or violence could result in increased costs and liabilities and decreased revenues for KCS. In addition, insurance premiums charged for some or all of the applicable coverage currently maintained by KCS could increase dramatically or certain coverage may not be adequate to cover losses or may not be available in the future.

KCSM s Mexican Concession is subject to revocation or termination in certain circumstances which would prevent KCSM from operating its railroad and would have a material adverse effect on the Company s business and financial condition.

KCSM operates under the Concession granted by the Mexican government, which is renewable for up to 50 years, subject to certain conditions. The Concession gives KCSM exclusive rights to provide freight transportation services over its rail lines for 30 years of the 50-year Concession, subject to certain trackage and haulage rights granted to other concessionaires. The SCT, which is principally responsible for regulating railroad services in Mexico, has broad powers to monitor KCSM s compliance with the Concession and it can require KCSM to supply it with any technical, administrative and financial information it requests. Among other obligations, KCSM must comply with the investment commitments established in its business plan, which forms an integral part of the Concession, and must update the plan every five years. The SCT treats KCSM s business plans confidentially. The SCT also monitors KCSM s compliance with efficiency and safety standards established in the Concession. The SCT reviews, and may amend, these standards every five years.

The Mexican Railroad Services Law and regulations provide the Mexican government certain rights in its relationship with KCSM under the Concession, including the right to take over the management of KCSM and its railroad in certain extraordinary cases, such as imminent danger to national security. In the past, the Mexican government has used such power with respect to other privatized industries, including the telecommunications industry, to ensure continued service during labor disputes. In addition, under Article 47 of the Mexican Railroad Services Law and its regulations, the SCT, in consultation with the Mexican Antitrust Commission, reserves the right to set service rates if it determines that effective competition does not exist in the Mexican railroad industry. The Mexican Antitrust Commission, however, has not published guidelines regarding the factors that constitute a lack of competition. It is therefore unclear under what particular circumstances the Mexican Antitrust Commission would deem a lack of competition to exist. If the SCT intervenes and sets service rates, the rates it sets may be too low to allow KCSM to operate profitably.

Under the Concession, KCSM has the right to operate its rail lines, but it does not own the land, roadway or associated structures. If the Mexican government legally terminates the Concession, it would own, control, and manage such public domain assets used in the operation of KCSM s rail lines. All other property not covered by the Concession, including all locomotives and railcars otherwise acquired, will remain KCSM s property. The Mexican government will have the right to cause the Company to lease all service-related assets to it for a term of at least one year, automatically renewable for additional one-year terms up to five years. The Mexican government must exercise this right within four months after revocation of the Concession. In addition, the Mexican government will also have a right of first refusal with respect to certain transfers by KCSM of railroad equipment within 90 days after revocation of the Concession.

The Mexican government may also temporarily seize control of KCSM s rail lines and its assets in the event of a natural disaster, war, significant public disturbance or imminent danger to the domestic peace or economy. In such a case, the SCT may restrict KCSM s ability to exploit the Concession in such manner as the SCT deems necessary under the circumstances, but only for the duration of any of the foregoing events. Mexican law requires that the

Mexican government pay compensation if it effects a statutory appropriation for reasons of the public interest. With respect to a temporary seizure due to any cause other than international war, the Mexican Railroad Services Law and regulations provide that the Mexican government will indemnify an affected concessionaire for an amount equal to damages caused and losses suffered. However, these payments may not be sufficient to compensate KCSM for its losses and may not be timely made.

The SCT may revoke the Concession if KCSM is sanctioned on three distinct occasions for unjustly interrupting the operation of its rail lines or for charging tariffs higher than the tariffs it has registered with the SCT. In addition, the SCT may revoke the Concession if, among other things, KCSM is sanctioned on five distinct occasions because KCSM restricts the ability of other Mexican rail operators to use its rail lines; KCSM fails to make payments for damages caused during the performance of services; KCSM fails to comply with any term or condition of the Mexican Railroad Services Law and regulations or the Concession; KCSM fails to make the capital investments required under its five-year business plan filed with the SCT; or KCSM fails to maintain an obligations compliance bond and insurance coverage as specified in the Mexican Railroad Services Law and regulations. In addition, the Concession would revoke automatically if KCSM changes its nationality or assigns or creates any lien on the Concession, or if there is a change in control of KCSM without the SCT s approval. The SCT may also terminate the Concession as a result of KCSM s surrender of its rights under the Concession, or for reasons of public interest or upon KCSM s liquidation or bankruptcy. Revocation or termination of the Concession would prevent KCSM from operating its railroad and would materially adversely affect the Mexican operations and the ability to make payments on KCSM s debt. If the Concession is terminated or revoked by the SCT for any reason, KCSM would receive no compensation and its interest in its rail lines and all other fixtures covered by the Concession, as well as all improvements made by it, would revert to the Mexican government.

In April 2006, the SCT initiated proceedings against KCSM, claiming that KCSM had failed to make certain minimum capital investments projected for 2004 and 2005 under its five-year business plan filed with the SCT prior to its April 2005 acquisition by KCS (collectively, the Capital Investment Proceedings). KCSM believes it made capital expenditures exceeding the required amounts. KCSM responded to the SCT by providing evidence in support of its investments and explaining why it believes sanctions are not appropriate. In May 2007, KCSM was served with an SCT resolution regarding the Capital Investment Proceeding for 2004, in which the SCT resolved to impose no sanction. In June 2007, KCSM was served with an SCT resolution regarding the Capital Investment Proceeding for 2005, in which the SCT determined that KCSM had indeed failed to make the minimum capital investments required for such year, and imposed a minimal fine. KCSM has filed an action in the Mexican Administrative and Fiscal Federal Court challenging this ruling. KCSM will have the right to challenge any adverse ruling.

KCSM believes that even if a sanction is ultimately imposed as a consequence of the 2005 Capital Investment Proceeding, there will be no material adverse effect on its results of operations or financial condition. However, if a sanction were to be imposed, it would be considered a generic sanction under Mexican law (i.e., sanctions applied to conduct not specifically referred to in specific subsections of the Mexican railway law). If KCSM is ultimately sanctioned by the SCT for generic sanctions on five occasions over the term of the Concession, KCSM could be subject to possible future SCT action seeking revocation of the Concession. Such revocation would materially adversely affect the results of operations and financial condition of KCSM.

KCS ownership of KCSM and operations in Mexico subject it to economic and political risks.

The Mexican government has exercised, and continues to exercise, significant influence over the Mexican economy. Accordingly, Mexican governmental actions concerning the economy and state-owned enterprises could have a significant impact on Mexican private sector entities in general and on KCSM s Mexican operations in particular. KCS cannot predict the impact that the political landscape, including the recently implemented multiparty rule, will have on the Mexican economy. Furthermore, KCSM s financial condition, results of operations and prospects may be affected by currency fluctuations, inflation, interest rates, regulation, taxation, social instability and other political, social and economic developments in or affecting Mexico.

The Mexican economy in the past has suffered balance of payment deficits and shortages in foreign exchange reserves. Although Mexico has imposed foreign exchange controls in the past, there are currently no exchange controls in Mexico. Pursuant to the provisions of NAFTA, if Mexico experiences serious balance of payment difficulties or the threat of such difficulties in the future, Mexico would have the right to impose foreign exchange controls on investments made in Mexico, including those made by United States and

Canadian investors. Any restrictive exchange control policy could adversely affect KCS ability to obtain dollars or to convert pesos into dollars for purposes of making interest and principal payments due on indebtedness, to the extent KCS may have to effect those conversions, and could adversely affect the Company s investment in KCSM. This could have a material adverse effect on KCS business and financial condition.

Mexican national politicians are currently focused on certain regional, political and social tensions, and reforms regarding fiscal and labor policies, gas, electricity, social security, and oil have not been and may not be approved. The social and political situation in Mexico could adversely affect the Mexican economy, which in turn could have a material adverse effect on KCS business, financial condition, and results of operation.

Downturns in the United States economy or in trade between the United States and Asia or Mexico and fluctuations in the peso-dollar exchange rate would likely have adverse effects on KCS business and results of operations.

The level and timing of KCS Mexican business activity is heavily dependent upon the level of United States-Mexican trade and the effects of NAFTA on such trade. The Mexican operations depend on the United States and Mexican markets for the products KCSM transports, the relative position of Mexico and the United States in these markets at any given time, and tariffs or other barriers to trade. Downturns in the United States or Mexican economy or in trade between the United States and Mexico would likely have adverse effects on KCS business results of operations and the Company s ability to meet debt service obligations. In addition, KCS has invested significant amounts in developing its intermodal operations at the Port of Lazaro Cardenas, in part to provide Asian importers with an alternative to the west coast ports of the United States, and the level of intermodal traffic depends, to an extent, on the volume of Asian shipments routed through Lazaro Cardenas. Reduction in trading volumes, which may be caused by factors beyond KCS control, including increased government regulations in light of recent concerns regarding the safety and quality of Asian-manufactured products, may adversely affect KCS business and results of operations.

Also, fluctuations in the peso-dollar exchange rates could lead to shifts in the types and volumes of Mexican imports and exports. Although a decrease in the level of exports of some of the commodities that KCSM transports to the United States may be offset by a subsequent increase in imports of other commodities KCSM hauls into Mexico and vice versa, any offsetting increase might not occur on a timely basis, if at all. Future developments in United States-Mexican trade beyond the Company s control may result in a reduction of freight volumes or in an unfavorable shift in the mix of products and commodities KCSM carries.

Any devaluation of the peso would cause the peso cost of KCSM s dollar-denominated debt to increase, adversely affecting its ability to make payments on its indebtedness. Severe devaluation or depreciation of the peso may result in disruption of the international foreign exchange markets and may limit the ability to transfer pesos or to convert pesos into U.S. dollars for the purpose of making timely payments of interest and principal on the non-peso denominated indebtedness. Although the Mexican government currently does not restrict, and for many years has not restricted, the right or ability of Mexican or foreign persons or entities to convert pesos into U.S. dollars or to transfer foreign currencies out of Mexico, the Mexican government could, as in the past, institute restrictive exchange rate policies that could limit the ability to transfer or convert pesos into U.S. dollars or other currencies for the purpose of making timely payments of the U.S. dollar-denominated debt and contractual commitments. Devaluation or depreciation of the peso against the U.S. dollar may also adversely affect U.S. dollar prices for KCS securities. Currency fluctuations are likely to continue to have an effect on KCS financial condition in future periods.

Mexico may experience high levels of inflation in the future which could adversely affect KCS results of operations.

Mexico has a history of high levels of inflation and may experience high inflation in the future. During most of the 1980s and during the mid and late 1990s, Mexico experienced periods of high levels of inflation. The annual rates of inflation for the last three years, as measured by changes in the National Consumer Price Index, as provided by Banco de México, were 3.6% in 2009, 6.5% in 2008 and 3.8% in 2007. A substantial

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increase in the Mexican inflation rate would have the effect of increasing some of KCSM s costs, which could adversely affect its results of operations and financial condition. High levels of inflation may also affect the balance of trade between Mexico and the United States, and other countries, which could adversely affect KCSM s results of operations.

Risk Factors Relating to Ongoing Litigation

KCS is party to various legal proceedings and administrative actions arising in the ordinary course of business including those specifically mentioned below:

KCSM was named as a defendant in a lawsuit, which if adversely resolved, could result in KCS being ordered to return the stock of KCSM to the Federal Government of Mexico, thus losing its Concession to operate its Mexican railroad.

On December 9, 2009, KCSM was notified of a lawsuit filed by Minera México, S.A. de C.V. (Minera México), a subsidiary of Grupo México, S.A.B. de C.V. and an affiliate of Ferromex, against the Federal Government of Mexico, the SCT, Ferrocarriles Nacionales de México (FNM), KCSM, Nafta Rail, S.A. de C.V., a subsidiary of KCS (Nafta Rail), and KCS. The lawsuit claims that after the privatization bidding process for the acquisition of a majority interest in Ferrocarril del Noreste, S.A. de C.V. (FNE) (now KCSM) had concluded in 1997, in which the bidding was awarded to Transportación Ferroviaria Mexicana, S. de R.L. de C.V. (TFM) and the relevant stock purchase agreement was signed, the defendants improperly amended the stock purchase agreement and the purchasers paid a price lower than the price offered. The lawsuit alleges that the Mexican Federal Government, the SCT, FNM, KCSM, Nafta Rail and KCS violated a variety of the rules and regulations associated with the privatization bidding process. As a result of these alleged improprieties, Minera México claims the acquisition of FNE by KCS (through TFM) should be declared null and void and, consequently, the capital stock of FNE should be returned to the Federal Government of Mexico and Minera México, as the second place bidder in the bidding process, should be awarded the right to purchase the capital stock of FNE. On February 9, 2010, Minera México agreed to dismiss this lawsuit.

KCSM is involved in several disputes related to providing service to a Mexican subsidiary of a large U.S. auto manufacturer, which if adversely resolved could have a negative impact on its business and operations.

In March 2008, a Mexican subsidiary of a large U.S. Auto Manufacturer (the Auto Manufacturer) filed an arbitration suit against KCSM under a contract for services to the Auto Manufacturer s plants in Mexico, which, as amended, had a stated termination date of January 31, 2008. The Auto Manufacturer claimed that the contract was implicitly extended and continued in effect beyond its stated termination date. The Auto Manufacturer is seeking a declaration by the arbitrator that the rates being assessed by KCSM are discriminatory, even though the rates being charged are within the legal rate limits set by Mexican law for such freight transportation. KCSM claimed that the contract did in fact expire on its stated termination date, and that services rendered thereafter are thus subject to the general terms and conditions (including rates) applicable in the absence of a specific contract, pursuant to Mexican law. Accordingly, KCSM filed a counterclaim against the Auto Manufacturer to, among other things, recover the applicable rate difference between the rates under the contract and KCSM s rates. On May 18, 2009, the arbitrator issued an award on the first phase of the arbitration proceeding, ruling that the contract had terminated on May 8, 2008. As of the date of this filing, the second phase of the arbitration proceeding, regarding the claim that the rates assessed by KCSM are discriminatory, is in the evidentiary stage and has not been resolved. Management believes the final resolution of these claims will not have any material impact on KCSM s results of operations.

In May 2008, the SCT initiated a proceeding against KCSM at the request of the Auto Manufacturer, alleging that KCSM impermissibly bundled international rail services and engaged in discriminatory pricing practices with respect to rail services provided by KCSM to the Auto Manufacturer. In March 2009, the SCT issued a decision determining that KCSM had engaged in the activities alleged, but imposed no sanction since this was the first time KCSM had engaged in such activities. On May 6, 2009, KCSM challenged the SCT s decision and the appeal is currently pending in the Administrative and Fiscal Federal Court.

On July 23, 2008, the SCT delivered notice to KCSM of new proceedings against KCSM, claiming, among other things, that KCSM refused to grant Ferromex access to certain trackage over which Ferromex alleges it has trackage rights on six different occasions and thus denied Ferromex the ability to provide service to the Auto Manufacturer at this location.

KCSM believes it has defenses to the imposition of sanctions for the forgoing proceedings and is vigorously contesting these allegations. KCSM does not believe that these SCT proceedings will have a material adverse effect on its results of operations or financial condition. However, if KCSM is ultimately sanctioned by the SCT for generic sanctions on five occasions over the term of the Concession, KCSM could be subject to possible future SCT action seeking revocation of the Concession. Revocation of the Concession would materially adversely affect KCSM s results of operations and financial condition.

Item 1B. *Unresolved Staff Comments*

None.

Item 2. *Properties*

Track Configuration

KCSR operates over a railroad system consisting of approximately 3,300 miles of main and branch lines in ten states extending from the midwest and southeast portions of the United States south to the Mexican border. Approximately 400 miles of KCSR s system consists of trackage rights that permit KCSR to operate its trains with its crews over other railroad s tracks.

Under its Concession from the Mexican government, KCSM has the right to operate approximately 2,600 miles of main and branch lines, but does not own the land, roadway, or associated structures and has approximately 700 miles of trackage rights. The Concession requires KCSM to make investments as described in a business plan filed every five years with the Mexican government. KCSM may defer capital expenditures with respect to its five-year business plan with the permission of the SCT. However, should the SCT not grant this permission, KCSM s failure to comply with the commitments in its business plan could result in fines and ultimately the Mexican government revoking the Concession. See Item 1A, Risk Factors KCSM s Mexican Concession is subject to revocation or termination in certain circumstances which would prevent KCSM from operating its railroad and would have a material adverse effect on the Company s business and financial condition.

Equipment Configuration

As of December 31, 2009 and 2008, KCS owned or leased the following units of equipment:

	2009		**2008**	
	Leased	**Owned**	**Leased**	**Owned**
Locomotives	382	536	416	627
Rolling stock:				

Box cars	6,199	875	6,460	1,581
Gondolas	2,856	1,746	3,271	1,781
Hoppers	4,949	882	5,841	923
Flat cars (intermodal and other)	1,335	512	2,071	583
Auto racks	1,761		1,753	
Tank cars	527	15	524	32
Other		51		57
Total	17,627	4,081	19,920	4,957

Average Age (In Years) of Leased and Owned Locomotives:	**2009**	**2008**
Road locomotives	13.5	13.5
All locomotives	20.0	19.3

The Company, at the date of this filing, has approximately 200 locomotives in storage which primarily reflects the current economic environment and some seasonality. Management believes that this equipment will be needed in the foreseeable future as the Company grows and/or economic conditions improve. The Company has continued to depreciate all stored locomotives; older locomotives will be retired in the normal course of business or in some cases disposed of through re-sale.

Property and Facilities

KCS operates numerous facilities, including terminals for intermodal and other freight; rail yards for train-building, switching, storage-in-transit (the temporary storage of customer goods in rail cars prior to shipment) and other activities; offices to administer and manage operations; dispatch centers to direct traffic on the rail network; crew quarters to house train crews along the rail line; and shops and other facilities for fueling, maintenance, and repair of locomotives and maintenance of freight cars and other equipment.

Capital Expenditures

The Company s cash capital expenditures for the three years ended December 31, 2009, 2008, and 2007, and planned 2010 capital expenditures are included in Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources Capital Expenditures . See also Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies and Estimates Capitalization, Depreciation and Amortization of Property and Equipment, Including Concession Assets regarding the Company s policies and guidelines related to capital expenditures.

Item 3. ***Legal Proceedings***

The Company is subject to various legal proceedings and claims that arise in the ordinary course of business. For more information on legal proceedings, see Item 1A, Risk Factors Risks Relating to Ongoing Litigation, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies and Estimates Provision for Environmental Remediation Provision for Personal Injury Claims, and Other Matters Litigation, and Item 8, Financial Statements and Supplementary Data Note 12 Commitments and Contingencies, and Item 9B, Other Information .

Item 4. ***Submission of Matters to a Vote of Security Holders***

No matters were submitted to a vote of security holders during the three months ended December 31, 2009.

Executive Officers of KCS and Subsidiaries

All executive officers are elected annually and serve at the discretion of the Board of Directors. All of the executive officers have employment agreements with KCS and/or its subsidiaries. The mailing address of the principal executive officers is 427 W. 12th Street, Kansas City, Missouri 64105.

Michael R. Haverty Chairman of the Board and Chief Executive Officer 65 The information in the Company s Definitive Proxy Statement under the heading The Board of Directors Directors Serving Until the Annual Meeting of Stockholders in 2012 with respect to Mr. Haverty is incorporated by reference.

David L. Starling KCS President and Chief Operating Officer 60 Mr. Starling joined KCS as President and Chief Operating Officer on July 1, 2008. Mr. Starling has also served as a Director, President and Chief Executive Officer of KCSR since July 1, 2008. He has served as Vice Chairman of the Board of Directors of KCSM since September 2009. Mr. Starling has served as Vice Chairman of the Board of Directors of Panama Canal Railway Company (PCRC), a joint venture company owned equally by KCS and Mi-Jack Products, Inc., since July 2008. Prior to joining KCS, Mr. Starling served as President and Director General of PCRC from 1999 through June 2008. From 1988 through 1999, Mr. Starling served in various leadership positions for American President Lines including most recently vice president Central Asia responsible for China, Taiwan.

Warren K. Erdman Executive Vice President Corporate Affairs 51 Served in this capacity since October 2007. He served as Senior Vice President Corporate Affairs of KCS and KCSR from January 2006 to September 2007. Mr. Erdman served as Vice President Corporate Affairs of KCS from April 15, 1997 to December 31, 2005 and as Vice President Corporate Affairs of KCSR from May 1997 to December 31, 2005. Prior to joining KCS, Mr. Erdman served as Chief of Staff to United States Senator Kit Bond of Missouri from 1987 to 1997.

Larry M. Lawrence Executive Vice President and Assistant to the Chairman 47 Served in this capacity since October 2007. Mr. Lawrence served as Senior Vice President and Assistant to Chairman-Strategies and Staff Studies of KCS from January 2006 to September 2007. Mr. Lawrence served as Assistant to CEO-Staff Studies and Planning of KCS from November 2001 until December 2005. Prior to joining KCS in 2001, Mr. Lawrence was a strategy consultant for 15 years with McKinsey, A. T. Kearney and KPMG.

Patrick J. Ottensmeyer Executive Vice President Sales and Marketing 52 Served in this capacity since October 16, 2008. Mr. Ottensmeyer joined KCS in May 2006 as Executive Vice President and Chief Financial Officer. Prior to joining KCS, Mr. Ottensmeyer served as Chief Financial Officer of Intranasal Therapeutics, Inc. from 2001 to May 2006. From 2000 to 2001, he served as Corporate Vice President Finance and Treasurer for Dade-Behring Holdings, Inc. From 1993 to 1999, Mr. Ottensmeyer served as Vice President Finance and Treasurer at Burlington Northern Santa Fe Corporation and BNSF Railway and their predecessor companies.

Michael W. Upchurch Executive Vice President and Chief Financial Officer 49 Served in this capacity since October 16, 2008. Mr. Upchurch joined KCS in March 2008 as Senior Vice President Purchasing and Financial Management. Prior to joining KCS, Mr. Upchurch served as Senior Vice President Finance of Red Development LLC, from December 2007 through February 2008. From September 2006 through December 2007, Mr. Upchurch worked as an independent consultant providing financial consulting services. From 1990 through September 2006, Mr. Upchurch served in various senior financial leadership positions at Sprint Nextel Corporation and its predecessor, Sprint Corporation, including Senior Vice President Financial Operations, Senior Vice President Finance Sprint Business Solutions and Senior Vice President Finance Long Distance Division.

José Guillermo Zozaya Delano President and Executive Representative KCSM 57 Has served in this position since April 20, 2006. Mr. Zozaya has 35 years of experience in law and government relations, most recently as the legal and government relations director for ExxonMobil México, S.A. de C.V., where he spent nine years prior to joining KCSM.

John E. Derry Senior Vice President of Human Resources 42 Served in this capacity since July 2008. He served as Vice President of Human Resources from February 2008 until July 2008. Mr. Derry joined KCS from YRC Worldwide, Inc. where he served in various Human Resource functions from January 2004 to February 2008. From September 2006 to February 2008, Mr. Derry served as Vice President of Human Resources for Yellow Transportation. Prior to joining YRC Worldwide, Inc. Mr. Derry spent 17 years with General Mills Inc. in various operations, labor relations and human resource roles.

Mary K. Stadler Senior Vice President and Chief Accounting Officer 50 Served in this capacity since March 2, 2009. From April 1990 through August 2008, Ms. Stadler served in various finance leadership positions at Sprint Nextel Corporation and its predecessor, Sprint Corporation, including Vice President Finance Operations and most recently served as its Vice President Assistant Controller.

Paul J. Weyandt Senior Vice President Finance and Treasurer 56 Served in this capacity since April 2005. He served as Vice President and Treasurer of KCS and of KCSR from September 2001 until March 2005. Before joining KCS, Mr. Weyandt was a consultant to the Structured Finance Group of GE Capital Corporation from May 2001 to September 2001. Prior to consulting, Mr. Weyandt spent 23 years with BNSF Railway, most recently as Assistant Vice President Finance and Assistant Treasurer.

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William J. Wochner Senior Vice President and Chief Legal Officer 62 Served in this capacity since February 2007. He served as Vice President and Interim General Counsel from December 2006 to January 2007. From September 2006 to December 2006, Mr. Wochner served as Vice President and Associate General Counsel. From March 2005 to September 2006, Mr. Wochner served as Vice President Sales and Marketing/Contracts for KCSR. From February 1993 to March 2005, Mr. Wochner served as Vice President and General Solicitor of KCSR.

There are no arrangements or understandings between the executive officers and any other person pursuant to which the executive officer was or is to be selected as an officer of KCS, except with respect to the executive officers who have entered into employment agreements designating the position(s) to be held by the executive officer.

None of the above officers is related to another, or to any of the directors of KCS, by family.

Part II

Item 5. *Market for KCS Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities*

Market Information

The Company s common stock is traded on the New York Stock Exchange under the ticker symbol KSU . Information as to the high and low sales price of the Company s common and preferred stock for the years ended December 31, 2009 and 2008 is set forth in Note 15 to the Consolidated Financial Statements in Item 8 of this Form 10-K and is incorporated by reference herein.

Dividend Policy

Common Stock. KCS has not declared any cash dividends on its common stock during the last five fiscal years and it does not anticipate making any cash dividend payments to common shareholders in the foreseeable future. Pursuant to KCSR s credit agreement, KCS is prohibited from the payment of cash dividends on its common stock.

Preferred Stock. Kansas City Southern is restricted from paying cash dividends on its Series D Preferred Stock when its coverage ratio (as defined in the indentures for KCSR s 8.0% Senior Notes and 13.0% Senior Notes) is less than 2.0:1. It is the Company s intention to pay timely dividends on all preferred stock in cash when dividend payments are not restricted under the covenants of its various debt agreements and the Company has adequate levels of liquidity. In the event that dividends on the Series D Preferred Stock are in arrears for six consecutive quarters (or an equivalent number of days in the aggregate, whether or not consecutive), holders of the Series D Preferred Stock, as applicable, will be entitled to elect two of the authorized number of directors at the next annual stockholders meeting, and at each subsequent stockholders meeting until such time as all accumulated dividends are paid on the Series D Preferred Stock, as applicable, or set aside for payment.

Holders

There were 4,446 record holders of KCS common stock on February 4, 2010; however, the number of actual holders of KCS common stock is greater due to the practice of brokerage firms registering many shares for clients in the brokerage firm s name.

Securities Authorized for Issuance Under Equity Compensation Plans

See Part III, Item 12, Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters for information about securities authorized for issuance under KCS equity compensation plans.

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Performance Graph

The following graph shows the changes in value over the five years ended December 31, 2009, of an assumed investment of $100 in: (i) KCS common stock; (ii) the stocks that comprise the Dow Jones Transportation Average Index(1); and (iii) the stocks that comprise the S&P 500 Index(2). The table following the graph shows the value of those investments on December 31 for each of the years indicated. The values for the assumed investments depicted on the graph and in the table have been calculated assuming that any cash dividends are reinvested.

COMPARISON OF FIVE YEAR CUMULATIVE TOTAL RETURN
Among Kansas City Southern, the S&P 500 Index
and the Dow Jones Transportation Index

	2004	2005	2006	2007	2008	2009
Kansas City Southern	100.00	137.79	163.45	193.63	107.45	187.76
S&P 500	100.00	104.91	121.48	128.16	80.74	102.11
Dow Jones Transportation Average	100.00	111.27	120.01	127.37	102.44	126.00

(1) The Dow Jones Transportation Average is an index prepared by Dow Jones & Co., Inc., an independent company.

(2) The S&P 500 is an index prepared by Standard and Poor s Corporation, an independent company. The S&P 500 Index reflects the change in weighted average market value for 500 companies whose shares are traded on the New York Stock Exchange, American Stock Exchange and the Nasdaq Stock Market.

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Item 6. *Selected Financial Data*

The selected financial data below *(in millions, except per share amounts)* should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations included under Item 7 of this Form 10-K as well as the consolidated financial statements and the related notes.

	2009	2008	2007	2006	2005(i)
Results of Operations					
Revenues	$ 1,480.2	$ 1,852.1	$ 1,742.8	$ 1,659.7	$ 1,352.0
Operating expenses	1,212.0	1,461.9	1,380.4	1,355.4	1,289.7
Operating income	$ 268.2	$ 390.2	$ 362.4	$ 304.3	$ 62.3
Net income	$ 69.0	$ 184.2	$ 154.2	$ 109.2	$ 83.1
Earnings per common share:					
Basic	$ 0.61	$ 2.02	$ 1.77	$ 1.20	$ 1.21
Diluted	0.61	1.86	1.57	1.08	1.10
Financial Position					
Total assets	$ 5,479.1	$ 5,439.2	$ 4,928.2	$ 4,637.3	$ 4,423.6
Total debt obligations, including current portion	1,980.0	2,086.1	1,755.9	1,757.0	1,860.6
Total stockholders equity	2,058.8	1,911.5	1,726.3	1,582.4	1,426.2
Total equity(ii)	2,341.6	2,185.2	1,969.3	1,682.7	1,426.2
Other Data Per Common Share					
Cash dividends per common share	$	$	$	$	$

(i) The 2005 results reflect the consolidation of Mexrail effective January 1, 2005 and KCSM effective April 1, 2005.

(ii) The adoption of the new accounting guidance on noncontrolling interests has resulted in the reclassification of amounts previously attributable to minority interest, now referred to as noncontrolling interest, to a separate component of total equity in the consolidated balance sheet.

Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations*

The following discussion is intended to clarify and focus on Kansas City Southern s results of operations, certain changes in its financial position, liquidity, capital structure and business developments for the periods covered by the consolidated financial statements included under Item 8 of this Form 10-K. This discussion should be read in conjunction with the included consolidated financial statements, the related notes, and other information included in this report.

CAUTIONARY INFORMATION

The discussions set forth in this Annual Report on Form 10-K may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. In addition, management may make forward-looking statements orally or in other writings, including, but not limited to, in press releases, quarterly earnings calls, executive presentations, in the annual report to stockholders and in other filings with the Securities and Exchange Commission. Readers can identify these forward-looking statements by the use of such verbs as expects, anticipates, believes or similar verbs or conjugations of such verbs. These statements involve a number of risks and uncertainties. Actual results could materially differ from those anticipated by such forward-looking statements. Such differences could be caused by a number of factors or combination of factors including, but not limited to, the factors identified below and those discussed under Item 1A of this Form 10-K, Risk

Factors. Readers are strongly encouraged to consider these factors and the following factors when evaluating any forward-looking statements concerning the Company:

fluctuations in the market price for the Company s common stock;

KCS dividend policy and restrictions on its ability to pay dividends on its common stock;

KCS high degree of leverage;

the Company s potential need for and ability to obtain additional financing;

KCS ability to successfully implement its business strategy, including the strategy to convert customers from using trucking services to rail transportation services;

the impact of competition, including competition from other rail carriers, trucking companies and maritime shippers in the United States and Mexico;

United States, Mexican and global economic, political and social conditions;

the effects of the North American Free Trade Agreement, or NAFTA, on the level of trade among the United States, Mexico and Canada;

uncertainties regarding the litigation KCS faces and any future claims and litigation;

the effects of employee training, stability of the existing information technology systems, technological improvements and capital expenditures on labor productivity, operating efficiencies and service reliability;

the adverse impact of any termination or revocation of KCSM s Concession by the Mexican government;

legal or regulatory developments in the United States, Mexico or Canada;

KCS ability to generate sufficient cash, including its ability to collect on its customer receivables, to pay principal and interest on its debt, meet its obligations and fund its other liquidity needs;

the effects of adverse general economic conditions affecting customer demand and the industries and geographic areas that produce and consume the commodities KCS carries;

material adverse changes in economic and industry conditions, including the availability of short and long-term financing, both within the United States and Mexico and globally;

natural events such as severe weather, fire, floods, hurricanes, earthquakes or other disruptions to the Company s operating systems, structures and equipment or the ability of customers to produce or deliver their products;

KCS business may be affected by market and regulatory responses to climate change;

disruption in fuel supplies, changes in fuel prices and the Company s ability to assess fuel surcharges;

KCS ability to attract and retain qualified management personnel;

changes in labor costs and labor difficulties, including work stoppages affecting either operations or customers abilities to deliver goods for shipment;

credit risk of customers and counterparties and their failure to meet their financial obligations;

the outcome of claims and litigation, including those related to environmental contamination, personal injuries, and occupational illnesses arising from hearing loss, repetitive motion and exposure to asbestos and diesel fumes;

acts of terrorism or risk of terrorist activities;

war or risk of war;

political and economic conditions in Mexico and the level of trade between the United States and Mexico; and

legislative, regulatory, or legal developments involving taxation, including enactment of new foreign, federal or state income or other tax rates, revisions of controlling authority, and the outcome of tax claims and litigation.

Forward-looking statements reflect only as of the date on which they are made. The Company will not update any forward-looking statements to reflect future events, developments, or other information. If KCS does update one or more forward-looking statements, no inference should be drawn that additional updates will be made regarding that statement or any other forward-looking statements.

CORPORATE OVERVIEW

Kansas City Southern, a Delaware corporation, is a transportation holding company that has railroad investments in the U.S., Mexico and Panama. In the U.S., the Company serves the central and south central U.S. Its international holdings serve northeastern and central Mexico and the port cities of Lazaro Cardenas, Tampico and Veracruz, and a fifty percent interest in Panama Canal Railway Company provides ocean-to-ocean freight and passenger service along the Panama Canal. KCS North American rail holdings and strategic alliances are primary components of a NAFTA railway system, linking the commercial and industrial centers of the U.S., Canada and Mexico. Its principal subsidiaries and affiliates include the following:

The Kansas City Southern Railway Company (KCSR), a wholly-owned subsidiary;

Kansas City Southern de México, S.A. de C.V. (KCSM), which became a wholly-owned subsidiary as of April 1, 2005, when KCS completed its acquisition of KCSM;

Mexrail, Inc. (Mexrail), a wholly-owned consolidated subsidiary; which, in turn, wholly owns The Texas Mexican Railway Company (Tex-Mex);

Meridian Speedway, LLC (MSLLC), a seventy-two percent owned consolidated affiliate;

Panama Canal Railway Company (PCRC), a fifty percent owned unconsolidated affiliate, that provides international container shipping companies with a railway transportation option in lieu of the Panama Canal and owns all of the common stock of Panarail Tourism Company (Panarail);

Southern Capital Corporation, LLC (Southern Capital), a fifty percent owned unconsolidated affiliate that owns and leases locomotives and other equipment; and

Ferrocarril y Terminal del Valle de México, S.A. de C.V. (FTVM), a twenty-five percent owned unconsolidated affiliate that provides railroad services as well as ancillary services in the greater Mexico City area.

KCS, as the holding company, supplies its various subsidiaries with managerial, legal, tax, financial and accounting services, in addition to management services for various other non-operating investments.

EXECUTIVE SUMMARY

2009 Financial Overview

This has been a pivotal year for Kansas City Southern. With the uncertain state of the world economy, KCS, like so many other companies, has had to make difficult decisions about where to invest valuable resources for growth in the future. The Company has remained focused on maximizing the value of the cross border network and the vision to be a strong, independent transportation company that consistently delivers exceptional service to its customers and increasing value to its shareholders. Management believes the Company s efforts leave it well positioned as the global economy begins to recover.

The Company reported 2009 earnings of $0.61 per diluted share on consolidated net income of $68.0 million for the year ended December 31, 2009, compared to annual earnings of $1.86 per diluted share on consolidated net income of $183.9 million for 2008. This earnings decline reflects a 20% reduction in revenues in 2009 as compared to 2008. This significant revenue decline was primarily driven by the economic downturn that has affected most business sectors, and has resulted in industry-wide declines in carload/unit volumes. The revenue declines were partially offset by reduced fuel costs, reflecting reduced consumption and prices, and increased efficiency. The revenue declines were further mitigated by the Company s cost containment measures including modifications to the Company s operations in response to volumes; however, due to increased depreciation and amortization expense and because certain operating costs are fixed in the short-term, operating expenses as a percentage of revenues increased to 81.9% in 2009, as compared to 78.9% in 2008.

Cash flows from operations decreased to $292.9 million as compared to $413.0 million for the years ended December 31, 2009 and 2008, respectively. The decrease is primarily due to lower carload/unit volumes as previously discussed. Capital expenditures are a significant use of cash for KCS and were $349.2 million for 2009, a 35% decrease compared to 2008. Despite the downturn in the economy, the Company continued to focus on the completion of strategic projects. During the second quarter of 2009, the Company completed construction and opened the newly rehabilitated line from Rosenberg to Victoria, Texas which diverts KCSR s operations from 157 miles of trackage rights to a more direct route, reducing the mileage between Laredo and Houston/Beaumont by 67 miles. In addition, the line reopened regular train service to the area, bringing needed rail capacity to south Texas to reduce highway congestion and the number of trucks on Texas highways. It also makes regional business more competitive, leading to future growth and jobs.

During 2009, the Company was focused on improving KCS financial condition and liquidity position. KCSM paid off its bank term loan and revolver using the proceeds of a $200.0 million debt offering in the first quarter. KCS also strengthened its balance sheet and liquidity through the sale of 4,330,208 shares of common stock with net proceeds of $73.9 million.

RESULTS OF OPERATIONS

Year Ended December 31, 2009, compared with the Year Ended December 31, 2008

The following summarizes the consolidated income statement components of KCS *(in millions):*

			Change	
	2009	**2008**	**Dollars**	**Percent**
Revenues	$ 1,480.2	$ 1,852.1	$ (371.9)	(20)%
Operating expenses	1,212.0	1,461.9	(249.9)	(17)%
Operating income	268.2	390.2	(122.0)	(31)%
Equity in net earnings of unconsolidated affiliates	7.7	18.0	(10.3)	(57)%
Interest expense	(173.7)	(138.9)	(34.8)	25%
Debt retirement costs	(5.9)	(5.6)	(0.3)	5%
Foreign exchange gain (loss)	2.1	(21.0)	23.1	(110)%
Other income, net	5.2	6.0	(0.8)	(13)%
Income before income taxes and noncontrolling interest	103.6	248.7	(145.1)	(58)%
Income tax expense	34.6	64.5	(29.9)	(46)%
Net income	69.0	184.2	(115.2)	(63)%

Noncontrolling interest	1.0	0.3	0.7	233%
Net income attributable to Kansas City Southern and subsidiaries	$ 68.0	$ 183.9	$ (115.9)	(63)%

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Revenues

The following summarizes revenues *(in millions)* and carload/unit statistics *(in thousands)* and revenue per carload/unit:

	Revenues			Carloads and Units			Revenue per Carload/Unit		
	2009	2008	% Change	2009	2008	% Change	2009	2008	% Change
Chemical and petroleum	$ 323.4	$ 347.8	(7)%	238.3	240.2	(1)%	$ 1,357	$ 1,448	(6)%
Industrial and consumer products	344.4	508.6	(32)%	267.0	367.6	(27)%	1,290	1,384	(7)%
Agriculture and minerals	360.0	455.0	(21)%	246.3	293.3	(16)%	1,462	1,551	(6)%
Total general commodities	1,027.8	1,311.4	(22)%	751.6	901.1	(17)%	1,367	1,455	(6)%
Coal	187.2	203.7	(8)%	301.2	301.3		622	676	(8)%
Intermodal	143.4	160.6	(11)%	516.4	520.9	(1)%	278	308	(10)%
Automotive	52.9	105.6	(50)%	51.7	101.6	(49)%	1,023	1,039	(2)%
Subtotal	1,411.3	1,781.3	(21)%	1,620.9	1,824.9	(11)%	$ 871	$ 976	(11)%
Other revenue	68.9	70.8	(3)%						
Total revenues(i)	$ 1,480.2	$ 1,852.1	(20)%						
(i) Included in revenues:									
Fuel surcharge	$ 77.9	$ 200.3							

Freight revenues include both revenue for transportation services and fuel surcharges. For the year ended December 31, 2009, revenues decreased $371.9 million compared to the prior year, primarily due to the overall decrease in carload/unit volumes resulting from the downturn in the economy, decreased fuel surcharge, and the effect of unfavorable fluctuations in the value of the U.S. dollar against the value of the Mexican peso for revenues denominated in Mexican pesos, partially offset by an increase in core pricing. Revenue per carload/unit decreased by 11% for the year ended December 31, 2009, reflecting unfavorable commodity mix in addition to the factors discussed above.

KCS s fuel surcharge is a mechanism to adjust revenue based upon changing fuel prices. Fuel surcharges are calculated differently depending on the type of commodity transported. For most commodities, fuel surcharge is calculated using a fuel price from a prior time period that can be as much as 60 days earlier. In a period of volatile fuel prices or changing customer business mix, changes in fuel expense and fuel surcharge may significantly differ.

The following discussion provides an analysis of revenues by commodity group:

Revenues by commodity group for 2009

Chemical and petroleum. Revenues decreased $24.4 million for the year ended December 31, 2009, primarily due to a decline in the fuel surcharge and unfavorable fluctuations in the value of the U.S. dollar against the value of the Mexican peso. Revenues decreased in chemical products used to manufacture glass and paint as a result of the downturn in the automotive and construction industries. Petroleum products also declined year over year due to an unfavorable customer mix, partially offset by an increase in volumes.

Industrial and consumer products. Revenues decreased $164.2 million for the year ended December 31, 2009, due to decreases in volume, fuel surcharge and unfavorable fluctuations in the value of the U.S. dollar against the value of the Mexican peso. Volumes in metals and scrap decreased as a result of weak demand for pipe used in oil drilling and slab shipments used in automobiles and appliances. Forest products were affected by decreased demand that resulted in temporary mill shutdowns to bring inventory in line with demand.

Agriculture and minerals. Revenues decreased $95.0 million for the year ended December 31, 2009, due to decreases in volume, fuel surcharge and unfavorable fluctuations in the value of the U.S. dollar against the value of the Mexican peso. Grain traffic accounted for the majority of the decrease as traffic patterns shifted due to a combination of factors. There was an abundant supply of grain, primarily corn that was grown in Mexico, as well as an abundant supply of alternative grains which drove a change in origination and traffic patterns. In addition, significantly lower vessel freight rates from U.S. ports along the Gulf of Mexico drove a substitution from rail to vessel for certain shipments to Mexico. The decrease was partially offset by an increase in food products revenue driven by new business.

Coal. Revenues decreased $16.5 million for the year ended December 31, 2009, primarily due to a reduction in fuel surcharge and a decline in petroleum coke shipments going to the cement and steel industry markets in Mexico, which continue to be affected by the decline in construction projects. Unit coal volumes to existing electric generation customers increased during 2009; however, related revenue per unit declined primarily due to a reduction in fuel surcharge.

Intermodal. Revenues decreased $17.2 million for the year ended December 31, 2009, primarily due to a decline in the fuel surcharge and an unfavorable change in product mix. The decrease in volume is due to the loss of business driven by unfavorable fluctuations in the value of the U.S. dollar against the value of the Mexican peso, reduced demand in consumer retail, and aggressive truck competition. The volume reduction was partially offset by an increase in haulage business and a fourth quarter increase in cross border automotive parts shipments.

Automotive. Revenues decreased $52.7 million for the year ended December 31, 2009, due to a decline in volume and unfavorable fluctuations in the value of the U.S. dollar against the value of the Mexican peso. The volume decrease was driven by the continued overall downturn in the automotive industry caused by consumer uncertainty and tightening credit markets. In addition, the bankruptcy of two U.S. automotive companies resulted in several unscheduled plant shutdowns in the first half of 2009. The decline in volume was partially offset by government incentive programs that were established during the second and third quarters of 2009.

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Operating expenses

Operating expenses, as shown below (*in millions*), decreased $249.9 million for the year ended December 31, 2009, when compared to the same period in 2008, primarily due to decreased carload/unit volumes, fuel expense, cost containment measures and the effect of favorable fluctuations in the value of the U.S. dollar against the value of the Mexican peso for operating expenses denominated in Mexican pesos. Certain prior period amounts have been reclassified to conform to the current year presentation.

			Change	
	2009	**2008**	**Dollars**	**Percent**
Compensation and benefits	$ 328.8	$ 369.9	$ (41.1)	(11)%
Purchased services	171.3	209.1	(37.8)	(18)%
Fuel	189.4	324.6	(135.2)	(42)%
Equipment costs	164.1	178.6	(14.5)	(8)%
Depreciation and amortization	182.5	168.6	13.9	8%
Casualties and insurance	43.1	72.7	(29.6)	(41)%
Materials and other	132.8	138.4	(5.6)	(4)%
Total operating expenses	$ 1,212.0	$ 1,461.9	$ (249.9)	(17)%

Compensation and benefits. Compensation and benefits decreased $41.1 million for the year ended December 31, 2009, compared to 2008, primarily due to labor reductions in response to declining carload/unit volumes, with further expense decreases in Mexico due to favorable fluctuations in the value of the U.S. dollar against the value of the Mexican peso.

Purchased services. Purchased services decreased $37.8 million for the year ended December 31, 2009, compared to 2008, primarily due to lower locomotive maintenance expense as a result of fewer locomotives in service, newer fleet and renegotiated maintenance contracts. Corporate expenses decreased as a result of cost containment measures. In addition, the Company recognized a deferred credit of $6.1 million related to the partial cancellation of a maintenance contract in 2009.

Fuel. Fuel expense decreased $135.2 million for the year ended December 31, 2009, compared to 2008, primarily due to lower diesel fuel prices, lower consumption driven by decreased carload/unit volumes, and increased fuel efficiency.

Equipment costs. Equipment costs decreased $14.5 million for the year ended December 31, 2009, compared to 2008 primarily due to a decrease in the use of other railroads freight cars.

Depreciation and amortization. Depreciation and amortization increased $13.9 million for the year ended December 31, 2009, compared to 2008, primarily due to a larger asset base, partially offset by the impact of lower rates based on the scheduled depreciation study in 2009 and a change in the estimated useful lives of certain Mexico concession assets.

Casualties and insurance. Casualties and insurance expenses decreased $29.6 million for the year ended December 31, 2009, compared to 2008, primarily due to fewer derailments and lower average cost per derailment. In addition, the Company reduced the personal injury reserve, reflecting favorable claims experience.

Materials and other. Materials and other decreased $5.6 million for year ended December 31, 2009, compared to 2008, primarily due to lower employee expenses and lower materials and supplies used for the maintenance of track and locomotives. The decrease was partially offset by legal settlements in 2009. In addition, 2008 included a reduction of a legal reserve.

Non-Operating Expenses

Equity in Net Earnings of Unconsolidated Affiliates. Equity in earnings from unconsolidated affiliates was $7.7 million and $18.0 million for the years ended December 31, 2009 and 2008, respectively. Significant components of this change were as follows:

Equity in earnings from the operations of PCRC was $2.9 million for the year ended December 31, 2009, compared to $8.2 million for 2008. The decrease is primarily due to a reduction in container volume attributable to the downturn in the economy.

Equity in earnings of Southern Capital was $3.5 million for the year ended December 31, 2009, compared to $5.1 million for 2008. The decrease is primarily due to the loss on sale of railcars and other equipment in 2009, lower lease income due to lease expirations and larger casualties expense recorded in 2009.

KCSM s equity in earnings of FTVM was $1.3 million for the year ended December 31, 2009, compared to $4.7 million for 2008. The decrease is primarily due to the decline in volume due to the downturn in the Mexican economy and a favorable adjustment related to negotiations of a maintenance agreement recorded in 2008.

Interest Expense. Interest expense increased $34.8 million for the year ended December 31, 2009, compared to 2008, primarily due to higher debt balances and average interest rates. In 2009 and 2008, the Company recorded interest expense reductions as a result of various tax-related settlements and in 2009 recognized interest expense from an unfavorable outcome related to a legal dispute.

Debt Retirement Costs. Debt retirement costs increased $0.3 million for the year ended December 31, 2009, compared to the year ended December 31, 2008. In January 2009, KCSR redeemed its 71/2% Senior Notes due June 15, 2009 and expensed $5.3 million for cash tender offer expenses and unamortized debt issuance costs. In addition, in March of 2009, KCSM repaid all amounts outstanding under the 2007 KCSM Credit Agreement and upon termination, wrote-off the unamortized debt issuance cost related to this debt. In May 2008, KCSR redeemed its 91/2% Senior Notes due October 1, 2008 and expensed $5.6 million for cash tender offer expenses and unamortized debt issuance costs.

Foreign Exchange. For the years ended December 31, 2009 and 2008, the foreign exchange was a gain of $2.1 million and a loss of $21.0 million, respectively, primarily due to fluctuations in the value of the U.S. dollar versus the value of the Mexican peso.

Other Income, net. Other income, net, decreased $0.8 million for the year ended December 31, 2009 compared to the same period in 2008, primarily due to decreases in royalty, interest and dividend income, partially offset by gains on sale of property.

Income Tax Expense. For the year ended December 31, 2009, the Company s income tax expense was $34.6 million, a decrease of $29.9 million as compared to $64.5 million for the year ended December 31, 2008. The effective tax rate was 33.4% and 25.9% for the years ended December 31, 2009 and 2008, respectively. The changes in income tax expense and the effective tax rate were due to lower pre-tax income in 2009, a shift in the composition of income in different taxing jurisdictions, foreign exchange rate fluctuations and a change in Mexican tax rates for tax years 2010 through 2013.

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Year Ended December 31, 2008, compared with the Year Ended December 31, 2007

The following summarizes the consolidated income statement components of KCS *(in millions):*

	2008	2007	Change Dollars	Change Percent
Revenues	$ 1,852.1	$ 1,742.8	$ 109.3	6%
Operating expenses	1,461.9	1,380.4	81.5	6%
Operating income	390.2	362.4	27.8	8%
Equity in net earnings of unconsolidated affiliates	18.0	11.4	6.6	58%
Interest expense	(138.9)	(156.7)	17.8	(11)%
Debt retirement costs	(5.6)	(6.9)	1.3	(19)%
Foreign exchange loss	(21.0)	(0.9)	(20.1)	2,233%
Other income, net	6.0	12.0	(6.0)	(50)%
Income before income taxes and noncontrolling interest	248.7	221.3	27.4	12%
Income tax expense	64.5	67.1	(2.6)	(4)%
Net income	184.2	154.2	30.0	19%
Noncontrolling interest	0.3	0.4	(0.1)	(25)%
Net income attributable to Kansas City Southern and subsidiaries	$ 183.9	$ 153.8	$ 30.1	20%

Revenues

The following summarizes revenues *(in millions)* and carload/unit statistics *(in thousands)* and revenue per carload/unit.

	Revenues			Carloads and Units			Revenue per Carload/Unit		
	2008	2007	% Change	2008	2007	% Change	2008	2007	% Change
Chemical and petroleum	$ 347.8	$ 320.4	9%	240.2	228.3	5%	$ 1,448	$ 1,403	3%
Industrial and consumer products	508.6	501.1	1%	367.6	393.8	(7)%	1,384	1,272	9%
Agriculture and minerals	455.0	403.7	13%	293.3	297.9	(2)%	1,551	1,355	14%
	1,311.4	1,225.2	7%	901.1	920.0	(2)%	1,455	1,332	9%

Total general commodities									
Coal	203.7	193.0	6%	301.3	314.1	(4)%	676	614	10%
Intermodal	160.6	143.1	12%	520.9	526.4	(1)%	308	272	13%
Automotive	105.6	110.9	(5)%	101.6	108.4	(6)%	1,039	1,023	2%
Subtotal	1,781.3	1,672.2	7%	1,824.9	1,868.9	(2)%	$ 976	$ 895	9%
Other revenue	70.8	70.6							
Total revenues(i)	$ 1,852.1	$ 1,742.8	6%						
(i) Included in revenues:									
Fuel surcharge	$ 200.3	$ 133.2							

For the year ended December 31, 2008, revenues increased $109.3 million compared to the prior year, primarily due to targeted rate increases, increased fuel surcharge, and new business opportunities partially offset by an overall decrease in carload/unit volumes. A large portion of the volume decrease in 2008 was

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realized in the fourth quarter resulting from the downturn in the economy. The effect of fluctuations in the value of the U.S. dollar against the value of the Mexican peso was not significant for the year ended December 31, 2008.

KCS s fuel surcharge is a mechanism to adjust revenue based upon changing fuel prices. Fuel surcharges are calculated differently depending on the type of commodity transported. For most commodities, fuel surcharge is calculated using a fuel price from a prior time period that can be as much as 60 days earlier. In a period of volatile fuel prices or changing customer business mix, changes in fuel expense and fuel surcharge may significantly differ.

The following discussion provides an analysis of revenues by commodity group.

Revenues by commodity group for 2008

Chemical and petroleum. Revenues increased $27.4 million for the year ended December 31, 2008, due to targeted rate increases, fuel surcharge increases, and increased traffic volumes from new business primarily in plastic products.

Industrial and consumer products. Revenues increased $7.5 million for the year ended December 31, 2008 primarily due to higher demand in the metals and scrap from coil and pipe products as well as new business, targeted rate increases, and fuel surcharge increases. These increases were partially offset by decreases in volume due to the declining housing market which impacted forest products and declines in beer export volume from Mexico reflected in other products due to a large beer producer relocating to an area not served by the KCS network in the first quarter of 2008.

Agriculture and minerals. Revenues increased $51.3 million for the year ended December 31, 2008, driven by targeted rate increases, fuel surcharge increases and increased length of haul of cross border traffic from customers moving their business from various competitors onto the KCS network. Grain accounted for the majority of the revenue increase even with a later-than-forecasted harvest decreasing volume. This volume decrease was partially offset by increased traffic in ores and minerals, particularly in rock and sand products, due to the strong energy sector.

Coal. Revenues increased $10.7 million for the year ended December 31, 2008, due to an increase in fuel surcharge participation, increased length of haul, rate increases, and improved system velocity on coal trains in the second half of 2008. The increase was partially offset by lower volumes during the first half of 2008 due to higher stockpile levels, utility customer maintenance outages, and adverse weather in the Midwest affecting deliveries.

Intermodal. Revenues increased $17.5 million for the year ended December 31, 2008, driven by targeted rate increases and fuel surcharge increases. Volumes of imports and exports of intermodal containerized business originating and terminating at the Port of Lazaro Cardenas increased and were offset by decreases in automotive related traffic (parts distribution) as well as certain haulage business.

Automotive. Revenues decreased $5.3 million for the year ended December 31, 2008. Decreases were driven by the overall downturn in the automotive industry as higher cost of fuel and tightening credit markets have automobile manufacturers re-tooling factories to build more fuel efficient vehicles as well as developing programs to incent the purchase of new cars. The overall decrease was partially offset by targeted rate increases and new longer haul traffic in the first half of 2008.

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Operating expenses

For the year ended December 31, 2008, operating expenses increased $81.5 million. The effect of fluctuations in the value of the U.S. dollar against the value of the Mexican peso was not significant for the year ended December 31, 2008. The following summarizes the Company s operating expenses *(in millions).* Certain prior period amounts have been reclassified to conform to the current year presentation.

			Change	
	2008	**2007**	**Dollars**	**Percent**
Compensation and benefits	$ 369.9	$ 384.0	$ (14.1)	(4)%
Purchased services	209.1	198.4	10.7	5%
Fuel	324.6	270.2	54.4	20%
Equipment costs	178.6	184.6	(6.0)	(3)%
Depreciation and amortization	168.6	159.0	9.6	6%
Casualties and insurance	72.7	69.3	3.4	5%
Materials and other	138.4	114.9	23.5	20%
Total operating expenses	$ 1,461.9	$ 1,380.4	$ 81.5	6%

Compensation and benefits. Compensation and benefits decreased $14.1 million for the year ended December 31, 2008, compared to 2007. Increases due to annual wage and salary rate increases and severance obligations were offset by lower share-based compensation expense as a result of forfeitures, decreases in incentive compensation and an increase in capitalized overhead rates based on updated studies.

Purchased services. Purchased services increased $10.7 million for the year ended December 31, 2008, compared to 2007, primarily due to an increase in locomotive maintenance expense in Mexico, equipment and track structure maintenance expenses, corporate expenses and switching costs.

Fuel. Fuel expense increased $54.4 million for the year ended December 31, 2008, compared to 2007, primarily due to higher diesel fuel prices, partially offset by lower consumption in certain parts of the network and increased fuel efficiency driven primarily by older locomotives being replaced with new locomotives through a strategic initiative in 2007 and 2008.

Equipment costs. Equipment costs decreased $6.0 million for the year ended December 31, 2008, compared to 2007, due to a decrease in the use of other railroads freight cars.

Depreciation and amortization. Depreciation and amortization increased $9.6 million for the year ended December 31, 2008, compared to 2007, primarily due to a larger asset base.

Casualties and insurance. Casualties and insurance expenses increased $3.4 million for the year ended December 31, 2008, compared to 2007, primarily due to the lower expense in 2007 from a favorable reinsurance litigation settlement received in the second quarter of 2007, and damages caused by the hurricanes in the third quarter of 2008, partially offset by decreases in personal injury and derailment expenses.

Materials and other. Materials and other increased $23.5 million for year ended December 31, 2008, compared to 2007, due to increased materials and supplies used for the maintenance of freight cars and locomotives and lower sales and use tax in the first quarter of 2007 as a result of a favorable tax ruling.

Non-Operating Expenses

Equity in Net Earnings of Unconsolidated Affiliates. Equity in earnings from unconsolidated affiliates was $18.0 million and $11.4 million for the years ended December 31, 2008 and 2007, respectively. Significant components of this change were as follows:

Equity in earnings from the operations of PCRC was $8.2 million for the year ended December 31, 2008, compared to $3.7 million in 2007. The increase is primarily due to increased freight revenue driven by higher volume from new and existing customers.

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Equity in earnings of Southern Capital was $5.1 million for the year ended December 31, 2008, compared to $4.8 million in 2007. The increase is primarily attributed to increased lease income as well as a reduction in interest and administrative expenses.

KCSM s equity in earnings of FTVM was $4.7 million for the year ended December 31, 2008, compared to $2.9 million in 2007. The increase primarily reflects reduced maintenance expense in 2008 and a non-recurring prior year loss recorded in 2007.

Interest Expense. Interest expense decreased $17.8 million for the year ended December 31, 2008, compared to the same period in 2007, primarily due to lower interest rates related to debt refinancing as well as lower accrued interest for various tax related matters as a result of certain settlements in the second quarter of 2008.

Debt Retirement Costs. Debt retirement costs decreased $1.3 million for the year ended December 31, 2008, compared to the year ended December 31, 2007. In May 2008, KCSR redeemed its 91/2% Senior Notes due October 1, 2008 and expensed $5.6 million for cash tender offer expenses and unamortized debt issuance costs. In June of 2007, KCSM redeemed its 121/2% Senior Notes due 2012 and entered into a new bank credit agreement. The charge of $16.7 million for the call premium and the write-off of unamortized debt issuance costs associated with the extinguished debt was partially offset by the $9.8 million write off of the unamortized purchase accounting fair value effect related to the 121/2% Senior Notes.

Foreign Exchange. For the years ended December 31, 2008 and 2007, the foreign exchange loss was $21.0 million and $0.9 million, respectively, primarily due to fluctuations in the value of the U.S. dollar versus Mexican peso exchange rates and a cumulative post-acquisition loss of $2.9 million in the fourth quarter, which was an out-of-period adjustment related to certain unsettled transactions recorded prior to 2004.

Other Income, net. Other income, net, decreased $6.0 million for the year ended December 31, 2008 compared to the same period in 2007, primarily due to lower interest and dividend income, and fewer gains on sales of land in 2008 as compared to the same period in 2007.

Income Tax Expense. For the year ended December 31, 2008, the Company s income tax expense was $64.5 million, a decrease of $2.6 million as compared to $67.1 million for the year ended December 31, 2007. The effective tax rate was 25.9% and 30.3% for the years ended December 31, 2008 and 2007, respectively. The reduction in the year-over-year effective rate reflects changes in foreign exchange rates partially offset by a tax asset valuation allowance recorded by KCSM during 2008.

LIQUIDITY AND CAPITAL RESOURCES

Overview

KCS primary uses of cash are to support operations; maintain and improve its railroad; pay debt service and preferred stock dividends; acquire new and maintain existing locomotives, rolling stock and other equipment; and meet other obligations. KCS cash flow from operations has historically been sufficient to fund operations, maintenance capital expenditures and debt service. External sources of cash (principally bank debt, public and private debt, preferred stock and leases) have been used to refinance existing indebtedness and to fund acquisitions, new investments and equipment additions. Due to the downturn in the economy and the timing of debt refinancing activities, the Company utilized $112.4 million of cash and cash equivalents during the year ended December 31, 2009 see Cash Flow Information below. On December 31, 2009, total available liquidity (the unrestricted cash balance plus revolving credit facility availability) was approximately $203 million.

The Company believes, based on current expectations, that cash and other liquid assets, operating cash flows, access to debt and equity capital markets, and other available financing resources will be sufficient to fund anticipated operating, capital and debt service requirements and other commitments in the foreseeable future. The Company intends to repay the outstanding balance of $40.0 million under the KCSR revolving credit facility prior to its scheduled maturity date of April 28, 2011. KCS has no significant scheduled debt maturities until 2012.

As of December 31, 2009, KCS has a debt capitalization ratio (total debt as a percentage of total debt plus total equity) of 45.8 percent. Its primary sources of liquidity are cash flows generated from operations, borrowings under its revolving credit facility and access to debt and equity capital markets. Although KCS has had adequate access to the capital markets, as a non-investment grade company, the financial terms under which funding is obtained often contain restrictive covenants. The covenants constrain financial flexibility by restricting or prohibiting certain actions, including the ability to incur additional debt for any purpose other than refinancing existing debt, create or suffer to exist additional liens, make prepayments of particular debt, pay dividends on common stock, make investments, engage in transactions with stockholders and affiliates, issue capital stock, sell certain assets, and engage in mergers and consolidations or in sale leaseback transactions. These restrictions, however, are subject to a number of qualifications and exceptions that provide the Company with varying levels of additional borrowing capacity. The Company was in compliance with all of its debt covenants as of December 31, 2009.

KCS operating results and financing alternatives can be unexpectedly impacted by various factors, some of which are outside of its control. For example, if KCS was to experience a reduction in revenues or a substantial increase in operating costs or other liabilities, its earnings could be significantly reduced, increasing the risk of non-compliance with debt covenants. Additionally, the Company is subject to economic factors surrounding debt and equity capital markets and its ability to obtain financing under reasonable terms is subject to market conditions. Volatility in capital markets and the tightening of market liquidity could impact KCS access to capital. Further, KCS cost of debt can be impacted by independent rating agencies, which assign debt ratings based on certain factors including credit measurements such as interest coverage and leverage ratios, liquidity and competitive position.

Standard & Poor s Rating Services (S&P) rates the senior secured debt as BB-, the senior unsecured debt as B+, and the preferred stock as CCC. S&P maintains a corporate rating of B and recently improved the Company s outlook to stable. Moody s Investors Service (Moody s) rates the senior secured debt as Ba2, the senior unsecured debt as B2, and the preferred stock as B3. Moody s maintains a corporate rating of B1 for KCS and B2 for KCSM and recently improved the outlook to stable for all issuers.

Long-Term Debt and Credit Facility Activity

KCSR Debt

On January 14, 2009, pursuant to an offer to purchase, KCSR commenced a cash tender offer and consent solicitation for any and all outstanding $200.0 million KCSR 71/2% senior unsecured notes due June 15, 2009 (the 71/2% Senior Notes). KCSR received consents in connection with the tender offer and consent solicitation from holders of over 88% of the 71/2% Senior Notes. On January 29, 2009, KCSR purchased the tendered notes in accordance with the terms of the tender offer with proceeds received in 2008 from the issuance of the $190.0 million 13.0% senior unsecured notes due December 15, 2013 (the 13.0% Senior Notes), and other borrowings.

KCSM Debt

On March 30, 2009, KCSM issued $200.0 million of 121/2% senior unsecured notes due April 1, 2016 (the 121/2% Senior Notes), which bear interest semiannually at a fixed annual rate of 121/2%. The 121/2% Senior Notes were issued at a discount to par value, resulting in an $11.0 million discount and a yield to maturity of 133/4%. The 121/2% Senior Notes are unsecured, unsubordinated obligations and rank pari passu in right of payment with KCSM s existing and future unsecured, unsubordinated obligations. KCSM used a portion of the net proceeds from the offering to repay all amounts outstanding under KCSM s unsecured credit agreement dated June 14, 2007 (the 2007 KCSM Credit Agreement). Upon repayment of the outstanding amounts, KCSM terminated the 2007 KCSM Credit Agreement, effective March 30, 2009. The 121/2% Senior Notes are redeemable at KCSM s option in whole or in part on and after April 1, 2013, at the following redemption prices (expressed as percentages of principal amount) plus any accrued and unpaid interest: 2013 106.250%, 2014 103.125%, 2015 100.000%. In addition, KCSM may redeem up to 35% of the notes any time prior to April 1, 2012 from the proceeds of the sale of capital stock in KCSM or KCS and are redeemable, in whole but not in part, at KCSM s option at their principal amount, in the event of certain changes in the Mexican withholding tax rate. The 121/2% Senior Notes include certain covenants that restrict or prohibit certain actions.

On January 22, 2010, KCSM issued $300.0 million principal amount of 8.0% senior unsecured notes due February 1, 2018 (the KCSM 8.0% Senior Notes), which bear interest semiannually at a fixed annual rate of 8.0%. The notes were issued at a discount to par value, resulting in a $4.3 million discount and a yield to maturity of 81/4%. KCSM used the net proceeds from the issuance of the KCSM 8.0% Senior Notes and cash on hand to purchase $290.0 million in principal amount of the 93/8% senior unsecured notes due May 1, 2012 (the 93/8% Senior Notes) tendered under an offer to purchase and pay all fees and expenses incurred in connection with the KCSM 8.0% Senior Notes offering and tender offer. The KCSM 8.0% Senior Notes are redeemable at KCSM s option, in whole or in part, on and after February 1, 2014, at the following redemption prices (expressed as percentages of principal amount) plus any accrued and unpaid interest: 2014 104.000%, 2015 102.000%, 2016 100.000%. In addition, KCSM may redeem up to 35% of the KCSM 8.0% Senior Notes any time prior to February 1, 2013 from the proceeds of the sale of capital stock in KCSM or KCS and are redeemable, in whole but not in part, at KCSM s option at their principal amount, in the event of certain changes in the Mexican withholding tax rate. The KCSM 8.0% Senior Notes include certain covenants that restrict or prohibit certain actions.

On January 22, 2010, the Company purchased $290.0 million of the tendered 93/8% Senior Notes in accordance with the terms and conditions of the tender offer set forth in the offer to purchase using the proceeds received from the issuance of $300.0 million of the KCSM 8.0% Senior Notes. Additionally, on February 1, 2010, the Company repurchased $6.3 million of the 93/8% Senior Notes. KCSM recorded debt retirement costs of $14.9 million in the first quarter of 2010. The remaining 93/8% Senior Notes mature on May 1, 2012 and are redeemable by KCSM at its option.

Common Stock Issuance

On April 27, 2009, the Company entered into an ATM Equity Offering[sm] Sales Agreement with Bank of America Merrill Lynch, Pierce, Fenner & Smith, Incorporated (the ATM Equity Offering), under which the Company received proceeds of $51.4 million (net of commission of $0.9 million and fees and other expenses of $0.2 million) from the issuance of 3,204,900 common shares, at a weighted average sales price of $16.38. On July 31, 2009, the Company entered into a Common Stock Purchase Agreement with certain institutional investors in which the Company issued 1,125,308 shares of the Company s common stock at a purchase price of $20.00 per share on August 3, 2009 for aggregate proceeds of $22.5 million. This completed the Company s offering of shares under the ATM Equity Offering and Common Stock Purchase Agreement.

Cash Flow Information and Contractual Obligations

Summary cash flow data follows *(in millions):*

	2009	2008	2007
Cash flows provided by (used for):			
Operating activities	$ 292.9	$ 413.0	$ 367.8
Investing activities	(346.4)	(538.0)	(366.8)
Financing activities	(58.9)	299.4	(24.5)
Net increase (decrease) in cash and cash equivalents	(112.4)	174.4	(23.5)

Cash and cash equivalents beginning of year	229.9	55.5	79.0
Cash and cash equivalents end of year	$ 117.5	$ 229.9	$ 55.5

During 2009, cash and cash equivalents decreased $112.4 million. Capital expenditures were partially offset by cash flows from operating activities, which decreased as a result of lower net income from reduced carload/unit volumes due to the downturn in the economy. In addition, the Company repaid $319.1 million of debt and received net proceeds of $262.9 million from the issuance of common stock and the 121/2% Senior Notes. During 2008, cash and cash equivalents increased $174.4 million due to improved operating performance, net proceeds from the issuance of the 8.0% Senior Notes and the 13.0% Senior Notes, and loan proceeds received from financing locomotives, which were partially offset by a higher level of capital expenditures and redemption of the 91/2% Senior Notes.

Operating Cash Flows. Net operating cash flows for 2009 decreased $120.1 million to $292.9 million. The decrease in operating cash flows was primarily a result of lower net income from reduced carload/unit volumes due to the downturn in the economy. Net operating cash flows for 2008 increased $45.2 million to $413.0 million. The increase in operating cash flows was primarily attributable to increased net income.

Investing Cash Flows. Net investing cash outflows were $346.4 million and $538.0 million during 2009 and 2008, respectively. This $191.6 million decrease was due to a reduced capital program in response to decreased operating cash flows. Net investing cash outflows for 2008 increased $171.2 million as compared to 2007, which was related to a higher level of capital expenditures.

Financing Cash Flows. Financing cash inflows were generated from the issuance of long-term debt, proceeds from the ATM Equity Offering and Common Stock Purchase Program and proceeds from the issuance of common stock under employee stock plans. Financing cash outflows were used for the repayment of debt, the payment of dividends on KCS preferred stock and the payment of debt costs. Financing cash flows for 2009, 2008, and 2007 are discussed in more detail below:

Financing cash outflows for 2009 were $58.9 million. During 2009, the Company repaid $319.1 million of debt, including the purchase of the 71/2% Senior Notes and repayment of borrowings under the 2007 KCSM Credit Agreement. During the same period, the Company received net proceeds of $189.0 million from the issuance of the 121/2% Senior Notes. The net cash outflows from these refinancing activities were substantially offset by $73.9 million in proceeds from the issuance of common stock under the ATM Equity Offering and Common Stock Purchase Agreement.

Financing cash inflows for 2008 were $299.4 million, resulting primarily from the issuance of debt and the financing of locomotive purchases, partially offset by the redemption of debt. During 2008, KCSR issued $275.0 million of 8.0% Senior Notes and used a portion of the proceeds from the issuance to redeem $200.0 million principal amount of the 91/2% Senior Notes and the applicable premium and expenses associated with the redemption. Also during 2008, KCSR issued $190.0 million principal amount of 13.0% Senior Notes at a discount and used the net proceeds and other borrowings to purchase a portion of the 71/2% Senior Notes on January 29, 2009. KCSM received $125.0 million during 2008 from financing locomotives purchased in late 2007 and the first half of 2008.

Financing cash outflows for 2007 were $24.5 million, resulting primarily from the costs associated with refinancing debt and preferred stock dividend payments. During 2007, KCSM issued $165.0 million of 73/8% senior unsecured notes and used the proceeds, together with a new $30.0 million term loan, to redeem the KCSM 121/2% Senior Notes due 2012 and pay the associated premium and expenses. KCSR entered into an amendment to its 2006 Credit Agreement for a $75.0 million term loan facility and used the proceeds to reduce amounts outstanding under KCSR s revolving credit facility under the 2006 Credit Agreement. KCSM entered into a credit agreement for a $30.0 million term loan facility and a revolving credit facility of up to $81.0 million. KCSM used the proceeds to repay all amounts outstanding under the 2005 KCSM Credit Agreement, to refinance a portion of the 121/2% Senior Notes due 2012, to pay costs associated with these refinancings and to pay the remaining amounts outstanding in respect of the KCSM s 101/4% Senior Notes.

Proceeds from the sale of KCS common stock pursuant to employee stock plans were $3.0 million, $8.6 million, and $0.7 million in 2009, 2008, and 2007, respectively.

Payment of preferred stock cash dividends were $11.0 million, $15.2 million and $23.3 million in 2009, 2008, and 2007, respectively. Dividends of approximately $0.2 million were paid each year on the 4.0% noncumulative preferred stock; approximately $4.2 million and $15.0 million of dividends were paid in 2008, and 2007, respectively, on the Series C Preferred Stock which was redeemed during 2008; and approximately $10.8 million, $10.8 million, and $8.1 million of dividends were paid in 2009, 2008, and 2007, respectively, on the Series D Preferred Stock. All cumulative dividends in arrears were paid February 15, 2007.

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Contractual Obligations. The following table outlines the material obligations under long-term debt, operating leases, and other contractual commitments on December 31, 2009 *(in millions)*. Typically, payments for operating leases, other contractual obligations and interest on long-term debt are funded through operating cash flows. Principal payment obligations on long-term debt are typically refinanced by issuing new long-term debt or equity. If operating cash flows are not sufficient, funds received from other sources, including borrowings under revolving credit facilities and proceeds from property and other asset dispositions might also be available. These obligations are customary transactions similar to those entered into by others in the transportation industry.

		Payments Due by Period			
	Total	**Less than 1 Year**	**1-3 Years**	**3-5 Years**	**More than 5 Years**
Long-term debt (including interest and capital lease obligations)	$ 2,701.6	$ 230.0	$ 770.6	$ 1,032.0	$ 669.0
Operating leases	1,104.2	146.6	252.5	199.3	505.8
Obligations due to uncertainty in income taxes	2.1		0.4	1.7	
Capital expenditures obligations(i)	379.0	121.0	258.0		