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WRIGLEY'S DUAL-CLASS EQUITY STRATEGY

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ABSTRACT

This case affords students the opportunity to discuss stockholders' equity issues in a unique and interesting format. The instruction of stock dividends is important; however, it typically is not very interesting. In the case of Wrigley, the stock dividend has a twist which allows discussion of corporate governance issues (including an international component), and stock price reaction topics, not only making the topic more interesting but also permitting the topic to be addressed in a way that goes beyond the mechanics.

This teaching case primarily involves the issue of corporate control via the use of a dual-class stock structure and the related issues of corporate governance. The use of super-voting shares held by management or founders allows them to control the company while putting up less than a majority of the equity.

BACKGROUND

Most people are familiar with the name Wrigley: Wrigley Field – home of the Chicago Cubs, Wrigley's Juicy Fruit, Doublemint, and Spearmint Gum, Wrigley Botanical Gardens, and the famous Wrigley building in downtown Chicago modeled after a Cathedral in Seville, Spain. These are all the legacy of an eleven year old runaway by the name of William Wrigley Jr. who left home in 1872. Mr. Wrigley ultimately landed in Chicago, selling cans of baking powder. To increase sales, he gave away chewing gum with each can of baking powder. When the gum became more popular than the baking powder, he dropped baking powder, started to sell gum and in 1891, he founded the Wm. Wrigley Jr. Co. In 1893, Mr. Wrigley introduced Juicy Fruit. At one point, Mr. Wrigley collected every phone book in the United States and mailed each person four sticks of gum. By 1920, his company was making over nine billion sticks of gum a year. The company went public in 1923, listing its shares on the New York Stock Exchange (NYSE) using the symbol WWY.

For over four generations, the Wrigleys have directed the company. William Wrigley Jr. stepped down in 1925 and turned the company over to his son Phillip Wrigley. Continuing the Wrigley dynasty, Phillip led the company until 1961 and then Phillip's son, William Wrigley Jr., (this is the second William Wrigley Jr.) became the CEO. In 1999, upon the untimely death of his father, another William Wrigley Jr. (this is the third William Wrigley Jr.) took the helm of the company.

When the current William Wrigley Jr. became the chief executive, sales were languishing and the company culture was conservative. At age 35, the young "Bill" Wrigley began to stir up the company by taking over competitors, acquiring debt, hiring top executives from outside the company and introducing new flavors. This was a dramatic break from the past; when Bill had suggested that the company should expand into mints, his father had responded: "We know gum." -- end of discussion. Additionally, Bill relaxed the dress code and did not follow his father's tradition of being called "Mr. Wrigley," which in the 1990's was quite an archaic business practice. He also started an aggressive acquisition program. In its first 82 years, WWY had only four brands of chewing gum. However, since Bill took over, its portfolio of products has grown at a tremendous rate, both through innovation and acquisitions. In 2004, only five years after taking control of the company, young Wrigley purchased Altoids mints and Life Savers candies for $1.48 billion. In 2005 alone, the company launched 72 new products. WWY became one of the fastest growing publicly traded food companies and was selected by Fortune magazine in 2005 as one of the "100 Best Companies to Work For." It was also listed in the "Top Ten" for its low employee turnover and excellent employee vacation policies.

DUAL-CLASS STRUCTURES

From the mid 1920s to the mid 1980s, the NYSE refused to list a company's stock unless each share of any class had exactly one vote, subsequently referred to as the "one-share, one-vote principle". The other exchanges sought a competitive advantage by accepting listings of common shares with different voting rights, although within limits. In 1986, the directors of the NYSE declared a moratorium on the enforcement of its one-share, one-vote rule and appointed a committee to review "qualitative listing standards". This resulted in many companies adopting dual-class structures with disparate voting rights.

In response to the NYSE moratorium, the Security and Exchange Commission (SEC) held unusual public hearings to determine whether it should require the NYSE to enforce the one-share, one-vote rule or whether to adopt a one-share, one-vote rule for all exchanges. By 1988, these debates ultimately resulted in SEC Rule 19c-4, which required a one-share, one-vote rule to protect the voting power of existing shareholders. However, the United States Court of Appeals for the District of Columbia subsequently invalidated rule 19c-4, claiming it exceeded the SEC's authority (Bainbridge, 1991). In 1994, the NYSE, the American Stock Exchange, and the NASDAQ eventually agreed to a common one-share, one-vote rule that largely paralleled 19c-4. Companies with existing dual-class structures were grandfathered.

AN INTRIGUING SPECIAL STOCK DIVIDEND

In April 1986, WWY, which had been listed on the NYSE since 1923, took advantage of the previously discussed NYSE moratorium and created a dual-class common stock structure by creating a new class of common shares – Class B, which were distributed as part of a 3 for 1 stock split. For each share of common stock, another share of common stock and a share of the Class B common stock were received. This Class B common stock has two distinct features: first, each Class B common share has 10 votes compared to one vote for each share of common stock, and secondly, the Class B common shares have restricted transferability and are not listed on any stock exchange. Nonetheless, they may be converted at any time on a share per share basis into common stock, which is traded on the NYSE and as such is freely tradable and transferable. Since the Class B shares are not listed on any exchange, they must be converted into common stock prior to any sale.

On April 17, 2006, the WWY board of directors declared a stock dividend of Class B common stock to be distributed to all common shareholders, and Class B shareholders. Distribution was on May 1, 2006. A 1 for 4 stock dividend was paid to common shareholders; that is, a common shareholder received a Class B share for every four shares of common stock held. Additionally, a 1 for 4 stock dividend was paid to Class B common shareholders; that is, for every four shares of Class B common stock held, a Class B common shareholder received one share of Class B common stock.

Owners' Equity Information

The Balance Sheet of WWY's December 31, 2005 annual report is recreated below (all dollar amounts in thousands, shares in actual amounts). As of December 31, 2005, WWY had 199,230,000 common shares issued and 9,631,000 common shares held in treasury. WWY had 35,619,000 Class B common shares issued and 2,408,000 Class B common shares held in treasury, for a total of 33,211,000 Class B common shares outstanding. No significant common stock or Class B common stock transactions occurred prior to April 17, 2006 or before the May 1, 2006 stock distribution.

POSTSCRIPT

In October 2006, for the first time in its history, WWY named a non-family member as chief executive – William D. Perez. William Wrigley Jr. assumed the new post of executive chairman, a position which reports to the board of directors.

In April 2008, WWY agreed to be acquired by Mars Inc. for approximately $23 billion in a deal that was to be partially financed by Berkshire Hathaway. In January 2010, Bill left Wrigley's, 15 months after the company was sold to Mars, Inc., to pursue other business and philanthropic interests.[1]

QUESTIONS/REQUIREMENTS

1. a. For the April 17, 2006 stock dividend, determine how many new Class B shares were issued and journalize the dividend declaration and issuance. Please show your computations. Assume that this is a "large stock dividend" and the Class B shares have a stated value of 6.69 cents per share.

   b. Assume that no significant transactions had occurred until the issuance and distribution of the stock dividend, i.e, assume the valuations on the December 31, 2005 Balance Sheet for the pre-stock dividend valuations. Reconstruct the

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[1] Chicagopressrelease.com. January, 22 2010. "William Wrigley Jr. leaves gum giant." http://chicagopressrelease.com/news/william-wrigley-jr-leaves-gum-giant

shareholders' equity section of the Balance Sheet immediately following the distribution of the stock dividend on May 1, 2006. What impact did the stock dividend have on shareholders' equity and its components of retained earnings and contributed capital? What impact did the stock dividend have on the capital structure of WWY? What impact did the stock dividend have on the total assets of WWY?

2. Where dual-class structures exist, they are predominately found in family or founder dominated businesses, including Comcast (Roberts family), Media General (Bryan family), News Corporation (Murdoch family), The Washington Post Co. (Graham family), Dow Jones & Co. (Bancroft family), Ben and Jerry's Ice Cream (Ben Cohen and Jerry Greenfield) and as well as Google (Larry Page and Sergey Brin). Why is a dual class structure more prominent in family or founder dominated businesses?

3. Dual-class structures are an anathema on U.S. exchanges, yet Canada has a long tradition of dual-class shares. Europe has recently adopted the "break-through" rule, which prohibits deviations from one share - one vote structures. What are the arguments for and against a dual-class structure? (Hint - Try an internet search using these terms: "dual-class equity," "break-through rule," "Golden Share," "VW Law.")

	2005	**2004**
ASSETS		
Current assets:		
Cash and cash equivalents	$257,704	$628,553
Short-term investments, at amortized cost	1,100	22,764
Accounts receivable (less allowance for doubtful accounts: 2005 - $8,013; 2004 - 11,682)	412,931	356,389
Inventories:		
Finished goods	213,915	135,527
Raw materials, work in process and supplies	287,810	262,580
Total Inventories:	501,725	398,107
Other current assets	93,903	65,336
Deferred income taxes - current	38,731	34,761
Total current assets	1,306,094	1,505,910
Marketable equity securities, at fair value	--	16,970
Deferred charges and other assets	285,392	250,158
Deferred income taxes - noncurrent	80,979	40,239
Goodwill	1,094,219	168,495
Other intangibles	411,105	42,311
Property, plant and equipment, at cost:		
Land	55,882	53,209
Buildings and building equipment	647,479	555,375
Machinery and equipment	1,629,231	1,464,903
Total Property, plant and equipment, at cost	2,332,592	2,073,487
Less accumulated depreciation	1,050,180	930,867
Net property, plant and equipment	1,282,412	1,142,620
TOTAL ASSETS	$4,460,201	$3,166,703

	2005	2004
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Line of credit		$90,000
Current portion of long-term debt and commercial paper	$100,000	
Accounts payable	312,954	216,764
Accrued expenses	412,164	270,898
Interest payable	20,510	338
Dividends payable	62,459	52,821
Income and other taxes payable	62,596	76,554
Deferred income taxes - current	10,128	10,595
Total current liabilities	980,811	717,970
Deferred income taxes - noncurrent	110,687	88,112
Other noncurrent liabilities	154,281	181,937
Long-term debt	1,000,000	
Total liabilities	2,245,779	988,019
Stockholders' equity:		
Preferred Stock - no par value (Authorized - 20,000,000 shares; Issued - None)		
Common Stock - no par value (Authorized: 2005 - 1,000,000,000 shares, 2004 - 400,000,000 shares; Issued: 2005 - 199,230,000 shares, 2004 - 198,930,000 shares)	13,274	13,254
Class B Common Stock - convertible (Authorized: 2005 - 300,000,000 shares, 2004 - 80,000,000 shares; Outstanding: 2005 - 33,211,000 shares, 2004 - 33,511,000 shares)	2,222	2,242
Additional paid-in capital	37,760	17,764
Retained earnings	2,702,947	2,435,838
Common Stock in treasury, at cost (2005 - 9,631,000 shares; 2004 - 7,670,000 shares)	(513,763)	(346,087)
Accumulated other comprehensive income (loss):		
Foreign currency translation adjustment	(27,633)	44,936
Gain (loss) on derivative contracts	(385)	758
Unrealized holding gains on marketable equity securities		9,979
	(28,018)	55,673
Total stockholders' equity	2,214,422	2,178,684
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$4,460,201	$3,166,703

4. One significant reason for organizing a business as a corporation as opposed to a proprietorship or partnership involves the continuous life and transferability of ownership, i.e., corporate ownership traded on a security exchange is easily transferable and liquid. Hence, this is a major reason for investing in a corporation. The majority shareholder groups of WWY include institutions, including mutual and index funds, pension funds, endowments, etc., who are interested in liquid investments. However, the Class B shares are not traded and must be converted into common shares in order to be sold. Why then do you think WWY would issue this special dividend consisting of Class B shares instead of common shares? In other words, what do you think might be the objective behind the special dividend? Do you consider Bill's goals and objectives to be aligned with the majority of shareholders?

   Use the facts below in answering this question.

   a. In 1999, when Bill took over the company upon his father's death, he held approximately 20,000,000 shares of common stock (approximately 93,000,000 common shares outstanding) and approximately 12,000,000 shares of Class B stock (approximately 22,000,000 class B shares outstanding).
   b. In 2006, just prior to this special stock dividend, Bill held approximately 10,000,000 shares of common stock (approximately 189,000,000 common shares outstanding) and approximately 17,000,000 shares of Class B stock (approximately 33,000,000 Class B shares outstanding).
   c. In 2006, after this special stock dividend, Bill held approximately 10,000,000 shares of common stock (approximately 189,000,000 common shares outstanding) and approximately 24,000,000 shares of Class B stock (approximately 89,000,000 Class B shares outstanding).
   d. After the special stock dividend, one of the major shareholders of WWY, the Wrigley Family Trust, had approximately 12% of the total voting power for WWY shares (including both common and Class B shares). On May 1, 2006, Bill was co-trustee of this trust.

5. How do you think investors on Wall Street may view the special dividend? [You may want to answer this question for each of the various types of investors, such as a typical short-term and long-term investor, individual and institutional investor (i.e., mutual fund and pension fund), and from the more unique perspective of a hedge fund, investment banker and private equity fund investor.] Why?

REFERENCES

Bainbridge, S. M. 1991. "The Short Life and Resurrection of SEC Rule 19c-4. Washington University Law Quarterly (Vol. 69) 565-634.

TEACHING NOTES

Teaching notes are available from the editor. Send a request from the "For Contributors" page of the journal website, http://gpae.bryant.edu.