Corporate governance and shareholder engagement

Everything we do is designed to deliver outstanding performance and service to our clients. Central to that is a considered approach to stewardship. So we are pleased to support the seven principles set out by the Financial Reporting Council (FRC) in The UK Stewardship Code. How we do this is explained below.

Principle 1

Institutional investors should disclose publicly their policy on how they will discharge their stewardship responsibilities.

Artemis is an active investment manager. As well as fundamental research, regular meetings with companies guide our decisions* – before and after we invest.

By meetings, we mean regular and constructive exchanges of views with a company's executives, non-executive directors and its investor relations team. Before that happens, our investment teams discuss informally what they want to achieve from any 'engagement' and set out formal objectives. Topics include strategy, operational performance, financing and risk – as well as corporate governance. Where our fund managers and analysts have specific concerns or need more time with management, we will ask for extra meetings.

Our aim is to grow the value of our clients' investments over the long term. To that end, we take seriously our duty to support and improve the corporate governance of the companies whose shares we own and to keep abreast of best practice. When companies fall short of guidelines such as the UK Corporate Governance Code we consider their explanations carefully. In some cases, we look for evidence they have acknowledged the problem and are moving towards best practice. In others, the size, complexity or nature of their business will explain why they take a different approach – say to the structure of the board and its committees.

To provide independent research on corporate governance we have chosen the specialist Institutional Shareholder Services (ISS). But this is to support what we do: it does not do our thinking for us. Artemis' approach to stewardship – that is, how we engage with companies and how we vote – is our own.

We report on these matters regularly to our clients and a quarterly summary of how we have voted is available on our website. Meanwhile the firm's stewardship statement and voting policy is subject to annual review and approval by our investment committee. We also review annually the services we get from ISS.

Further information can be found on the stewardship and voting page of our website.

Principle 2

Institutional investors should have a robust policy on managing conflicts of interest in relation to stewardship which should be publicly disclosed.

Artemis is a privately owned, independent partnership and fund management is all we do. So we don't encounter some of the conflicts of interest faced by larger investment or financial services companies. But it does happen, even in less complex businesses – and we recognise that. For example, the pension scheme of a company in which we are investing might be a client of Artemis; or we may have investments in one of our main distributors, or in Affiliated Managers Group Inc (AMG) which owns a stake in our business; or one of our partners, non-executive directors or employees may be a director of one of our holdings.

How we vote may benefit, or be perceived to benefit, Artemis or a particular investor. So we have put in place a firm-wide policy setting out how we will deal with actual or potential conflicts of interest. Its central tenet is: clients always come first. Where there is a possibility of a conflict of interest any decision to vote against the voting policy is discussed with Artemis' chief investment officer, and the final decision with explanation is recorded.

We record and cross-reference all potential conflicts in a 'matrix'. This allows us to monitor and prevent any disadvantage to our clients. Both the policy on conflicts of interest and the accompanying matrix are reviewed and approved every year by our management committee.

Further information about potential conflicts of interest is available on request.

Principle 3

Institutional investors should monitor their investee companies.

Our aim is to outperform the market and produce superior long-term returns for our clients. To do this, we use fundamental analysis. Alongside the share price, we make our own calculation of a company's value by looking at the factors affecting its business now and in the future. This involves gaining detailed knowledge, through:

- meetings and calls* with senior company managers, their advisers and analysts;
- analysis of published company reports, announcements and circulars;
- broader internal and external research and data;
- proprietary screening tools.

Artemis rarely attends general meetings. We prefer to talk privately with management as we believe this is a much more effective way to monitor strategy, performance, risk, capital allocation, governance and remuneration. Where relevant, discussions will also include environmental and social issues. We review progress and, if we have concerns, challenge management on their decisions. Then, after each meeting,

* The exception is our quantitative based investment strategies which use SmartGARP®, Artemis' in-house proprietary, quantitative model. This analyses many factors, both company-specific and macroeconomic, to construct a portfolio of stocks. Meeting managements does not form part of this process.

our fund managers and analysts discuss what further action is needed.

Fund managers and analysts have specific areas of expertise across a range of subjects: country, industry, company, corporate governance, finance, economics, business and so on. Their experience helps each investment team to decide what is appropriate in terms of monitoring and engagement. The approach will reflect our view of the current and future prospects of the company, whether there are specific issues to address and the stock's current and likely future position in a portfolio.

No team at Artemis works in isolation. Often, members from different strategies attend meetings together – depending on interest, knowledge of the company and expertise in the issues to be discussed. Fund managers and analysts record the details of any 'engagement' in a database which allows information to be shared. Alongside external research, this is our main resource for monitoring actual and potential investments.

As investors, we may not wish to be made 'insiders' – that would stop us being able to buy or sell the relevant shares. So we ask investee companies to make sure they get our agreement before giving us privileged information.

Principle 4

Institutional investors should establish clear guidelines on when and how they will escalate their stewardship activities.

Artemis is an active but not an 'activist' investor; we don't buy holdings in companies with a view to changing the way they are run. Nor do we want to or feel obliged to micro-manage their affairs. But we will intervene where we feel it necessary. It may be that we have concerns about strategy, operational performance, acquisitions and disposals, internal controls (or lack of them) or remuneration.

What we do about these concerns depends on what is best for our clients. For example, we may:

- talk to the board and management;
- write to the companies in which we invest to explain our expectations as owners;
- collaborate with other shareholders to bring pressure to bear on a board;
- abstain or vote against management's resolutions;
- submit resolutions at shareholders' meetings.

The approach will depend on what is most effective for a particular issue. Generally, operational and financial matters, and execution of strategy, are likely to involve meeting the executive team. Concerns about board oversight, governance and risk tend to be discussed with non-executives. And in certain circumstances it may be appropriate to speak to the chairman or senior independent director.

In any engagement it is important that there is a proper dialogue. Where we feel a message needs reinforcing, in serious situations or when time is tight we use a combination of the activities listed above. Our success (or otherwise) is measured in the long-term in terms of a company's achievement of its overall objectives including shareholder value. This does not stop us selling a holding if that is the most effective response.

Principle 5

Institutional investors should be willing to act collectively with other investors where appropriate.

Our approach emphasises meeting and talking to company directors. But this does not stop us collaborating with other large shareholders if collective action could be more effective and our objectives (including the need for confidentiality) are the same. It may also involve us contacting individual shareholders directly or through industry groups such as the Investment Association and Investor Forum. We consider each case carefully, on its own merits. Issues on which we have acted collectively include corporate strategy and its implementation, capital allocation and directors' pay.

Institutional investors interested in collective engagement should contact:
stewardship@artemisfunds.com

Principle 6

Institutional investors should have a clear policy on voting and disclosure of voting activity.

It is our responsibility to exercise our clients' voting rights in a considered manner, within the context of a positive relationship with a company's management. Artemis aims to vote its shares in all stocks in the UK and overseas unless we are restricted from doing so by local market practice or clients have made other arrangements.

Our voting is informed and carried out by an independent specialist, ISS. Together, we have developed guidelines which take into account local, national and international standards. This ensures our expectations for corporate governance are appropriate to each business we invest in.

ISS draws on best practice from around the world for its analysis. Artemis' fund managers have access to this in the form of governance reports. ISS also provides them with a summary of all resolutions put forward at company meetings and assesses the extent to which governance arrangements are in line with best practice.

This research is very valuable. But we would emphasise that our fund managers make the final decision on how to vote.

Sometimes our instructions to ISS may differ from our agreed policy. This could be for the reasons explained in Principle 1 (above) or it may be that we have talked to the company and received a satisfactory explanation. We may also need to review resolutions on a case-by-case basis. Part of the process is keeping a clear record of votes cast and our reasons for voting against, abstaining from or voting with management on contentious issues. Where our instructions differ from our policy, and it's a UK company in which we have a significant holding, we will tell them why.

We prefer to support management's resolutions: where we may not is set out publicly in an appendix to this document. Companies with queries should contact:
stewardship@artemisfunds.com

At the moment, we do not lend stock. If a client's custodian does so, Artemis will not recall it for voting without prior arrangement. Where share-blocking is an issue – that is, voting would bar us from buying or selling a company's stock around the time of the AGM – we prefer the option to trade.

Principle 7

Institutional investors should report periodically on their stewardship and voting activities.

A summary of our votes and details of those instances in which we have voted against management are included in the standard quarterly investment reports we send to our institutional clients. We also provide a quarterly summary on the stewardship and voting page of our website.

We have not sought an independent opinion on our shareholder engagement or voting. However, Artemis' operational voting processes and procedures are subject to review/oversight by internal audit/compliance on a regular basis. Artemis' investment committee reviews and approves the statement on stewardship and the voting policy annually. These topics are also discussed at the committee's quarterly portfolio meetings. The firm carries out due diligence when outsourcing the processing of votes to third parties such as ISS: any external service must meet the required standard and demonstrate effective operating controls. We review the services provided by ISS annually.

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Further information

For further information please contact

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Appendix: How we vote

Set out below are the principles which direct our votes and define the instances in which our clients' interests may override support for management's proposals. Unless otherwise stated, these apply across all regions.

Composition of the board

Independence

Every company should be headed by a board which is effective and responsible collectively for the company's long-term success. Our view is that at least half of the board should be independent, while smaller companies should have a minimum of two independent non-executive directors.

Where the independence of directors does not conform to the UK Corporate Governance Code ("the Code") or observe local best practice, we look carefully at the reasons why. When defining 'independence', reference is often made to the length of time a director serves on a board (tenure); whether he or she holds share options in the company; and relationships, both business and personal, which may influence their decisions.

In our view, failing to satisfy formulaic criteria does not necessarily stop non-executive directors discharging their duties and responsibilities effectively. For instance, we do not feel the holding of options by non-executive directors of AIM companies (also common in the US) automatically undermines their independence. Nor, more generally, does tenure of more than nine years. We believe it is important to consider directors' contribution, their judgement and their character.

In some countries, particularly in Europe, it is a legal requirement or best practice for employees to be represented on the board. In this case we assess the independence of the elected directors only. In Japan, we expect at least two outside directors on a traditional two-tier board; and where there is a committee structure, the majority should be independent.

Otherwise, in the absence of a satisfactory explanation, we are likely to vote against individual directors if the board does not conform to the Code or to local best practice.

Chairman

In most instances we will vote against combining the roles of CEO and chairman. We believe the roles of chairman and chief executive should be separate. The chairman leads the board and makes sure it functions effectively. There ought to be a clear division between this and running the business. While it may be necessary for a short time for the same director to perform both roles, we would want to see a clear rationale for this decision, what additional steps have been taken to provide additional independent oversight and to know how and when the anomaly will be resolved.

The combined role is more common in the US and we will view this arrangement in the light of board composition more generally. Where there have been material failures of governance, stewardship, risk oversight or instances of problematic pay practices or reductions in shareholder rights for example, we will vote against combining the roles of CEO and chairman.

We will support shareholders' proposals to separate the two roles and appoint a lead independent director.

In the UK we will vote against the election of a former CEO as chairman unless the company has given a strong justification or the situation is temporary.

Election of directors

We believe it is in shareholders' interests for directors to be submitted to regular re-election (as long as they are performing well). Our preference is for annual election by a majority vote and we believe that boards should not be classified (a structure under which directors serve terms of different length). In normal circumstances we will support shareholders' proposals to declassify a board or introduce majority voting.

Where we are concerned about an individual's performance, how the business is doing or the long-term strategy, we will consider voting against the re-election of directors. We may also vote against if we believe someone holds too many directorships and cannot carry out their responsibilities effectively; or if their attendance at meetings of the board or a committee has been poor for at least two years.

Committees

The nomination committee should lead the process for appointing directors and make recommendations to the board. A majority of the members should be independent. Audit and remuneration committees should consist of three (or two for smaller companies) independent non-executive directors.

We will consider voting against the re-election of the committee chairman or members of the committee in these situations: where the committee does not conform to best practice; if we believe it has failed in its duties; or when there has been no engagement with shareholders on key issues.

In the UK, if we have not supported the remuneration report for two consecutive years we will vote against the re-election of the remuneration committee chairman.

As part of a board's approach to succession planning we expect the report and accounts to contain information on progress towards meeting best practice guidelines on gender diversity at board and senior management levels. For UK, European and North American large cap companies we will consider voting against the chairman of the nomination committee if there are no women on the board, abstain where there is one woman on the board and/or there is little evidence this issue is being addressed. In future years, we are likely to broaden the scope of companies considered to mid and small cap and the criteria required in order to gain our support.

Report & accounts and audit

We are likely to vote against resolutions relating to the report & accounts where the company has restated results within the last year for reasons other than new accounting standards or where the auditors have given a qualified opinion (that is, not agreed with the disclosure and accounting procedures applied). We will consider the following issues on a case-by case basis: where the auditors have highlighted fundamental uncertainties within the accounts, or other concerns; if the company proposes to change auditors after a qualified opinion; or the inclusion of an 'emphasis of matter' (a matter of significant uncertainty) in the audit report.

Appendix: How we vote

If non-audit fees are more than audit fees for two consecutive years without a good explanation being offered, we will vote against the resolution authorising the board to fix the auditors' remuneration.

Remuneration

We believe management should be appropriately rewarded for good long-term performance, however, levels and in particular increases in pay should be justified with a clear rationale. We look for a simple structure to remuneration. This will typically consist of a salary, pension/ benefits (if applicable), an annual bonus partially deferred into shares and a long-term incentive with performance measured over at least three years. We encourage additional holding periods for shares following vesting. Performance targets should be challenging and support the strategy of the company. Measures of long-term performance should focus on sustained growth – for instance in earnings, cash generation, dividends, return on capital and a measure linked directly to returns to investors. For short-term incentive plans, a combination of strategic and financial measures is normally appropriate. We expect bonus targets to be disclosed preferably within one year following payment. Executive directors should own enough shares to link their interests to those of shareholders. We pay particular attention to the dilution effect of share plans.

Whilst our preferred remuneration structure is set out above it may be appropriate for a company to use restricted (time-based) shares without a performance link, as part or all of its long-term incentive arrangements for executives. In order to consider these types of schemes there would need to be a considerable discount (at least 50%) in awards, longer vesting periods versus a traditional performance-based share plan and clear reasons why this structure is the most suitable. However, we expect at least one element of executive pay to be linked to performance.

We will not support the remuneration policy or report if cash payments or vesting of awards under performance-based plans are not conditional on meeting/exceeding set performance targets, if 'long-term' incentive schemes run for less than three years or if dilution levels are excessive. We will vote against the remuneration report if performance conditions have changed retrospectively or where discretion has not been used appropriately.

In the UK we are unlikely to support remuneration policies that do not make it explicit that any new appointees will have their pension contributions set in line with the pension contributions provided to the majority of the workforce.

In Japan, executive pay is low by international standards and performance-based pay still uncommon. So we are likely to support the payment of bonuses except to outside directors.

Subject to local laws we are likely to vote against the remuneration policy where a director is on more than 12 months' notice or where severance payments on early termination of the contract are greater than 12 months' salary (pension and benefits). If a bonus is to be paid, this should be calculated pro rata. We are likely to vote against the remuneration report where the award paid to someone on their recruitment is greater than the amount they have forfeited by leaving their previous employment. Awards should be in shares and performance-related. We will consider proposals to pay a success or transaction bonus on a case-by-case basis. Payments to directors following a merger or take-over can be problematic. Any early vesting of awards should be pro-rated for time lapsed and based on underlying performance. We will not support golden parachutes or other similar exit payments which are not justified.

We will support shareholder proposals aiming to improve best practice in remuneration.

Shareholders' rights

We will vote against anti-takeover provisions and reductions to voting rights which we do not believe are in the interests of shareholders. We will normally support shareholder resolutions which seek to improve shareholders' rights and are in the best interests of shareholders generally – for instance, 'one-share one-vote'.

Corporate actions

A 'corporate action' is any event which materially changes a company and affects its stakeholders, such as a merger, rights issue or restructuring. We consider every corporate action on its own merits. Routine requests for capital should follow guidelines and take account of pre-emption rights. We will look at proposals to amend articles of association/ incorporation and any bundled resolutions, case by case. We do not support resolutions which allow any other business.

Other shareholder resolutions

Supporting shareholder resolutions in areas such as the environment and energy, consumer and product safety, labour standards, political lobbying is based on whether additional disclosure is likely to enhance or protect shareholder value in both the short and long term.

Last reviewed: February 2019.