Participation bond

History of participation mortgage bonds

The Part Bond industry was born when attorneys realised that the needs of conservative investors were not being met by either the stock market, which are regarded as high risk investments, or by bank deposits which offered relatively low interest rates. Attorneys created a new investment product when they used money collected from all their clients and lent the accumulated amount to property buyers or developers against the security of a mortgage bond over the property. The industry was formalized with the introduction of the Participation Bonds Act 55 of 1981. Part Bonds are currently governed by the Collective Investment Schemes Control Act.

What is a participation mortgage bond?

The purchase or development of prime commercial and industrial properties is financed by means of a Participation Mortgage Bond. The loan is secured by a first mortgage bond over the property, registered in favour of Fedbond Nominees (Pty) Ltd. FedGroup Participation Bond Managers (Pty) Ltd (FG), acting as the manager, invites investors to invest in the fund's portfolio of mortgage bonds. Each investor has a participatory interest in the portfolio of mortgage bonds – hence the term "Participation Mortgage Bond". A Participation Mortgage Bond is regularly referred to as a Part Bond. A Part Bond offers investors a low risk interest bearing investment which is secured by a portfolio of commercial and industrial properties. Part-Bonds typically offer a 2% higher interest rate than other similar bank investment products.

How secure are participation bonds?

The investment is secured by all the first mortgage bonds over prime industrial and commercial property in the FedBond Scheme. Although the bond is registered in the name of the nominee company, the Collective Investment Control Act views it as a debt owing to the participants (investors), and not to the nominee company (Section 57).The properties that make up the security of the investment change whenever a new bond is issued or when a borrower repays their bond. The initial capital is secure and the full amount is repayable after five years. The capital is not subject to the risks of loss and volatility associated with alternative investments such as equities or bonds. The investment is also secured by a first mortgage bond over prime commercial and industrial property.

Not more than 75% of the value of the property may be advanced.

- Full due diligence completed on area, tenant and building
- External valuations on the buildings
- Personal sureties are signed
- Cessation in place for rental income during the term of the bond
- Building insurance in place

Is the interest taxable?

Interest is taxable in the hands of the investor, subject to the income tax regulations which may apply from time to time.- Currently R23 800 for under 65's and R34 500 for over 65's. An IT3b is sent

to clients on an annual basis. Whether interest is being reinvested or taken out, the same applies, because income tax is payable on the earlier of receipt or accrual. The interest accrues to the investor prior to it being reinvested, which therefore makes it taxable.

Who is the ideal client?

The ideal client is a risk adverse investor who would like to receive above average income on a monthly basis, while at the same time preserving the initial capital over a five year period. Part-Bonds offer an investor a secure and reliable vehicle in which to grow their capital by reinvesting their monthly interest – Who would consider a part bond as an investment.

- Fully secure
- Excellent rates
- Low risk
- Regulated under the rules of the CISCA, which is regulated by the FSB
- Alternative investment
- Diversifying a client's portfolio

Source: Fedgroup