

What is a Collective Investment Scheme?

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COLLECTIVE INVESTMENT SCHEME (“CIS”)

A collective investment scheme (“CIS”) can be described as an investment vehicle which allows investors to pool their money into a portfolio, sharing in the risk and return of the portfolio in proportion to their participatory interest in the portfolio. Collective Investments are generally medium to long-term investments.

Unit Trusts are currently the most common CISs in South Africa. Originally these were designed to give ordinary people access to the JSE. The average investor does not usually have sufficient money to buy a spread of quality shares (and a range of shares is important to reduce risk). Via a unit trust an investor can own part of a diversified, professionally managed blue-chip portfolio by investing a modest amount of money, either once-off or on a monthly basis.*

Old school unit trust investors might wonder why there is so much talk about collective investment schemes. Aren't they one and the same thing? The Collective Investment Schemes Control Act 2002, which replaced the Unit Trusts Control Act, makes provision for various types of collective investment schemes, including hedge funds, OICs (open-ended investment schemes), and others. In effect, unit trusts are now one type of collective investment scheme allowed under the Act.*

STRUCTURE OF A COLLECTIVE INVESTMENT SCHEME (CIS)*

Each CIS comprises a number of separate legal entities. The portfolio, which might be referred to as the “fund” or “underlying assets” is made up of the cash contributions of many individuals, which are invested in shares, bonds, cash, property, or other securities. Each participatory interest is in exact proportion to the amount invested by each individual. The “pool” of units or shares reflects the proportional ownership of each participatory interest. Every CIS is governed by a deed, which falls under the authority of the Registrar at the Financial Services Board (FSB). The Registrar has the authority to inspect the work of the trustee and the manager.*

Each CIS is obliged to appoint a trustee or custodian, and one of the functions of the trustee is to ensure that the manager operates the CIS in accordance with the deed. Another important function of the trustee is to act as custodian of all cash and securities in the portfolio. Underlying assets do not in any sense belong to the manager or management company, but are held on behalf of investors by the trustee. This provides important protection for investors.

The manager (still commonly referred to as the management company, although strictly speaking this term is outdated) is responsible for all aspects of the management of the fund, including marketing, creating and selling units (or “participatory interest”), repurchasing units, keeping records, and making investment decisions.

TYPES OF COLLECTIVE INVESTMENT SCHEMES*

CISs can be classified according to the type of structure or the types of underlying assets. In terms of structure, most CISs in South Africa are unit trusts, meaning that the portfolio is held in trust for investors by a trustee. In terms of the Collective Investments Schemes Control Act (CISCA) a CIS can also be set up as a company (in which case the participatory interest is a “share” rather than a “unit”). Types of collective investment schemes include (but are not limited to) unit trusts, hedge funds, open-ended investment schemes (OICs), participatory bonds, declared collective investment schemes, and collective investment schemes in property.

While the type of structure used to house a collective investment scheme is not unimportant, classification according to underlying assets is generally of more interest to investors. The underlying assets making up the portfolio of a collective investment scheme could include any or all of the following:



CASH

(money “on call” in overnight deposits)



FIXED DEPOSITS

(fixed-term interest bearing investments)



MONEY MARKET INSTRUMENTS

(for example, Bankers’ Acceptances and NCDs)



BONDS

(loan stock issued by government or parastatals)



LOCAL EQUITIES

(JSE listed)



OFFSHORE EQUITIES

(shared listed on overseas stock exchanges)



DERIVATIVES

(geared instruments such as futures, options and warrants)



UNIT TRUSTS

(some CIS portfolios consists of investments in other CISs, such as fund of funds, which invest in other unit trusts)



PROPERTY

(JSE limited property companies)

*Source: Profile’s Unit Trusts & Collective Investments