

Bonds (debentures)

Definition of the Bonds

Bonds are transferable deeds/ instrument, issued by the companies or governments which represent long term loans, for incremental financial revenue. Usually, they are allocated by public subscription.

Characteristics of the Bonds

- 1) Equal in value. 2) Have nominal value. 3) transferable.
- 4) Could not be divided against the companies.

Terms Applied to Bonds (Bond's names):

1- The Investment Certificates: they are 3 types:

- a. Investment certificates of an increasing nature: Certificates where money remains with the bank for a long term that may extend up to ten years, accumulating an ascending increase (on the principal and interest). At the end of the term, the certificate holder receives what they paid plus the increase (interest).
- b. Investment certificates with a current yield: i.e, annual interest. Certificates that yield a current return, the holder of this certificate receives specified annual interest.
- c. Investment certificates of an increasing value with lottery draws: Certificates that earn increasing interest and are entered into draws to award prizes to the winning certificates.

Investment Certificates with Prize Opportunities

- These blend traditional interest-earning features with prize draws. Investors may receive a fixed interest rate while also having the chance to win additional prizes.
- **Key Features:**
 - **Attractive Interest Rates:** May offer competitive rates alongside the chance to win.

- **Encouragement to Save:** The potential for prizes can motivate individuals to save more.

2- Treasury Bills:

These are short-term bonds issued by the government, usually for a period of three months, and then they are open for public subscription via tenders (=bidding process). These bonds are characterized by a high standard of liquidity because they are short-term and guaranteed. For these mentioned reasons, it is considered the best-seller for the commercial banks, although they yield scant revenue.

3- Loan Bonds:

Negotiable, indivisible certificates of equal face value issued to subscribers in exchange for amounts they lent to the company as a long-term loan. This loan is raised through a public subscription.

Key Features of Loan Bonds

- a- **Issuer:**
 - Typically issued by corporations, municipalities, or government entities to raise capital.
- b- **Structure:**
 - Represents a formal agreement where the issuer borrows money from investors and agrees to pay it back with interest over a specified period.

Types of Bonds Issued by Corporations:

- a- **Ordinary Bond:** A bond issued with a face value equal to the amount paid by the subscriber upon subscription. Upon maturity, the subscriber receives back the face value of the bond and receives fixed interest based on this value.
- b- **Bond Redeemable with an Issue Premium:** A bond issued with a nominal value exceeding the cash value paid upon subscription. (i.e., nominal value is 1000SAR, and issue value paid by the investor is 900SAR, the difference which is 100SAR is paid back to the investor upon maturity) Annual interest is calculated based on the nominal value and not the issue value.

- c- Guaranteed Bond:** An ordinary bond issued with a face value equal to the amount paid by the subscriber upon subscription, based on which interest is calculated. However, this bond is accompanied by a **personal guarantee** (such as a government or bank guarantee) or a real/in-kind guarantee (such as a mortgage established by the company on its real estate for the benefit of these bondholders).

Difference between Bonds and Shares

- 1) The bond is considered a debt on the company; the share is a portion of the capital.
- 2) The bond holder has a right to get a fixed profit, whether the company was in black or in red, but the shareholder would not obtain any benefits, if the company did not get any profits.
- 3) The bond does not give its holder the right to attend the general assembly, vote or control and any other privilege that has been given to the shareholder.
- 4) At dissolution, the bond holder will have the priority to recoup the bond value, nevertheless, the shareholder does not get any amount before dissolving the bonds and pay the debts.

Rules of Transacting Bonds

Bonds are prohibited, because they are based on usury (Riba), which is prohibited by the Holy Quran and Prophetic Sunnah.

Allah's Messenger (ﷺ) cursed the one who accepts usury, the one who gives it, the one who records it and the two witnesses to it, saying, "They are all the same." [Reported by Muslim].

عَنْ جَابِرٍ - رَضِيَ اللَّهُ عَنْهُ - قَالَ: (لَعَنَ رَسُولُ اللَّهِ ﷺ أَكِلَ الرِّبَا، وَمُؤَكِّلَهُ، وَكَاتِبَهُ، وَشَاهِدَيْهِ، وَقَالَ: " هُمْ سَوَاءٌ ") رواه مسلم

The Legitimate Alternatives to Bonds:

A- In case of the companies' deficit:

Rather than taking interest-bearing loans, companies should raise capital via equity issuance (new shares) or forming new joint ventures/partnerships.

B- In case of the governmental budget deficit

1- The individuals' good- loan (without usury/riba)

2- Advancing Zakat Collection The Prophet (peace be upon him) borrowed the Zakat of his uncle Al-Abbas two years in advance.

3- Encouraging public voluntary donations.

4- Imposing Exceptional Taxes to Cover Budget Deficits: