Media Release

Date: 21 January 2019

Funds analysis reveals most exotic SMSF investments – and if they're worth it

A SuperConcepts data analysis of 2450 SMSF funds worth $3.2 billion has revealed why trustees typically make investments in assets that are deemed "exotic".

An upcoming Investment Patterns Report highlights the Top 10 exotic SMSF assets as:

Frozen Semen

"Frozen semen is more tradeable than bullion because you can sell it units," said Phil LaGreca, SuperConcepts analyst. "Think of it as Liquid Gold."

Frozen Semen is often bought in "straws" that require storage using Nitrogen. The value of the semen is aligned to the heritage of the stallion and scarcity of the total volume of semen from this lineage available on the market.

"If a horse comes from a winning line of showjumping or dressage it can command enormous fees for a date night – technically known as 'Stallion Standing Fees'," said Mr LaGreca.

If a stallion is a multiple title winner, the value of its semen increases. This value can experience capital gains if it's highly sort after but has restricted market supply. Traders will hunt for straws that have special value.

"Like any SMSF asset, it needs to be professionally stored and insured, so these costs need to be factored against any capital growth forecasts," says Mr LaGreca.

Commercial Laser

While a $15,000 industrial grade laser is a curious line item in asset holdings, it was an obvious business decision for a Tasmanian beauty salon specialising in hair removal.

The Diode 808 Laser is a Queen among lasers in the court of permanent hair removal.

"Super funds can buy equipment as a business asset and we often see this with small business owners," says Phil LaGreca.

"The super fund leases the equipment to a business, which is typically owned by the members. There are rules around this including a 5% cap on the value of fund investments that are leased to your business.

“Equipment comes with risk and this particular machine broke at some point in the year, which is something that needs to be considered when buying machinery with super funds,” says Mr LaGreca.

ATM

SMSFs buy ATMs with the prospect of regular income via monthly flat fees, plus a fractional transaction fee.

The reality of ATM investing took a sour turn in recent years after SMSFs found the returns not quite as promised.

ATM “owners” buy the machine from a distributor who places them in high traffic areas such as petrol stations, shopping centres and supermarkets.

The SMSF would then pay the same distributor to service the ATM and collect and remit the fees back to the fund. Until they stop.

Distribution companies can lose contracts, go out of business, and the fees dry up.

In some cases, SMSFs are sold ATMs that don’t exist, or are paid with fees taken from new ATM investors until the scheme falls apart.

“Quite often ATM investors sign a 10 year lease, which makes them pretty obsolete and impossible to sell at that point,” says Phil LaGreca.

“Capital depreciation is inherent in buying machinery or equipment, which means it’s done for the income but an SMSF needs to know if the loss of capital for an upfront investment is offset by the expected returns.

“Physical assets come with different risks to financial assets because they are subject to damage, wear or theft.

“Many times people buy these things with their super funds to help their own business due to cash flow restrictions,” says Mr LaGreca.

Commercial washers and dryers

While washers and dryers don’t normally ignite the flames of investment passion, SuperConcepts funds analysts discovered one SMSF with $134,000 worth of washers and dryers that returned $55,000 income for the 2018 FY.

“It’s impressive but the income will decline each year and there are increasing maintenance costs, which over time will render the machines worthless,” says Mr LaGreca.

In this case the SMSF purchased from an Australian supplier and offered hire purchase agreements with the option for the party to buy at the end of the agreement.

"These particular machines were leased to holiday parks, aged care facilities and motor inns, so they had a very steady income," Mr LaGreca said.

Water vending machine

One SMSF backed up their concerns about reducing plastic bottles on the environment by investing in an ethical alternative.

Water Kiosk Vending bills itself as providing a return that makes a difference, helping the environment and making a profit.

"We noticed a fund with $27,500 invested in two of these kiosks that produce still or sparkling water and also have a stainless steel bottle available for purchase," says Mr LaGreca.

"It's currently returning 15% p.a, which is decent, and they seem to move them around shopping centres, unis, so good foot traffic areas.

"While it's providing a good return on its own, this is a pretty good example of the flexibility and freedom that an SMSF gives you for ethical investment vehicles, which we're seeing more of," he says.

Water rights

Rural properties have various rights in the title deed and water rights are often split out. Why? So you can trade your water rights with other parties.

One SMSF held "260 units" of water rights typically bought per megalitre valued at $563,200.

A fund analysis revealed income from this investment between December 2017 to March 2018 was $15,649.50.

"Just say you've got a river running through your property, you could sell over 100 megalitres to neighbours up or downstream," says Mr LaGreca. "Or sell the water rights back to the original seller and rent the water you use. Or sublease the rights to one party who might retail it to others. You just hope there's always water when you need it."

Not your mothers sewing machine

$18,130 sounded like a pretty fancy sewing machine when SuperConcepts analysts were looking at exotic fund investments. Turns out the Brother 32G automatic tacker sewing machine did a bit more than darn socks really well.

This investment was made by another small business involved in leather working and fabric design. Think saddles, cowboy boots, intricate floral designs on denim jeans.

“Calculating the return on an investment such as this would depend on the market size, contracts in play, and the value of the work being produced in the time frame before it’s superseded technology,” says Mr LaGreca.

“The same issues of running costs, maintenance, down time and similar factors would need to be incorporated to understand the total performance of this investment over the span of its limited lifespan.

“This particular investment has not performed well with reported income from 2011-17 being $13,288.55,” says Mr LaGreca

Cattle

Livestock is the rural equivalent of urban machinery in terms of SMSF investments.

“Farmers regularly buy livestock as an asset that is leased back to the business,” says Mr LaGreca.

“These are typically leased back for the production of milk and dairy products, so they’re usually around for longer than say cattle bred for meat stock.

“The other thing we’ve seen is they are kept for breeding and the calf are sold,” he said.

And how is the return on investment calculated?

“Offspring are recorded as distributions, so they’re like a dividend of the mother who was the initial asset,” says Mr LaGreca.

Taxi Plate

It might be the world’s most utilitarian vanity plate, but some people still pay $220,000 for a T Plate.

“This Canberra-based taxi plate has been purchased as an income generating asset,” says Mr LaGreca.

“The value is derived from the fact that a limited number of licenses are made available to provides the right to operate a taxi.

“The value in this asset is changing because the limited right to operate is being disrupted by ride sharing services that allow anyone to become a fare-charging driver,” says Mr LaGreca.

A beaut Ute

A 1950 Austin A40 Ute valued at $4000 is categorised as a collectible item in terms of a fund’s asset allocations. The question begs whether $4000 in any generic blue chip stock paying regular dividends would be a wiser investment?

The rarity of collectibles give rise to the idea that scarcity improves the value among buyers looking for that particular item. It firstly assumes a market exists for the item. And that there are so few of these available that its perceived value outweighs the actual value.

There are some rules around collectibles. Basically they can’t be used for personal use, must be stored correctly away from the owner’s primary residence, and be insured.

“We’ve seen more than one SMSF fund with a classic car, but you can’t buy it and drive it or rent it to a related party,” says Mr LaGreca. “So it takes some of the fun out of it if you can only store it and insure it.

“Some people do rent them out for income, as wedding vehicles for example, and they hope it’ll appreciate over time if they hang onto it.

So what are the rules around SMSF investments?

The freedom of an SMSF means that you directly invest in what you think is best for your fund. The most common exotic investments are allocated as either “collectible” or “in-house assets”, but there are strict rules dictating how these must be treated to avoid adults simply regressing to buying toys they never had as kids.

In-house assets

These are usually the business assets used to generate income. Think the premises that a small business operates from, or the plant machinery that underpins the revenue generating aspect of a business.

An SMSF cannot invest more than 5% of its total fund assets in “in-house assets”.

An in-house asset is any asset subject to a loan or lease agreement with a related party or an investment in a related company or trust.

Some assets are specifically excluded from being an in-house asset, such as commercial property which means the 5% cap doesn’t apply.

Business assets like machinery, horses, taxi plates, washers & dryers would be in-house assets if leased to a related party.

That means either:

- The market value of all in-house assets held by an SMSF cannot exceed 5% of the value of the funds; or
- If the market value of these assets is over 5%, the trustees can only lease these assets to unrelated parties.

Collectibles and personal use assets

This is the area where SMSF investment passion is on full display.

We're talking artwork, jewellery, antiques, artefacts, coins, medallions and bank notes, postage stamps and first day covers, rare folios, manuscripts and books memorabilia, wine or spirits, cars, recreational boats, memberships of sporting or social clubs, and other assets used or kept primarily for person use or enjoyment (excluding land).

The Cooper Review imposed some restrictions to ensure assets were bought for genuine investment purposes such as generating income and capital growth.

For collectibles, there are now a series of additional specific investment standards that are to be met by the SMSF. These are:

- Asset not leased to a related party,
- Asset not stored in a private residence of a related party,
- Documented decision of asset storage,
- Asset to be insured within 7 days of acquisition in the SMSF's name
- Asset not used by a related party, and
- If asset disposed of to a related party must occur at market price assessed by a qualified independent valuer.

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