



# THE OXFORD CLUB'S ULTIMATE INCOME LETTER

*Retire Early... Retire Rich* | DECEMBER 2010/JANUARY 2011, VOLUME 02, NO. 12

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## Real Estate Bounce Or Not, This REIT is Money in the Bank...

by Louis Basenese

Dear Member,

Alexander Green and I completely agree that home prices won't rebound in 2011. And we're not alone in our predictions, either...

The chief economist for price-data provider, Zillow, says price declines are "going to continue into 2011." That's after suffering a \$1.7 trillion drop in value in 2010. (Ouch!) And Morgan Stanley predicts much of the same. In a recent report, it said price declines should extend through 2012.

Of course, the continued malaise in the residential housing market all boils down to fundamentals. They flat out stink.

A mounting inventory of foreclosed homes – currently eight million are in some stage of default – promises to flood the market with supply for years. Meanwhile, demand is all but guaranteed to remain weak thanks to high unemployment, tighter lending standards and a high percentage of homeowners with negative equity (23.2%).

However, just because the residential market is in the tank, doesn't mean ALL types of real estate suffer from similarly gloomy prospects.

In fact, there's one niche that's enjoying fundamentals that are exactly the opposite. According to Tier 1 Research, demand for this type of real estate is growing twice as fast as supply. And that growth trend promises to extend through at least 2012.

Even better, potential buyers remain among the market's most financially fit. They're sitting on enough buying power to fuel \$100 billion worth of purchases each quarter.

Given such compelling fundamentals, it's time we shrug off the knee-jerk reaction to avoid all things real estate and tap into this under-the-radar niche for reliable income and appreciation in 2011 (and beyond).

So let's get to it...

## We Must Build it Before They Browse

The type of real estate I'm talking about is none other than data centers – highly specialized and secure buildings that house networking, storage and communications technology infrastructure.

Think servers, storage devices, switches, routers and fiber-optic transmission equipment. Or more plainly, the guts that run the internet and the businesses that rely so heavily on being online.

Demand for such buildings is booming worldwide simply because our love for the internet keeps booming. Industry giant, Cisco Systems, predicts that internet traffic will triple by 2014 to 64 exabytes per month. (To put that in perspective, it only takes five exabytes to store every word ever spoken.)

Of course, before such a dramatic ramp-up can occur, we need the infrastructure to facilitate it.

Accordingly, Tier 1 Research expects that global data center demand should easily outstrip supply for the foreseeable future. In 2012, for instance, the research firm estimates that data center demand should jump 16%. Meanwhile, supply should only increase by 7%.

Such a supply and demand imbalance always leads to profits. It's basic economics. And the good news is we can tap into this imbalance without the hassle (and expense) of building our very own data center. All we have to do is snap up real estate investment trust, **CoreSite Realty Corp.** (NYSE: COR).

## Tapping the Data Center Boom for Reliable Income

Denver-based CoreSite owns and operates a portfolio of 11 data centers, offering over two million net rentable square feet. Its facilities are located in some of the largest and fastest-growing areas in terms of data center demand – Los Angeles, Chicago, New York City, San Francisco Bay and Northern Virginia.

Its business is strikingly simple. All it does is rent out data center space – from an entire building down to a single cage or cabinet. The

benefits of companies outsourcing their data center needs to CoreSite are numerous. They include quicker time to market, scalability, no need for financing and cost reduction, all thanks to economies of scale.

Based on CoreSite's growing customer list, which includes AT&T, Microsoft, Google, Facebook and The Nasdaq OMX Group (among others), this is clearly a business model with significant merit and profit potential. Especially since CoreSite is uniquely positioned to capitalize on the substantial uptick in data center demand that Tier 1 Research is predicting. Consider...

- Based on its current real estate holdings, CoreSite can easily double its square footage that's available for rent.
- It can expand quickly via acquisitions. The company grew from one data center when it started operations in 2000 to its current size of 11 facilities, most via acquisitions. Management is now both experienced and in a financial position to take advantage of irresistible opportunities.
- The compelling industry growth trends – and supply constraints – also allow CoreSite to charge higher rent. In the last quarter alone, the company realized a 23% increase in rental rates on renewals.

Since CoreSite is structured as a REIT, it's required to pay out 90% of earnings to us. Which means that as the company's data center footprint – and profits – grows, so should our income.

The company currently pays an annual dividend of \$0.52 per share. That's equal to a respectable 4% yield. However, I expect the yield to increase significantly. I say that because industry peer, Digital Realty Trust, boasts a similar growth strategy (via acquisitions). And since going public in 2004, it has roughly doubled its yield.

In my opinion, CoreSite holds equal promise. So all we need is a little patience and we should be amply rewarded with a heftier dividend check. (Never a bad thing.)

## Under the Radar and Undervalued

CoreSite only went public in September. To date, only two other data center REITs have gone public. So we're talking about an exclusive club of REITs that's garnering minimal mainstream coverage. Such ignorance bodes well for us in terms of capital appreciation potential, too.

As institutional investors – and then the rest of the investment world – inevitably wake up to the growth in data centers, they should naturally be drawn to CoreSite's enviable fundamentals and bid up share prices.

Getting in ahead of that move and collecting dividends while we wait is an attractive proposition, no doubt. But the opportunity is even sweeter here.

You see, we can currently buy CoreSite at a

20% discount to its IPO price of \$16 per share. Based on its price-to-book ratio, it's also the cheapest data center REIT available with the second-highest yield.

Put simply, CoreSite represents a compelling bargain to capitalize on the next real estate boom in data centers. Considering that private equity juggernaut, The Carlyle Group, is hanging tight to its 60% stake post-IPO, there's no doubt this company boasts compelling long-term profit potential.

So let's follow their lead. Even if it means confessing to friends at the next dinner party that yes, indeed, we're investing in *some* types of real estate in 2011.

**Action to Take:** *Buy CoreSite Realty Corp. (NYSE: COR) at market. And use our customary 25% trailing stop to protect your principal and your profits. OC*

## It's Time for Some Healthcare Reform of Our Own

As you know, we're constantly monitoring each and every recommendation. If a pick is a laggard or key fundamentals change, we have no reservations recommending that you close out your position.

After all, it makes no sense to hang on to an investment when we're not keen on the underlying fundamentals. Especially if we've come across a more compelling opportunity to act on. And that's precisely what's going on with **Health Care REIT** (NYSE: HCN).

You'll recall that we added Health Care REIT to our Perpetual Income Portfolio a little over a year ago. It represented a low-risk way to capitalize on the uncertainty surrounding the healthcare debate. Shares were being unfairly punished. But no matter what happened in Washington, people were certain to keep visiting the doctor and getting old.

Health Care REIT offered other advantages, too, including a geographically diverse portfolio, low tenant turnover and a majority of triple-net leases, whereby the tenants are responsible for most operating costs (taxes, insurance and maintenance). A yield of 6.3% didn't hurt, either.

The recommendation worked out well for us, rising as much as 20% above our entry. We got paid a total

of \$2.74 in dividends along the way, too. However, the recent price action has been less than inspiring.

Shares are off some 13% from their recent high. And fundamentals are to blame.

The company reported third-quarter results that narrowly missed expectations. It raised over \$1 billion in capital, including \$500 million via a stock offering at \$43.75 per share, which dilutes our ownership stake.

Renewed uncertainty over healthcare reform – now that a Virginia judge ruled that a portion of the newly passed law is unconstitutional – is also a factor. Investors simply don't want to be exposed to any healthcare risks, real or perceived.

Add it all up, and I'm convinced we'd be better served redeploying our capital elsewhere. That's why I'm recommending you exit your position in Health Care REIT.

Sell your shares at market for a small gain if you haven't done so already. Since we've held the position for over a year, we also qualify for more favorable tax treatment (never a bad thing). And consider reinvesting the proceeds in this month's recommendation of CoreSite.

# Are You on the IRS' Naughty List?

by Bob Carlson, Advisory Panelist, *The Oxford Club*

Trillions of dollars are hiding in Individual Retirement Arrangements (IRAs). This money is protected from taxation... at least until owners take distributions. And that doesn't sit well with a revenue-hungry government.

Fact is, the Internal Revenue Service (IRS) is keeping a careful watch on what we do with this \$4.3 trillion worth of assets. And some of us aren't being nice.

A recent study of IRA owners over the age of 70 and a half found that a high percentage of those with large IRAs weren't taking their required minimum distributions (RMDs).

Remember, tax law dictates that money in an IRA must start coming out in specific increments no later than April 1 following the year an IRA owner reaches 70 and a half.

The failure of so many taxpayers to take RMDs has created a goldmine of unpaid taxes and penalties. And the IRS is salivating to get its hands on this money.

Here's what you need to know to make sure you're not on their list...

## Making a List, Checking it Twice

If you're over the age of 70 and a half, the IRS should receive two reports from your IRA custodian.

- **Form 5498:** This report provides the IRS with basic information about the owner of each IRA. Name, address, Social Security number, IRA balance and whether an RMD was required for the year.
- **Form 1099-R:** This report is generated if a distribution was taken for the year.

These reports make it easy for the IRS to determine if RMDs are being taken. And yet,

many taxpayers still aren't complying.

When the IRS recently checked the records for a sample of taxpayers, it found that 43% of taxpayers whose Form 5498 indicated an RMD was required didn't have a Form 1099-R on file.

The absence of the form suggests these taxpayers failed to take an RMD. It also suggests that the IRS didn't receive its tax payments. So it's no wonder the IRS is stepping up enforcement to collect this cache of unpaid taxes. Especially since it can also levy a hefty 50% penalty of the RMD amount.

## Three Safeguards Against An IRS Audit

Here are three steps we can all take to stay off the IRS naughty list and avoid penalties and audits:

**Safeguard #1: Leave good records.** Your executor and beneficiary need to be able to locate records of your IRAs easily so they can determine whether you took RMDs for the year.

**Safeguard #2: Report yourself.** If you failed to take an RMD, take it as soon as possible. And report it on Form 5329. There are some excuses for a late RMD. If you think you qualify, say so and attach a statement to the form. Otherwise, pay the penalty.

**Safeguard #3: Know the rules.** Even when you manage your IRAs properly, there are still situations when the IRS' eyebrows may get raised.

- **Multiple IRAs:** When you have multiple IRAs, you compute one aggregate RMD for all the accounts. Then, you decide how you plan to take that RMD (from one account or portions from each). However, if the IRS doesn't think your RMDs add up to the right amount, you might have to

prove it. So be ready.

- **Early Distributions:** The IRS is also keeping an eye on early distributions – withdrawals taken before the age of 59 and a half. Why? Because such distributions are subject to a 10% early withdrawal fee. Since they're reported on Form 1099-R, it's easy for the IRS to determine if you owe money.
- **IRA Rollovers:** When you don't complete a rollover within 60 days, it's treated as a distribution (i.e. – a taxable event). Not too long ago, the IRS used to be fairly lenient and waive the penalty. Nowadays, the agency seems less and less understanding of mistakes and late rollovers. The best bet to avoid problems with IRA rollovers is to have them made directly from one IRA custodian to another.
- **Contribution Limits:** Contribution limits change over time and vary depending on

your age. That creates confusion and many people end up contributing too much to IRAs. And the IRS is looking to crack down on excess contributions.

- **Unconventional Investments:** The IRS is now looking for situations when IRAs are used to invest in small businesses and/or unconventional investments. This is too complicated a topic to cover in depth here. Just know that there are ways to properly invest in such assets and ways that will disqualify your entire IRA, triggering a cannonade of income taxes and penalties. I recommend seeking good tax advice before making any such investments.

Ultimately, the best advice I can offer when dealing with the IRS (on any issue) is to be informed and be proactive. Know the tax rules. And verify all paperwork so you can correct any inaccuracies or inadvertent errors quickly. 

## Simple Oversights Can Lead to Hefty Penalties

In a gesture of goodwill – and to ease the blow of the 2008 market collapse – the IRS suspended RMDs for 2009 so IRA owners who didn't need the distributions could let their balances recover.

Many taxpayers took advantage of the reprieve. But the suspension was only for one year. And there's no indication that Congress plans to suspend RMDs retroactively for 2010 or for any year in the future.

So if you took advantage of the one-year suspension for RMDs, be sure you take an RMD this year (unless you qualify for an exemption). Otherwise, it could cost you dearly. Remember, the penalty for failing to take a RMD is a stiff 50% of the RMD amount.

Even if you didn't take advantage of the suspension, there's reason to be on guard. When the IRS recently studied a sample of Forms 5498 and 1099-R, a sizeable group of taxpayers ended up on the naughty list who hadn't actually broken the rules.

For example:

- In some cases the IRA custodian was wrong. Either a 1099-R wasn't filed when it should've been or the taxpayer wasn't required to take an RMD though the 5498 said he was.
- Some taxpayers turned 70 and a half during the year the form covered but postponed their RMDs until the following April 1 – which they're allowed to do.
- Other taxpayers died during the year and their beneficiaries took the required RMDs.
- In some cases the owners died during the year, but the IRS couldn't locate the beneficiaries. And the IRS couldn't verify if the beneficiaries took the RMDs.

Even if you follow all the rules, it never hurts to review your copies of Forms 5498 and 1099-R each year so you can detect (and correct) any discrepancies early.



# New Year's Resolutions? Bah Humbug!

by Dr. Dan Murphy, Contributing Editor, *The Oxford Club*

An anthropologist from Mars studying how Earthlings would like to view themselves need only do this: Glance at the New Year's resolutions we make every year.

In the United States, we would like to be slender, physically fit, sober, non-smoking people who constantly improve their education, work at highly fulfilling jobs, keep their credit card balances at zero, give back to the community, manage stress well, regularly take adventures and spend lots of time with their families.

Were we to meet such a person, we'd most likely detest them. However, there's no need to worry about such an encounter because within eight weeks of making a New Year's resolution, the percentage of people who stick to any one of the above goals is in the single digits.

New Year's resolutions date back to at least the second century B.C.E., when two-faced Janus was the god in charge of resolutions. One face saw the future. The other one saw the past. This made him ideally suited to choose a new direction in life.

However, if it were as easy to get those holiday pounds off as praying to Janus, we'd still be sacrificing sheep to him in our local temples. Instead we lay down our credit cards at the altars of health clubs, diet plans and bookstores (for the latest self-improvement books), hoping that this year we'll defy the towering odds.

Want a worthwhile alternative? *Don't* make a New Year's resolution this year, or ever again. Instead, decide whether you're ready to make a lifestyle change. If the answer is yes, here are some rubrics:

- ✓ Start with a mini-retreat, preferably not at home, and not less than three days in length.

Whether attempted solo or accompanied by trusted friends, some quiet time is essential. Exercise and good food improve the chances of success. Intoxicants don't. During the retreat, pick one goal.

- ✓ Romance your chosen goal, rather than assaulting it. Read up on the topic. Chat with friends who have actually succeeded in accomplishing this goal. Your friends will be flattered, and you'll be startled by their insights.
- ✓ Lifestyle change is accomplished at a steady walk, not by Olympic long jumps. As Mark Twain said, "Habit is habit, and not to be flung out of the window by any man, but coaxed downstairs a step at a time."
- ✓ Keep this Spanish proverb in mind: "Habits are at first cobwebs, then cables." You see, habits and life patterns are linked to who we are by many strands. And attempting to yank a long-standing behavior out of the web tugs all the other strings. So yes, behaviors are as tough as cables. But if you have the right tools and good energy, cutting those undesired cables and weaving newly chosen ones shouldn't be a problem.
- ✓ Adopt simple goal-appropriate mantras to repeat when your resolve slips. For a healthy diet try, "Fresh fruit and vegetables, lean meat and fish, avoid the white stuff (bread, pasta, rice, potatoes, sugar)." For outdoor exercise, say, "There's no such thing as bad weather, there are only improperly dressed people."

Bottom line, on New Year's day, wake up unburdened by resolutions. During the upcoming weeks, think about the person you'd like to be. Pick one goal, romance it, accomplish it and when you're wearing the results as comfortably as your favorite sweater, move on to the next goal. **OC**

## THE PERPETUAL INCOME PORTFOLIO

Companies and funds with the financial wherewithal to consistently deliver dividend payouts and a modest amount of capital appreciation to shareholders.

COMPANY/SYMBOL	REC. DATE	REC. PRICE	CURRENT PRICE	DIVIDENDS COLLECTED	CURRENT YIELD	RATING	TRAILING STOP*
<b>STOCKS</b>							
Aqua America Inc. (NYSE: WTR)	Feb-10	\$16.67	\$22.21	\$0.45	2.9%	Buy	\$16.80
Automatic Data Processing (Nasdaq: ADP)	Nov-10	\$45.27	\$46.86	\$0.36	3.2%	Buy	\$35.14
The Chubb Corp. (NYSE: CB)	Jan-10	\$50.65	\$59.20	\$1.11	2.6%	Buy	\$45.01
Compass Diversified Holdings (NYSE: CODI)	Dec-09	\$11.06	\$16.88	\$1.36	7.8%	Buy	\$13.34
CoreSite Realty Corp. (NYSE: COR)	Dec-10	NEW	NEW	\$0.00	4%	Buy	Use 25% TS
Genuine Parts Co. (NYSE: GPC)	Nov-09	\$37.15	\$51.12	\$2.04	3.2%	Buy	\$38.42
Getty Realty Corp. (NYSE: GTY)	Oct-10	\$28.95	\$30.85	\$0.00	6.4%	Buy	\$23.23
Health Care REIT Inc. (NYSE: HCN)	Nov-09	\$43.42	\$45.11	\$2.74	5.1%	Sell	Take Profits
Inergy, L.P. (NYSE: NRGY)	Nov-09	\$32.12	\$39.10	\$2.79	7.4%	Hold	\$32.02
Kimberly-Clark Corp. (NYSE: KMB)	Jul-10	\$62.40	\$62.74	\$1.32	4.3%	Buy	\$49.65
RPM International Inc. (NYSE: RPM)	Sep-10	\$18.80	\$21.50	\$0.21	4.0%	Buy	\$16.34
Southern Co. (NYSE: SO)	Nov-09	\$31.96	\$37.90	\$1.80	4.8%	Buy	\$28.85
Tanger Factory Outlet (NYSE: SKT)	Nov-09	\$40.42	\$49.80	\$1.55	3.1%	Buy	\$38.22
Telefonica, S.A. (NYSE: TEF)	Jun-10	\$59.96	\$67.62	\$2.70	6.3%	Hold	\$60.64
Windstream Corp. (Nasdaq: WIN)	Nov-09	\$10.08	\$13.99	\$1.00	7.1%	Buy	\$10.65
<b>BOND/INCOME FUNDS</b>							
Blackrock Ltd Dur Income Trust (NYSE: BLW)	Feb-09	\$12.35	\$16.46	\$1.88	6.0%	Buy	\$14.92
Calamos High Income (NYSE: CHY)	Jun-06	\$14.50	\$12.36	\$5.79	8.0%	Buy	\$11.39
Eaton Vance Sr. Floating Rate Trust (NYSE: EFR)	Feb-09	\$8.15	\$17.00	\$1.74	6.5%	Hold	\$14.45
Eaton Vance Equity Inc (NYSE: EOS)	Jun-06	\$17.25	\$12.00	\$7.51	10.9%	Buy	\$11.73
Western Asset Global (NYSE: EHI)	Jun-06	\$11.95	\$12.76	\$4.47	9.2%	Buy	\$11.28

Prices as of 12/17/2010. \* For stocks, use a 25% trailing stop. For bond/income funds, use a 15% trailing stop. Trailing stops are adjusted to reflect dividends collected.



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