



Teacher Retirement Investment Company of Texas, Ltd.

2017 Annual Financial Report



A Component Unit of the Teacher Retirement System of Texas
Fiscal Year, August 31, 2017

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Teacher Retirement Investment Company of Texas Ltd.

Annual Financial Report
For the Period Ended August 31, 2016

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REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS

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Teacher Retirement Investment Company of Texas, Ltd.

Report on the financial statements

We have audited the accompanying financial statements of the Teacher Retirement Investment Company of Texas, Ltd. ("TRICOT") as of and for the year ended August 31, 2017 and the related notes to the financial statements, which collectively comprise TRICOT's basic financial statements as listed in the table of contents.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to TRICOT's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of TRICOT's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Teacher Retirement Investment Company of Texas, Ltd. as of August 31, 2017, and the changes in financial position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other matters***Required supplementary information***

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis be presented to supplement the basic financial statements. Such information, although not a required part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. This required supplementary information is the responsibility of management. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America. These limited procedures consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.



Austin, Texas

November 3, 2017

Teacher Retirement Investment Company of Texas Ltd. Management's Discussion and Analysis (Unaudited)

The following is Management's Discussion and Analysis (MD&A) of the Teacher Retirement Investment Company of Texas Ltd.'s (TRICOT) financial statements as of August 31, 2017 and for the year then ended. The information presented here should be considered in conjunction with other areas of the *TRICOT Annual Financial Report*.

FINANCIAL HIGHLIGHTS

Teacher Retirement Investment Company of Texas Ltd., (TRICOT), a private limited company incorporated in the United Kingdom (UK) began operations in fiscal year 2016. TRICOT, as a separate legal entity, is a wholly owned subsidiary and blended component unit of the Teacher Retirement System of Texas (TRS) Pension Trust Fund.

- TRICOT's primary purpose is to increase the size and number of investment opportunities for the TRS portfolio, especially in private equity funds, real assets funds, and co-investments for either of those investment types.
- TRICOT helps support the sourcing and portfolio management of TRS' \$10 billion in exposure to private investments in Europe through 75 investment vehicles and 28 manager relationships.
- Since inception, the TRICOT team has identified 116 potential deals totaling \$13.3 billion in equity. More than half of these deals were identified in 2017, achieving the target to increase deal opportunities by 50% over the prior year. As of August 31, 2017, TRICOT-sourced deals had \$728 million in exposure to private investments in Europe through 5 investment vehicles under 4 manager relationships.
- TRICOT's net position was \$204,717 as of August 31, 2017.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to TRICOT's financial presentation, which consists of the following components:

- Fund financial statements
- Notes to the financial statements
- Required supplementary information

Collectively, this information presents the net position restricted for fiduciary activities as of August 31, 2017, and summarizes any changes in net position for the year then ended. The information available in each of these sections is summarized as follows:

***Teacher Retirement Investment Company of Texas Ltd.
Management's Discussion and Analysis (Unaudited) - Continued***

Fund Financial Statements

Fiduciary fund financial statements are presented as of August 31, 2017. These financial statements reflect the resources available to pay administrative expenses related to TRICOT's mission.

Notes to the Financial Statements

The financial statement notes provide additional information that is essential to a full understanding of the data provided in the TRICOT financial statements. Information available in the notes to the financial statements is described below:

- Note 1 provides a general description of TRICOT and a summary of significant accounting policies, including the basis of accounting, budgets and appropriations, and explanations of major asset and liability classes.
- Note 2 provides information on capital assets.
- Note 3 describes cash, deposits and deposit risk factors.
- Note 4 provides information on operating leases.
- Note 5 presents tax disclosure information.

Required Supplementary Information

Required supplementary information for TRICOT consists of Management's Discussion and Analysis.

FINANCIAL ANALYSIS OF TRICOT

Net position restricted for fiduciary activities at August 31, 2017 was a \$204,717.

Additions from amounts paid on behalf of TRICOT and transfers in from Teacher Retirement System of Texas (TRS) totaled \$2,057,007.

Deductions from TRICOT's net position restricted for fiduciary activities are predominantly administrative expenses. During fiscal year 2017, administrative expenses and transfers out totaled \$1,953,376.

A condensed summary of TRICOT's financial statements are presented as of August 31, 2017 and for the year then ended. Comparative data in total as of August 31, 2016, and for the year then ended has also been presented.

Fiscal year 2017 increase in cash and receivables is due to expenditures reimbursements that were outstanding at year end. Prepaid and other increased due to the addition of a new lease. Accounts payable and other increased due to expenditures that were outstanding at year end. Amounts paid on behalf of TRICOT decreased due to a reduced need for consulting services. Transfers in from TRS and administrative expenses increased because these expenditures are cost based and the prior year was not a full year of operations.

Teacher Retirement Investment Company of Texas Ltd.
Management's Discussion and Analysis (Unaudited) - Continued

Statement of Fiduciary Net Position (Condensed)

	Fiscal Year 2017	Fiscal Year 2016	Dollar Change	Percentage Change
Assets				
Cash and Receivables	\$ 163,094	\$ 56,008	\$ 107,086	191.2 %
Prepaid and Other	131,981	69,608	62,373	89.6
Capital Assets	7,193	9,831	(2,638)	(26.8)
TOTAL ASSETS	\$ 302,268	\$ 135,447	\$ 166,821	123.2 %
Liabilities				
Accounts Payable and Other	\$ 96,734	\$ 34,361	\$ 62,373	181.5 %
Due to TRS	817		817	100.0
TOTAL LIABILITIES	\$ 97,551	\$ 34,361	\$ 63,190	183.9 %
Total Fiduciary Net Position	\$ 204,717	\$ 101,086	\$ 103,631	102.5 %

Changes in Fiduciary Net Position (Condensed)

	Fiscal Year 2017	Fiscal Year 2016	Dollar Change	Percentage Change
Additions				
Amounts Paid on Behalf of TRICOT	\$ 432,840	\$ 702,077	\$(269,237)	(38.3) %
Transfers In from TRS – Cash	570,796	40,105	530,691	1,323.3
Transfers In from TRS - Expenditures	1,053,371	1,241,618	(188,247)	15.16
TOTAL ADDITIONS	\$2,057,007	\$1,983,800	\$ 73,207	3.7 %
Deductions				
Administrative Expenses	\$1,952,559	\$1,882,714	\$ 69,845	3.7 %
Transfer out to TRS	817		817	100.0
TOTAL DEDUCTIONS	1,953,376	\$1,882,714	\$ 70,662	3.8 %
Change in Fiduciary Net Position	\$ 103,631	\$ 101,086	\$ 2,545	2.5 %

***Teacher Retirement Investment Company of Texas Ltd.
Management's Discussion and Analysis (Unaudited) - Continued***

REQUEST FOR INFORMATION

This financial report is designed to provide a general overview of the Teacher Retirement Investment Company of Texas Ltd. (TRICOT) for those with an interest in TRICOT's finances.

Questions concerning any of the information provided in this report or requests for additional information should be addressed to the Communications Department of the Teacher Retirement System of Texas, 1000 Red River Street, Austin, Texas 78701.

Teacher Retirement Investment Company of Texas Ltd.

Statement of Fiduciary Net Position

AS OF AUGUST 31, 2017

ASSETS

Cash

Cash in Bank (Note 3)	\$	81,980
TOTAL CASH	\$	81,980

Receivables and Other Assets (Note 1E)

Due from Teacher Retirement System of Texas	\$	67,250
VAT (Value Added Tax) Receivable		11,050
Corporate Taxes Receivable		2,814
Prepaid Expenses		47,668
Deposits and Other Assets		84,313
TOTAL RECEIVABLES AND OTHER ASSETS	\$	213,095

Capital Assets (Note 2)

Depreciable Assets	\$	11,989
Less Accumulated Depreciation		(4,796)
TOTAL CAPITAL ASSETS	\$	7,193

TOTAL ASSETS	\$	302,268
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LIABILITIES (Note 1E)

Accounts Payable and Other	\$	4,112
Due to Teacher Retirement System of Texas		817
Payroll Taxes Payable		65,000
Corporate Taxes Payable		27,622
TOTAL LIABILITIES	\$	97,551

NET POSITION

Net Investment in Capital Assets	\$	7,193
Restricted for Fiduciary Activities		197,524

NET POSITION RESTRICTED FOR FIDUCIARY ACTIVITIES	\$	204,717
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The accompanying Notes to the Financial Statements are an integral part of this financial statement.

Teacher Retirement Investment Company of Texas Ltd.

Statement of Changes in Fiduciary Net Position

FOR FISCAL YEAR ENDED AUGUST 31, 2017

ADDITIONS

Amounts Paid On Behalf of TRICOT	\$	432,840
Transfers In from Teacher Retirement System of Texas:		
of Cash		570,796
of Expense		1,053,371
TOTAL ADDITIONS	\$	2,057,007

DEDUCTIONS

Administrative Expenses		
Seconded Employees and Other Services	\$	789,573
Professional Fees and Services		432,981
Materials and Supplies		9,626
Communications and Utilities		3,150
Repairs and Maintenance		4,668
Travel		26,725
Rentals and Leases		309,524
Printing and Reproduction		211
Payroll Tax Expense		327,576
Corporate Tax Expense		28,240
Foreign Transaction (Gain)/Loss/Fees		2,431
Depreciation Expense		2,638
Other Expenses		15,216
Transfers Out To Teacher Retirement System of Texas		817
TOTAL DEDUCTIONS	\$	1,953,376

Net Change in Net Position	\$	103,631
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NET POSITION RESTRICTED FOR FIDUCIARY ACTIVITIES-BEGINNING OF YEAR	\$	101,086
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NET POSITION RESTRICTED FOR FIDUCIARY ACTIVITIES-END OF YEAR	\$	204,717
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The accompanying Notes to the Financial Statements are an integral part of this financial statement.

Teacher Retirement Investment Company of Texas Ltd.
Notes to the Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. REPORTING ENTITY

The accompanying financial statements reflect the financial position of the Teacher Retirement Investment Company of Texas Ltd., (TRICOT), a private limited company incorporated in the United Kingdom (UK). TRICOT, as a separate legal entity, is a wholly owned subsidiary and blended component unit of the Teacher Retirement System of Texas (TRS) Pension Trust Fund. The primary purpose of TRICOT is to increase the size and number of investment opportunities for the TRS portfolio, especially in private equity funds, real assets funds, and co-investments for either of those investment types. TRICOT's Board of Directors is composed of one Managing Director. This Managing Director position is appointed by the Executive Director of TRS.

TRICOT provides investment advisory services exclusively to TRS pursuant to an intercompany agreement. TRICOT does not make investment decisions or enter into investment contracts and has no authority to legally bind TRS. All investment opportunities are referred to TRS for consideration, due diligence, decision-making, and authorization.

B. MEASUREMENT FOCUS, BASIS OF PRESENTATION AND BASIS OF ACCOUNTING

The financial statements present only the financial position and changes in financial position of TRICOT and include all activities for which TRICOT exercises fiscal control and responsibility. They are not intended to, and do not, present fairly the financial position or changes in financial position of TRS. The reporting period is for the fiscal year ended August 31, 2017.

As a blended component unit of the TRS Pension Trust Fund, TRICOT reports its accounts in the same manner, which is as a fiduciary fund. *Fiduciary* funds are used to report assets held in a trustee or agency capacity on behalf of others. TRICOT operations are accounted for with a self-balancing set of accounts that comprise its assets, liabilities, additions and deductions. The fiduciary financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Additions are recognized when earned, and deductions are recognized when the liability is incurred, regardless of the timing of related cash flows. All economic resources, including financial and capital assets, and related liabilities, both current and long-term, and the changes therein are reported in the fund financial statements.

TRICOT is not an employer under UK law and does not make contributions to any retirement plans. TRS employees are seconded from the Austin, Texas headquarters to TRICOT and remain employees and members of TRS for all purposes, including health insurance, pension contributions, benefits, Social Security and Medicare taxes. The salary and benefit costs to TRS for seconded employees are allocated and transferred to TRICOT for transfer pricing and UK corporate income tax reporting purposes. Additionally, TRS employees provide legal, accounting and administrative services for TRICOT. When non-seconded TRS employees perform work on behalf of TRICOT, the proportionate cost of that labor is allocated to TRICOT. No allocation of the pension liabilities and expense for non-seconded TRS employees is necessary or required. TRS' risk management programs apply to TRICOT.

Teacher Retirement Investment Company of Texas Ltd.

Notes to the Financial Statements

TRICOT's accounting records are maintained in United States (US) dollars. Purchases and receipts made in Great Britain Pounds (GBP) are translated into US dollars at the exchange rate on the dates of the transactions.

C. NEW ACCOUNTING PRONOUNCEMENTS

The accompanying financial statements were prepared in conformity with generally accepted accounting principles (GAAP) as prescribed by the Governmental Accounting Standards Board (GASB). During the year ended August 31, 2017, TRICOT implemented the accounting standards shown below. The implementation of Statements 74, 80 and 82 did not have any effect on TRICOT's financial statements.

GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, was issued June 2015 and is effective for fiscal years beginning after June 15, 2016. This statement replaces GASB Statement 43 and establishes standards for financial reporting and amends note disclosure and supplemental information requirements for other postemployment defined benefit plans administered through qualified trusts.

GASB Statement No. 80, *Blending Requirements for Certain Component Units*, amends the blending requirements for the financial statement presentation of component units of all state and local governments and is effective for fiscal years beginning after June 15, 2016.

GASB Statement No. 82, *Pension Issues*, amends certain pension reporting requirements of GASB Statements No. 67, No. 68, and No. 73 and is effective for fiscal years beginning after June 15, 2016.

TRICOT is currently evaluating its accounting practices to determine the potential impact on the financial statements for the following GASB statement:

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, relates to governmental employers that provide postemployment benefits other than pensions and is effective for fiscal years beginning after June 15, 2017.

D. BUDGETS AND APPROPRIATIONS

The administrative costs and capital asset outlay for TRICOT are controlled by annual budgets approved by TRS and the Managing Director of TRICOT.

E. ASSETS AND LIABILITIES

Receivables

Receivables represent the amount of money owed to TRICOT for goods or services delivered or used for which payments have not been received at fiscal year-end.

- *Due from Teacher Retirement System of Texas* represents cash transfer amounts owed to TRICOT by TRS for which payment has not been made.

Teacher Retirement Investment Company of Texas Ltd.

Notes to the Financial Statements

- *Value Added Tax (VAT)* receivables represent amounts owed at fiscal year-end to TRICOT by the United Kingdom for the refund of value added taxes that will not be received until the next fiscal year.
- *Corporate Taxes receivable* represent a tax deferral based upon timing differences.

Prepaid and Other Assets

Prepaid expenses reflect payment for expenses related to rental and lease costs applicable to a future accounting period. Other Assets are deposits made to retain services and rental properties.

Capital Assets

Capital assets associated with the entity's activities are included in the statement of net position. Purchases of capital assets are reported at cost on the acquisition date. Depreciation of all exhaustible capital assets is charged as an expense against operations. Depreciation is calculated using the straight-line method over the asset's useful life. This represents a change in method from the previous year which used an 18% reducing basis method. The difference between the two methods is minimal for fiscal year 2017. Note 2 includes a table identifying the capitalization threshold and estimated useful life by asset type.

Liabilities

Liabilities represent the amount of money owed by TRICOT for goods or services received at fiscal year-end for which payment has not been made as of the balance sheet date.

- *Accounts Payable* represents the liability for assets or services received at fiscal year-end for which payment has not been made.
- *Taxes Payable* represents amounts owed by TRICOT at fiscal year-end but not paid to the United Kingdom until the next fiscal year.
- *Due To Teacher Retirement System of Texas* represents cash transfer amounts owed to TRS by TRICOT for which payment has not been made.

Related Party Transactions

As a blended component unit of TRS, TRICOT relies upon TRS for financial resources. Those resources are recognized through three basic types of revenue.

- Amounts paid on behalf of TRICOT represent amounts paid by TRS on behalf of TRICOT and recognized as revenue in accordance with GASB 24. The associated expenses are also recorded on an accrual basis at the same time in order to present the full costs of operations.
- Transfers in of cash from TRS represent cash contributions for operational expenses, net of any reimbursements from TRICOT back to TRS. The cash transfers are to TRICOT's bank account to provide operating funds to TRICOT. For fiscal year 2017, TRS contributed \$570,796 in cash.
- Transfers in of expense from TRS represent monies paid directly by TRS then allocated to TRICOT for reporting purposes. For fiscal year 2017, TRS contributed \$1,053,371 in transferred expenses.
- Amounts due from TRS totaled \$67,250 at the end of fiscal year 2017 and arise from expenses incurred by TRICOT, however funding has not transferred from TRS. Amounts due to TRS of Texas totaled \$817 and arise from amounts payable to TRS which have not been transferred by TRICOT.

Teacher Retirement Investment Company of Texas Ltd.
Notes to the Financial Statements

NOTE 2: CAPITAL ASSETS

Capital assets are presented at historical cost or, if not purchased, at fair value at the date of acquisition. To the extent assets are purchased by TRICOT for use in operations, appropriate straight-line depreciation has been charged over the estimated useful lives of the assets. Capitalization thresholds for applicable capital asset classes and useful lives for exhaustible assets are shown below:

Asset Class	Capitalization Threshold	Depreciable Life
Furniture and Equipment	\$5,000	5 years

The table below presents the composition of TRICOT's capital assets.

Asset Class	Balance 09/01/2016	Additions	Deletions	Balance 08/31/2017
Depreciable Assets				
Furniture and Equipment	\$ 11,989			\$ 11,989
Less Accumulated Depreciation				
Furniture and Equipment	(2,158)	(2,638)		(4,796)
Capital Assets, Net	\$ 9,831	\$ (2,638)	\$ 0	\$ 7,193

NOTE 3: DEPOSITS

A. CASH AND DEPOSITS

Cash and deposits of TRICOT are maintained in demand deposit accounts with J.P. Morgan Chase Bank, N.A. in the United States (US) and the United Kingdom (UK). As of August 31, 2017 the balance in these accounts totaled \$48,943, and the carrying amount totaled \$81,980.

B. DEPOSIT RISK FACTORS

Custodial Credit Risk

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, the system will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. TRICOT does not have a formal deposit policy for custodial credit risk.

Deposits in US bank accounts are covered by the Federal Deposit Insurance Corporation (FDIC) which insures bank balances less than \$250,000. Deposits in UK bank accounts are covered by the Financial

Teacher Retirement Investment Company of Texas Ltd.
Notes to the Financial Statements

Services Compensation Scheme (FSCS) which insures bank balances less than £75,000. Deposits in excess of these insured amounts are uninsured and uncollateralized. As of August 31, 2017, deposits in TRICOT US and UK bank accounts were not exposed to custodial credit risk

Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of a deposit or an investment. TRICOT does not have a formal deposit policy for foreign currency risk. As of August 31, 2017, TRICOT held \$44,337 in GBP.

NOTE 4: OPERATING LEASES

During fiscal year 2017, TRICOT renegotiated and extended the non-cancelable operating lease agreement for office building space until June 12, 2018. Rental expenses related to the lease for the fiscal year ended August 31, 2017 were \$222,214.

In fiscal year 2017, TRICOT maintained three operating lease agreements for apartments for the TRS seconded employees. The first lease expires August 14, 2018. The second lease expires November 15, 2017. TRICOT signed a third operating lease on another apartment for an additional seconded employee. This lease expires June 20, 2018. Rental expenses related to the leases for the fiscal year ended August 31, 2017 totaled \$84,239.

NOTE 5: TAX DISCLOSURE

A. TAX ON ORDINARY ACTIVITIES

For the period ended August 31, 2017, TRICOT had tax on profit on ordinary activities. The 2017 income tax charge is made up as follows:

• Current tax	
UK corporation tax at 19.58%	\$27,622
Tax overprovided in previous years	<u>0</u>
Total current tax	\$27,622
• Deferred tax	
Origination and reversal of timing differences	\$ 637
Effect of changes in tax rate	<u>(19)</u>
Total deferred tax	<u>618</u>
Tax on profit on ordinary activities	<u><u>\$ 28,240</u></u>

Teacher Retirement Investment Company of Texas Ltd.
Notes to the Financial Statements

B. FACTORS AFFECTING THE 2017 TOTAL TAX CHARGE

The tax assessed on profit/loss on ordinary activities for the year is lower than the standard rate of corporation tax in the UK of 19.58%. The differences are reconciled below:

Profit on ordinary activities before taxation	<u>\$144,319</u>
Profit on ordinary activities at standard United Kingdom corporation tax rate of 19.58% (2016 20%)	28,259
Effects of;	
Expenses not deductible for tax purposes	0
Effect of tax rate changes	<u>(19)</u>
Total tax expense	<u>\$ 28,240</u>

C. FACTORS THAT MAY AFFECT FUTURE TAX CHARGES

The UK Government legislated in the Finance (No.2) Act 2016, which received Royal Assent on September 15, 2016, that the main rate of corporation tax statutory rate would be reduced from 19% to 17% effective from April 1, 2020. This will affect the rate at which future UK cash tax will be payable and has been taken into account in calculating deferred tax.

D. 2017 DEFERRED TAX

Deferred tax asset at September 1, 2016	\$ 3,432
Deferred tax credit/ (charge) to income statement	<u>(618)</u>
Deferred tax asset at August 31, 2017	<u>\$ 2,814</u>
Made up of:	
Depreciation in excess of capital allowances	\$2,814

E. OTHER TAX EXPENSE

Tax expense also includes amounts paid to Her Majesty's Revenue and Customs office by TRS for seconded employees working in the UK. These costs were allocated to TRICOT per the intercompany agreement. Refer to Note 1.B for more information on seconded employees.

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