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By Email to commentletters@efrag.org

Dear Göran,

Re: Public Consultation on Strengthening the European Contribution to the International Standard-setting Process

On behalf of the Accounting Standards Committee of Germany (ASCG) and the German Accounting Standards Board (GASB) we are writing to comment on the EFRAG Proposal for Public Consultation – Strengthening the European Contribution to the International Standard-setting Process (consultation paper). We appreciate the opportunity to comment on the above mentioned EFRAG Proposal for Public Consultation.

In the following we would like to provide the context that influences our detailed comments in *Appendix 1* which we base on the consultation paper and the documents attached as *Appendices 4 through 7*.

We unreservedly welcome and support EFRAG's objective to enhance the EU's proactive input to the IASB. Indeed, we have been involved in EFRAG's work for a long time and value the dialogue and relationship which has developed between both organisations. We also have been urging EFRAG for quite some time to review and enhance its governance to be able to better argue jointly "our case" for a stronger European voice with the IASB and drive our argument for better governance at the IASB.

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Consequently, we welcome EFRAG's proposal. However, while it contains many positive developments, it reflects at least one key contradiction, being that EFRAG seems to want to gain access to the resources of the NSS and NFM while implying that – since they represent national interests – they have to be kept either out of or in a minority in key parts of EFRAG's governance structure.

In addition, our main issues, which we set out in detail in *Appendix 1* are as follows:

- We cannot enter into an agreement with EFRAG which will effectively remove the ASCG's control over its own human resources and work plan.
- The consultation paper sets out a governance structure for EFRAG which, in our view, is too detailed. We believe that EFRAG's governance structure should be kept simple and without conflicts of interests.
- The proposed EU funding of EFRAG is not yet committed. We expect our constituents to make any funding commitments contingent and subject to the funding of EFRAG by the EU.

We are – in essence – an independent organisation with a mandate granted by the German government to set accounting standards in Germany and to represent Germany in international fora dealing with accounting issues. In addressing issues with far-reaching consequences for our constituents, such as the distinction between liabilities and equity, we execute our mandate. We firmly believe that this does not mean we are “representing national interests” but giving national input or feedback for further discussion. We also would argue that a “European perspective” is the result of a broad and intensive consultation process which leads to “a European view” which is then presented e.g. to the IASB.

Therefore, rather than being a passive provider of financing to EFRAG, ASCG and GASB look forward to continue to support actively and engaged EFRAG's role. To the extent EFRAG looks to Germany to provide funding in line with earlier ECOFIN's resolutions we did explain our situation previously to you.

We hope that EFRAG's Supervisory Board will take our detailed comments and our desire to support the proposal's intent into consideration. We are happy to discuss those comments and be available to answer any questions you may have.

Yours sincerely

Neubuerger

*Accounting Standards
Committee of Germany*

Knorr

*German Accounting
Standards Board*



Appendices

- Appendix 1 Joint ASCG and GASB responses to the issues relating to an enhanced governance and operational structure of EFRAG on which EFRAG asks for input in its consultation paper
- Appendix 2 Differences between the EFRAG Consultation Paper and the EFRAG Internal Rules and EFRAG Statutes
- Appendix 3 ASCG/GASB Comments on Rules set out in the EFRAG Internal Rules (Proposal for the general Assembly; Approved by the SB on 16 July 2008)
- Appendix 4 EFRAG staff resources and funding 2008 to 2010
- Appendix 5 EFRAG Internal Rules (Proposal for the general Assembly; Approved by the SB on 16 July 2008)
- Appendix 6 EFRAG Statutes (16 August 2006)
- Appendix 7 Working Arrangement between European Commission and EFRAG (23 March 2006)



Appendix 1

Joint ASCG and GASB responses to the issues relating to an enhanced governance and operational structure of EFRAG on which EFRAG asks for input in its consultation paper

1. Enhancing the EU's pro-active input to the IASB by building on EFRAG's structures and experience

We fully support the objective of enhancing the EU's pro-active input to the IASB via EFRAG. We also agree that EFRAG should not become a Standard Setter within the EU. Rather, in view of the movement towards global financial reporting standards, we would hope that IASB standards can and will be endorsed for adoption within the EU without adjustments or delay.

For this reason we propose to clarify that the statement in the discussion paper that "EFRAG needs to place more emphasis on developing its own research and discussion papers at an early stage of the IASB's consideration" does NOT mean that EFRAG has the objective to develop its own accounting standards. For the same reason we are not supportive of EFRAG engaging in the development of standards for Small and Medium-sized Entities (SME) in the EU.

2. Further involvement of National Standard Setters (NSS) and coordination of European resources and the creation of a Planning and Resource Committee

Further involvement of National Standard Setters

In section 5.1 the consultation paper argues that the proposed EFRAG enhancement is driven by a closer partnership with the NSS by participation of the NSS in pro-active work and through a Consultative Forum of Standard Setters (CFSS).

Given the cooperation between EFRAG and the NSS in the past we fail to see what tangible "enhancement" there is from the NSS perspective, given that

- (i) NSS are not admitted to the General Assembly (GA) or the Supervisory Board (SB) or to the committees where budget decisions are being made;
- (ii) NSS would be offered only limited other rights;
- (iii) going forward, the so far welcomed feedback of NSS on "national issues" may be considered "un-European" since reflecting "national interests"; and
- (iv) furthermore, NSS and NFM are asked to contribute substantial resources (cash and in-kind) to EFRAG in the future;



We would like to point out that NSS work is in the public interest and subject to regulatory oversight. Additionally, NSS have a fiduciary responsibility regarding funds collected from their members, since their contributions are not levies but rather voluntary contributions or membership dues. Therefore, we propose that EFRAG reconsiders how to involve NSS in the overall governance of EFRAG. Related to this we would welcome clarification of what an “associate membership” may entail or criteria which would be applied by EFRAG for admitting new “members” to its General Assembly.

Equally, since NFM are supposed to be granted certain rights in the proposed new EFRAG structure, e.g. membership on the Governance and Nominating Committee and the possibility to be appointed to the SB as “public policy” members, we would welcome if EFRAG clarified who qualifies as NFM and how their representatives are being chosen.

Co-ordination of European Resources

We agree that the European stakeholders should speak with one European voice towards the IASB in order to strengthen the European interest and effectively articulate the European requirements in the IASB standard setting process.

However, we like to point out that “European interests” on standard setting issues will, by definition, NOT be reflective of national interests, but rather of national issues such as laws, national tax issues etc. where solutions will have to be found to reconcile global standard aspirations with local needs. For sure, a compromise has to be found but the need for such compromise has to be accepted by EFRAG and, hence, could not be rejected as being “not in the European interest”.

We hope that EFRAG will recognize this need in an appropriate form since it is also the concept applied by the EU commission itself.

According to the consultation paper, the Planning and Resource Committee will have the task of “organizing the practical work of the NSS to provide input to impact assessment reports coordinated by EFRAG.” The current “Internal Rules” (proposal for the GA, as approved by the SB on 16 July 2008; *Appendix 5*) speak of “assist in organizing”.

As explained earlier, ASCG is an organisation which is obligated to fund and manage the standard setting process in Germany on the basis of a contract with the German government. Therefore, we cannot enter into an understanding or agreement with EFRAG which (i) would effectively subject ASCG or its financial and human resources to the discretion - directly or indirectly – of EFRAG, or (ii) could remove the ASCG’s control over e.g. its own work plan.

For the same reasons, while we are happy – based on prior agreements – to make certain staff available to EFRAG for pre-agreed projects, we will need to be reimbursed for their actual cost if the respective project is led by EFRAG.

We believe the lead of pro-active projects should not automatically be with EFRAG but either with EFRAG or with a NSS, depending on who is most qualified for the respective project or has the issue already on its agenda and has the appropriate resources available. EFRAG could decide on the lead by consensus if more than one party declares an interest in the lead. In the instance that a NSS leads a project, we believe that the respective NSS should also provide at its cost the required resources, but should report to EFRAG such cost to allow for full transparency of the total cost of EFRAG's mandate.

Creation of a Planning and Resource Committee

Given that EFRAG advises the EU on critical matters of broader interest, and given that the EU comprises 27 member states, we believe it would be conceptually appropriate to think of TEG as having to reflect this broad constituency. However, we are also aware that such an ideal approach could result in numerous organisational and practical issues which the EFRAG proposal – indirectly – tries to deal with. We believe that an appropriate approach would be to open TEG so that NSS (where they exist or may be formed) may be (or become) involved in TEG, in particular if those NSS provide EFRAG with important resources. The ASCG and GASB are happy to assist EFRAG in finding constructive solutions to the above mentioned problem.

We advocate keeping EFRAG's governance structure simple and, therefore, argue in favour of a smaller number of committees than currently proposed. We feel this could be accomplished if the current set-up was removed, under which NSS cannot be part of the SB and do not have a voting right on TEG, for the reasons explained above. If all members in TEG including the NSS had a voting right, a PRC would not be required and TEG, as the principal organisation defining and managing EFRAG's technical work programme could be charged with setting the agenda. In such instance, the SB would be able to limit its mandate to oversight of such agenda setting.

If a Planning and Resource Committee (PRC) was created nevertheless, we would object to its proposed composition. The consultation paper proposes that the PRC's members should be four NSS representatives, two members of the SB, two additional members who could be members of the SB, and the TEG chair. The PRC members will be appointed by the SB. We believe that no SB member should be member of the PRC since this would create a conflict of interest (SB members would monitor themselves as PRC members and/or get involved in quasi-executive responsibilities). Furthermore, as pointed out earlier, the PRC's or TEG's decision-making cannot affect the responsibilities that fall into the domain of NSS.



3. Enhanced governance, transparency of EFRAG and accountability to European organizations and institutions

We welcome the consultation paper's proposal to enhance public accountability by changing EFRAG's governance structure, liaising regularly with the EC at relevant levels and opening meetings of the SB and PRC to the public. Additionally, the nomination processes to the various EFRAG bodies will be open, the SB [and PRC] will publish regular reports of their activities, EU approval and the submission of audited financial statements will be required when the EC contributes to the funding of EFRAG.

We note though that founding fathers of EFRAG (i.e. European organisations or associations) will continue to be the only members of the General Assembly (GA). NFM and NSS will continue to be excluded from EFRAG membership and, therefore, from GA membership. As long as NSS are expected to contribute significant funding to EFRAG, EFRAG will have to be accountable to the provider of these funds. Normally, the funding providers are key members of the General Assembly. Consequently, we propose to revise the EFRAG membership criteria to allow membership of all organizations providing resources to EFRAG and to review the voting rights.

In the current proposal the GA will create a Governance and Nominating Committee (GNC) to make recommendations to the GA on the appointment of SB members. However, having thoroughly studied the proposal for the creation and objective of the GNC, we believe that the SB members should not be appointed by the GA based on recommendations of the GNC, but that SB members should be elected by the GA based on set criteria for SB membership which could be reflected in the statutes of EFRAG. Therefore, a GNC could be formed as a committee of the SB rather than the GA and be charged exclusively with appointing TEG members (and PRC members if this committee was established under the new structure).

While the SB will no longer be exclusively composed of representatives of EFRAG's founding fathers, we note that the IASCF proposes that the founding fathers continue to appoint the chairman and the vice chairman of the Supervisory Board and will retain the majority on the currently proposed GNC. We also note that preparers, SMEs, users, accountants and public members can become SB members (by appointment via the GNC) but not representatives of NSS, despite the fact that they are asked to contribute funding far in excess of the founding fathers. In line with our proposal regarding membership in EFRAG we propose that all organisations providing funding to EFRAG should also be eligible for election (rather than appointment) to the SB.

The consultation paper proposes the composition of the Supervisory Board (SB) to be reviewed after two years. We currently do not fully understand the need for such a review. Since the proposed restructuring of EFRAG will be extensive, we believe that the best approach would be to have the GA elect a new SB following the changes proposed by EFRAG in its consultation paper as well as our comments on the composition of the SB set out in this comment letter. This would allow the "new" SB

to support and monitor the operational development of EFRAG over an extended period (i.e. the 3 years) subsequent to the “enhancement”.

In section 4.2 the consultation paper argues that one of the principal responsibilities of the SB is “monitoring the progress of the work of [...] PRC”. As already mentioned before, we propose that no SB member should become member of the PRC. Additionally, we propose that the TEG chair should be appointed as chair of the PRC.

4. Balanced involvement of European stakeholders in EFRAG

As already set out above, we do not believe that the NSS are appropriately represented in the proposed EFRAG structure. We also believe that the NFM are not appropriately represented in EFRAG, either. Even though the NFM are potentially eligible to be appointed to the SB as public policy members, only four of the proposed 17 SB members are public policy members and these may also come from public authorities, other relevant public bodies as well as academia, so the chance for any NFM to be appointed to the SB is rather remote. Additionally, it is currently unclear to us what is meant by “relevant public bodies”.

In section 5 of the background paper it is argued that the EFRAG founders represent the same professional backgrounds as the ultimate stakeholders of the NSS and – to some extent – the NFM. In our view, all parties providing resources to EFRAG should be eligible for membership and vote in the GA.

As set out in the consultation paper, in principle, the SB may appoint chairs of up to three NSS to be non-voting members of the TEG. Four NSS are expected to provide fundamental funding to EFRAG. We believe that these four NSS should be appointed to the TEG. To avoid a possible conflict of interest we believe that it does not necessarily have to be the NSS chairs being appointed to the TEG, since the NSS chair could also be a PRC member. The respective person who will be participating in the TEG meetings on behalf of the NSS should be determined by the respective NSS.



5. A significant increase in EFRAG's human and financial resources

We understand that EFRAG will significantly increase financial and human resources to enhance its contribution to the IASB and to be a credible voice from Europe. The consultation paper proposes a total expected budget of EUR 6 Mio. in the short term and EUR 7.5 Mio. in the long term. The funding shall be provided by the NFM European member organizations and the EC. In addition to a base funding by European member organizations and the NFM of total EUR 3 Mio., the EC has indicated its willingness to consider up to 50% of the EFRAG budget, at the earliest beginning in 2010. Prerequisites for the EC funding are that the proposed EFRAG reform set out in the consultation paper will be adopted and the EC finds a legal basis for its funding of EFRAG. However, the proposed EC funding is not yet committed; consequently, we expect our constituency to make its funding commitment contingent and subject to the funding of EFRAG by the EU.

The consultation paper states an expected budget of EUR 6 Mio. and EUR 7.5 Mio., respectively. The consultation paper does neither discuss the planned financing nor the planned spending of EFRAG in sufficient detail to provide stakeholders with the necessary information to make an informed decision. Additionally, we note that the consultation paper does not cover how the additional EUR 1.5 Mio. required for field tests, feedback statements, public hearings etc. shall be borne.

EFRAG expects contributions-in-kind of approx. EUR 1 Mio. for TEG membership and staff secondments and only briefly indicates in the consultation paper that a charging model of these costs will be evaluated. We would welcome more information on the sources of these in-kind contributions and how long they will be provided to EFRAG without reimbursement to be able to assess the viability of the longer term financing of the expenditures of EFRAG.

A budget setting out the expected income and expenditure of EFRAG for the years 2008 to 2010 was provided separately from the consultation paper (*Appendix 2*) and was not issued for public comment. Further information about the funding of EFRAG is only available on request. It will therefore be difficult for third parties to understand the proposed financing and spending of EFRAG's expected budget without having requested this further information. Additionally, the budget paper provided separately indicates a required budget for 2010 of EUR 6.5 Mio. instead of the EUR 6 Mio. proposed in the consultation paper. The budget for 2008-2010 provided by EFRAG and the budget set out in the consultation paper do not match. Consequently, it is unclear which budget will be the one the NSS and other relevant parties are expected to finance in the end and which one will be the basis for the proposed 50% EC funding of EFRAG. We would welcome more information on this matter.

6. Other comments

We propose that a thorough reconciliation of the Internal Rules and the EFRAG Statutes with the final EFRAG structure and role is being conducted prior to any approval of the EFRAG Internal Rules by the General Assembly. This is being recommended as we note that the current version of the EFRAG Internal Rules and



the EFRAG Statutes differ in various aspects from the consultation paper (*Appendix 2*). We believe such documents are essential to a final and binding commitment by all parties concerned, including the EU Commission. We also believe that a review of the current working arrangement between the EC and EFRAG will have to be performed to reflect EFRAGs enhancement decisions.

In *Appendix 3* you will find preliminary comments on the Internal Rules of EFRAG.



Appendix 2

Differences between the EFRAG Consultation Paper and the EFRAG Internal Rules and EFRAG Statutes

EFRAG Internal Rules

Article 5: The Internal Rules define an Audit and Budget Committee (Article 6) and a Nominating Committee of the SB (Article 7). The Consultation Paper is silent on the ABC, and the Nomination Committee is proposed to be renamed to “Governance and Nominating Committee”.

The **Nomination Committee for the SB** (NC) is now named “Governance and Nominating Committee” (GNC) under the proposed new structure. However, in the Internal Rules in Article 5 it is named “Nominating Committee for the SB”. In Article 7 it is named “Nominating Committee for the TEG and PRC”.

Article 7: In the proposed new structure, there is no specific Nominating Committee for PRC and TEG, as is currently in the Internal Rules. If this Nominating Committee is the new proposed Governance and Nominating Committee, then its role is to nominate candidates for the SB only, not for TEG and PRC. Additionally, the number of members in the NC as per the Internal Rules is inconsistent with the number and role of members of the proposed GNC as per the Consultation Paper.

Article 8: The Internal Rules state that the SB appoints the TEG chair and can appoint the TEG vice-chair

The Discussion Paper only proposes the responsibility of the SB to appoint TEG members (not the respective positions within TEG).

Article 11: The definition of the role of TEG needs to be revised according to the role defined in the final EFRAG structure paper.

Article 20: The Internal Rules state that the PRC members will be appointed by the SB; however, it does not state that the appointment is following a public call for candidates.

The description of requirements for “other members” of the PRC should be uniform in the Internal Rules and the Consultation Paper:

Internal Rules: “Two additional members (that may have other backgrounds or alternatively could be members of the SB but at least have professional backgrounds that are representative of financial reporting stakeholders at large. [...] All members



should be persons of high standing that have recent experience of financial reporting and insight into the major reporting issues and objectives of European stakeholders.”

Consultation Paper: “two additional members (who have other professional backgrounds...) [...] All members should be of persons of high standing who have recent experience of financial reporting (but who are not necessarily technical accounting experts) and insight into the major reporting issues and objectives of European stakeholders.”

Article 20 No. 2 of the Internal Rules states that the Nominating Committee for the TEG and PRC recommends the appointment of PRC members to the SB. The proposed EFRAG structure in the Consultation Paper does not mention a Nomination Committee for TEG and PRC.

The Internal Rules also request in No. 2 that “NSS represented on the PRC shall provide a formal commitment to provide a certain level of staff resources for the term of appointment of its representatives to the PRC”. The Consultation Paper is silent on additional resource expected from NSS PRC members.

The Internal Rules propose that a call for candidates can be organized amongst the NSS before selecting the four members representing the NSS. The Consultation Paper currently requires a public call for the four representatives of the NSS.

Article 21: The Internal Rules define the objective of the PRC to “ensure that the subjects added to the long term proactive agenda are the most important accounting issues seen from a European point of view”. The Consultation Paper does not include this objective when defining the role of the PRC.

The role of the PRC in the Internal Rules and the Consultation Paper should be defined consistently. Currently, the definitions differ in a number of issues, e.g.

- “Assist in organizing the practical work of NSS ...” (Internal Rules) and “...organizing the practical work of NSS ...” (Consultation Paper) or
- “...set the agenda for pro-active work in relation to issuance of discussion papers...” (Internal Rules) and “set the agenda for proactive work that results in the issuance of discussion papers ...” (Consultation Paper).

Article 25: The Internal Rules state that “the PRC can advise the TEG to establish a Working Group that provides advice for the purpose of a pro-active project.” The role definition of the PRC in the Consultation Paper is silent on this issue.

Article 27: The Internal Rules state that “the Audit and Budget Committee [ABC] of the SB monitors the expenditures within the limits of resources authorized by the GA.”

The Consultation Paper does not define the ABC and does not mention the expenditure monitoring in the role definition of the SB.



Appendix 1 to the Internal Rules (Statutes of EFRAG)

Section 3: The Statutes of EFRAG state that the Governance and Nominating Committee for the SB shall comprise of up to 7 members. Two members of the Committee will be representatives of NFM. The Consultation Papers does not define a maximum number of members of the GNC but defines that 1/3 of the GNC members will be from NFM. Additionally, it is not defined how to deal with an odd-numbered total of members (1/3 of 5 is 1,666; so will there be 1 or 2 NFM member(s) in the GNC?).

The role of the GNC defined in the Statutes is broader than in the Consultation Paper.

Statute: The role of the Committee is to seek candidates for membership of EFRAG's Supervisory Board, select the most qualified candidates and make recommendations to the GA on behalf of its members."

Consultation Paper: "The GA will establish a GNC to make recommendations to the GA on the appointment of SB members...".

Appendix 3

ASCG/GASB Comments on Rules set out in the EFRAG Internal Rules (Proposal for the General Assembly, Approved by the SB on 16 July 2008)

Article 3: The Internal Rules state that the SB appoints a vice-chair who shall chair the PRC as defined in Article 20 of the Internal Rules.

The ASCG and GASB propose that no SB member should also be member of the PRC and that the TEG chair should chair the PRC.

Article 10: The Internal Rules state that the SB may appoint three chairs of NSS as non-voting members to the TEG.

The ASCG and GASB believe that the four NSS expected to provide fundamental resources to EFRAG should be appointed to the TEG and that the respective person representing the NSS on TEG meetings should be determined by the respective NSS.

Article 19: The Internal Rules state that

- if members of EFRAG, TEG, PRC or the SB publish articles or statements they should carefully consider the potential negative impact on EFRAG and
- if TEG expects the article of a TEG members that directly or indirectly mentions their links to EFRAG to have a negative impact on EFRAG the publication cannot take place.

The ASCG and the GASB believe that this should not only apply to negative impacts but to any impact a publication or statement of an EFRAG, TEG, PRC or SB member might have on EFRAG.

Article 20: No. 2 (second bullet point) states that “if necessary, a public call for candidates at large will also be organised for two stakeholder representatives if they are selected from outside the SB”.

The ASCG and GASB do not believe that the wording “if necessary” is appropriate. A public call should be organised for all members on the SB.

Article 21: The Internal Rules state that the high level Consultative Group (CG) organised by the PRC will focus on conceptual and policy issues.

The ASCG and GASB believe that the issues the Consultative Group shall focus on are fairly wide and, therefore, require a large CG with either a large variety of specialists or a group rather consisting of generalists. A group of specialists bears



the risk that generally some members of the group will detach themselves from the discussion of certain issues they are not specialised in. A group of generalists may be smaller in size but bears the risk that the members have only general knowledge on the issues under discussion. Therefore, the consultation provided by this group would only be on a general basis.

The Internal Rules state that a subgroup of the PRC consisting of the TEG chair and the non-SB members of the PRC shall manage the joint resources.

The ASCG and GASB propose that no SB member shall also be member of the PRC since the role of the SB is to supervise the PRC and SB members being also PRC members would lead to the members supervising themselves. Bearing this in mind, no subgroup of the PRC would be necessary if no SB members will also be PRC members.

Article 27: The Internal Rules state in No. 3 that “the SB will organise an annual meeting with organisations that are not members of the Association but accepted to contribute to the funding of EFRAG. This meeting will be aimed at discussing funding and governance issues”.

The ASCG and GASB believe that this rule in the Internal Rules is only supposed to appease the non-member stakeholders, especially those providing fundamental funding to EFRAG. NSS and NFM are not granted sufficient rights in the EFRAG structure in relation to the funding they are expected to provide to EFRAG. A once-a-year meeting to discuss funding and governance issues without any right to decide on these issues does not make any difference.