III

(Preparatory acts)

EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 11 May 2018


(CON/2018/25)

(2018/C 261/01)

Introduction and legal basis

On 1 February 2018 the European Central Bank (ECB) received a request from the Council of the European Union for an opinion on a proposal for a Council Directive laying down provisions for strengthening fiscal responsibility and the medium-term budgetary orientation in the Member States (1) (hereinafter the ‘proposed directive’).

The ECB’s competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union (TFEU) since the proposed directive is relevant to the primary objective of the European System of Central Banks of maintaining price stability, as referred to in Articles 127(1) and 282(2) of the TFEU and Article 2 of the Statute of the European System of Central Banks and of the European Central Bank (hereinafter the ‘Statute of the ESCB’). The ECB is also competent to be consulted on the proposed directive under Article 126(14) of the TFEU, which is the legal basis of the proposed directive, according to which the Council of the European Union shall, acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and the ECB, adopt the appropriate provisions which shall then replace Protocol (No 12) on the excessive deficit procedure annexed to the TFEU and the Treaty on European Union. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. General observations

1.1. The financial and economic crisis has clearly demonstrated that ambitious reform to the economic governance framework is in the profound and overwhelming interest of the European Union, the Member States and, in particular, the euro area (2). The Stability and Growth Pact (SGP), which is implemented and reinforced through secondary legislation in the form of Council Regulation (EC) No 1466/97 (3) and Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies (OJ L 209, 2.8.1997, p. 1).

(1) COM(2017) 824 final.
(2) See Opinions CON/2011/13 and CON/2012/18. All ECB opinions are published on the ECB’s website at www.ecb.europa.eu
(3) See Opinions CON/2011/13 and CON/2012/18. All ECB opinions are published on the ECB’s website at www.ecb.europa.eu
In line with the position expressed in the context of the adoption of the abovementioned legal acts, the ECB welcomes the proposed directive, which aims to integrate the substance of the Treaty on Stability, Coordination and Governance (TSCG) into the Union legal framework. The proposed directive follows up onto Article 16 of the TSCG, which called for incorporating the substance of the TSCG into the Union legal framework within five years from the date of entry into force of the TSCG, i.e. by 1 January 2018 (¹). The substance of the TSCG has been interpreted by the European Commission to correspond with the so-called ‘fiscal compact’ (²). The ECB considers that several amendments to the proposed directive are necessary in order to further strengthen fiscal responsibility in the Member States, simplify the legal framework and ensure more effective implementation and enforcement of fiscal rules at Union and national level.

2. Specific observations

2.1. Simplification of the current legal framework

2.1.1. The proposed directive aims to simplify the legal framework and ensure a more effective and systematic monitoring of implementation and enforcement of fiscal rules at both Union and national level, as part of the overall Union economic governance framework. The proposed directive also aims to diminish the possible risks of duplications and conflicting actions inherent in the co-existence of intergovernmental arrangements alongside the mechanisms provided for under Union law. While the ECB welcomes, as stated in paragraph 1.2, the objectives of the proposed directive, it has concerns as to whether the proposed directive achieves these objectives.

2.1.2. As regards the TSCG, the proposed directive aims to integrate the fiscal compact into Union law. However the provisions of the proposed directive deviate substantially from those of the fiscal compact, which may lead to a weakening of the rules of the fiscal compact and increase uncertainty as a result of the coexistence of multiple fiscal frameworks. In particular, the fiscal compact rules are weakened due to the fact that the proposed directive does not contain any reference to the Member States’ obligation under the fiscal compact to have their budgetary position in balance or in surplus, or to keep the structural deficit to an upper limit of 0,5 % of gross domestic product, which can become 1,0 % of gross domestic product in cases where the debt level is significantly below 60 % of gross domestic product and where there are low risks to sustainability. In the same vein, the fiscal compact contains the obligation to ensure rapid convergence towards the medium-term objective in line with the SGP. The ECB considers that these obligations need to be clearly reflected in the proposed directive.

³ Article 16 of the TSCG called for taking the necessary steps with the aim of incorporating the substance of the TSCG into the Union framework within five years from the date of entry into force of the TSCG, i.e. by 1 January 2018, on the basis of an assessment of the experience with its implementation. This is also in line with the Five Presidents’ Report on ‘Completing Europe’s Economic and Monetary Union’, Report by Jean-Claude Juncker, in close cooperation with Donald Tusk, Jeroen Dijsselbloem, Mario Draghi and Martin Schulz, 22 June 2015, available on the Commission’s website at www.ec.europa.eu
⁴ The ‘fiscal compact’ is set out under Title III of the TSCG.
2.1.3. In addition, the proposed directive will not replace the TSCG, as the TSCG contains provisions that exceed the scope of the proposed directive. However, since the TSCG will still be applicable for all Member States, with the exception of the Czech Republic and the United Kingdom, the proposed directive does not seem to diminish the risk of duplication and conflicting actions inherent in the coexistence of intergovernmental arrangements alongside the mechanisms provided for under Union law. The explanatory memorandum that accompanies the proposed directive states that the proposed directive should not affect the commitments of the TSCG’s contracting parties made under Articles 7 and 13 of the TSCG. However, the proposed directive will affect the commitments of the Member States that are contracting parties to the TSCG under Article 3 of the TSCG, which contains the fiscal compact provisions, without repealing or replacing them (1). The alignment of the provisions of the proposed directive with Article 3 of the TSCG would ensure clarity as regards the coexistence of the TSCG alongside the proposed directive and contribute to the achievement of the objectives of the proposed directive.

2.1.4. Moreover, the ECB understands that most of the Member States that are contracting parties to the TSCG have already implemented the provisions of the fiscal compact into their national laws. In some cases, this implementation has been made at constitutional or an equivalent level. Considering that the fiscal compact contains provisions that are more stringent than those set out in the proposed directive, in particular with regard to the upper limit for the structural deficit of 0.5% of gross domestic product, it is expected that these national laws will also contain more stringent fiscal requirements. Therefore, if Member States that have not yet fully transposed the fiscal compact into their national law decide to implement the fiscal compact provisions in a more lenient manner due to the proposed directive being adopted, or if some Member States choose to amend their national laws in that manner, this may result in unequal and disparate fiscal rules throughout the Union. This issue reinforces the ECB’s suggestion, which is set out in paragraph 2.1.2, to clearly reflect in the proposed directive the obligations found in the fiscal compact. Ensuring that the provisions of the fiscal compact are reflected will provide legal clarity and equal treatment across the Union.

2.1.5. Finally, as far as the Union fiscal framework in general is concerned, it seems that the proposed directive contains provisions which are similar or related to provisions in the SGP, the ‘Six-pack’ or the ‘Two-pack’. Some examples are the provisions establishing independent bodies found in the proposed directive and in Regulation (EU) No 473/2013, as well as the provisions on numerical fiscal rules and medium-term budgetary frameworks of Directive 2011/85/EU. The ECB is of the view that in these cases, the proposed directive would need to clarify how the provisions of the proposed directive would interact in practice with the already existing provisions in Union law and, if necessary, amend the relevant legal acts to ensure legal clarity.

2.2. Medium-term objective

2.2.1. The proposed directive stipulates that Member States should set up a framework of binding and permanent numerical fiscal rules specific to them. This framework should establish a medium-term objective in terms of structural balance, in order to ensure that the ratio of government debt to gross domestic product at market prices does not exceed the reference value set out in Article 1 of Protocol (No 12) on the excessive deficit procedure (2), or approaches the reference value at a satisfactory pace. The ECB understands that this medium-term objective does not refer to the medium-term objective defined under the SGP, and in particular under Regulation (EC) No 1466/97, and that the intention of the Commission is to create an obligation for Member States to enshrine, in their fiscal frameworks, a medium-term objective that may be different from the medium-term objective set out in the SGP. The ECB considers that the proposed directive needs to define, in a clear and comprehensive manner, how this new medium-term objective in terms of structural balance is defined, and, as noted in paragraph 2.1.2, how it reflects the upper limit for the structural deficit of 0.5% of gross domestic product found in the fiscal compact. Supplying such a definition would ensure that Member States have clarity as regards their obligations and that there are uniform and harmonised fiscal rules across the Union.

2.2.2. The fiscal compact also contains an obligation for the contracting parties to ensure rapid convergence towards their respective medium-term objective in line with the SGP, with the time frame for such convergence taking into consideration country-specific sustainability. The ECB notes that an obligation requiring rapid convergence should be inserted into the proposed directive. It considers that convergence towards the medium-term objective referred to in the proposed directive should be further specified, with the rules in the SGP seen as a minimum convergence pace.

(1) This is a matter to be decided by the contracting parties to the TSCG.
(2) Annexed to the TFEU.
2.2.3. Finally, the ECB welcomes the obligation on Member States to include in their fiscal planning a medium-term growth path of government expenditure, which would be net of discretionary revenue measures, and which would be of a binding and permanent character. In contrast to the expenditure rules referred to in the fiscal compact, which replicate the SGP, the expenditure rule in the proposed directive provides for fixed multiannual expenditure targets to be applied for the duration of the legislative term as soon as new governments take office. These targets must be respected by annual budgets throughout that period. While such a fixed rule might support fiscal discipline and create additional fiscal space in times of economic expansion, more clarity would be needed on how to enforce this rule over the medium term. Moreover, the proposed directive needs to clarify whether Member States would need to adjust their annual expenditure targets in the event of the economy developing differently from the assumptions made by the Member States when they set their multiannual expenditure targets.

2.3. Automatic correction mechanism

2.3.1. The ECB welcomes the introduction of the automatic correction mechanism, in line with Article 3(1)(e) of the TSCG, which goes beyond the procedure for the correction of deviations provided under Article 6(2) of Regulation (EC) No 1466/97. This tool will enable Member States to correct deviations from the medium-term objective and the adjustment path towards it, and to compensate for deviations from the government expenditure path referred to in the proposed directive (1).

2.3.2. The ECB has nevertheless identified a number of elements of this mechanism that could be further revised in order to ensure that the mechanism is applied in a more effective manner by Member States. In particular, while the proposed directive states that the correction mechanism would be automatically activated in the event of a ‘significant observed deviation’, it does not define this term or contain any guidance as to its scope. The ECB suggests defining the term ‘significant observed deviation’ in the proposed directive in order to bring legal clarity to the applicability of the correction mechanism.

2.4. Independent bodies

2.4.1. The ECB supports the provisions of the proposed directive, which aim to strengthen the role of independent bodies by assigning them a mandate that goes beyond their existing tasks under Regulation (EU) No 473/2013. Notably, the ECB welcomes the anchoring of the ‘comply-or-justify principle’ in Union legislation, as this would reinforce the role of the independent bodies in the fiscal surveillance process. However, Regulation (EU) No 473/2013 already provides for the establishment of these independent bodies and assigns to them a number of related tasks. The proposed directive should, therefore, not duplicate existing provisions of Union law, but rather only expand the tasks attributed to these independent bodies in order to ensure that they are able to cover the scope of the proposed directive.

Where the ECB recommends that the proposed directive is amended, specific drafting proposals are set out in a separate technical working document accompanied by an explanatory text to this effect. The technical working document is available in English on the ECB’s website.

Done at Frankfurt am Main, 11 May 2018.

The President of the ECB

Mario DRAGHI

(1) See Article 3(2)(b) of the proposed directive.
**Text proposed by the Commission**

**Article 2 Definitions**

For the purposes of this Directive, the definitions of “government”, “deficit” and “debt” set out in Article 2 of Protocol No 12 on the excessive deficit procedure annexed to the TEU and to the TFEU shall apply.

In addition, the following definitions shall also apply:

a) “exceptional circumstances” means an unusual event outside the control of the Member State concerned and which has a major impact on the financial position of the general government, or a severe economic downturn for the euro area or the Union as a whole;

b) “independent bodies” means bodies that are structurally independent or bodies endowed with functional autonomy vis-à-vis the budgetary authorities of the Member State, and which are

**Amendments proposed by the ECB**

**Amendment 1**

Article 2 of the proposed directive

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<td>b) “independent bodies” means bodies that are structurally independent or bodies endowed with functional autonomy vis-à-vis the budgetary authorities of the Member State, and which are</td>
<td>b) “independent bodies” means independent bodies as defined in Regulation (EU) No 473/2013; means bodies that are structurally independent or bodies endowed with functional</td>
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1 This technical working document is produced in English only and communicated to the consulting Union institution(s) after adoption of the opinion. It is also published in the Legal framework section of the ECB’s website alongside the opinion itself.

2 Bold in the body of the text indicates where the ECB proposes inserting new text. Strikethrough in the body of the text indicates where the ECB proposes deleting text.
<table>
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<th>Text proposed by the Commission</th>
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<td>underpinned by national legal provisions ensuring a high degree of functional autonomy and accountability. (c) “structural balance” means the cyclically-adjusted balance of the general government, net of one-off and temporary measures.'</td>
<td>autonomy vis-à-vis the budgetary authorities of the Member State, and which are underpinned by national legal provisions ensuring a high degree of functional autonomy and accountability. (c) “structural balance” means the cyclically-adjusted balance of the general government, net of one-off and temporary measures.; d) “significant observed deviation” means a deviation from the medium-term objective or the adjustment path towards it that is evaluated in accordance with paragraph 3 of Article 6 of Council Regulation (EC) No 1466/97.’</td>
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**Explanation**

Reference should be made to the existing definition of independent bodies under Regulation (EU) No 473/2013 so as to avoid duplicating definitions. This amendment should be read together with amendments 4 and 5. In addition, the term ‘significant observed deviation’ should be defined in order to bring legal certainty to the applicability of the automatic correction mechanism as set out in Article 3(2)(b) of the proposed directive. See paragraphs 2.4.1 and 2.3.2 of the Opinion.

**Amendment 2**

**Article 3(1)(a) and (b) of the proposed directive**

‘1. Each Member State shall set up a framework of binding and permanent numerical fiscal rules which are specific to it, strengthen its responsible conduct of fiscal policy and effectively promote compliance with its obligations deriving from the TFEU in the area of budgetary policy over a multiannual horizon for the general government as a whole. That framework shall include in particular the following rules:

(a) a medium-term objective in terms of structural balance shall be set in order to ensure that the ratio of government debt to gross domestic product at market prices does not exceed the reference value set out in Article 1 of Protocol No 12 on the excessive deficit procedure or approaches it at a

‘1. Each Member State shall have in place set up a framework of binding and permanent numerical fiscal rules which are specific to it, strengthen its responsible conduct of fiscal policy and effectively promote compliance with its obligations deriving from the TFEU in the area of budgetary policy over a multiannual horizon for the general government as a whole. That framework shall include in particular the following rules:

(a) a medium-term objective in terms of structural balance shall be set in order to ensure that the ratio of government debt to gross domestic product at market prices does not exceed the reference value set out in Article 1 of Protocol (No 12) on the excessive deficit procedure or approaches it at a
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<td>satisfactory pace.</td>
<td>satisfactory pace. This medium-term objective shall be consistent with the requirements imposed by Article 2a of Council Regulation (EC) No 1466/97, in particular with the requirement that the budgetary position of the general government shall be close to balance or in surplus. This indicates that the medium-term objective shall not exceed the upper limit of the structural deficit of 0.5% of gross domestic product, which can become 1.0% of gross domestic product where the debt level is significantly below 60% of gross domestic product.</td>
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<td>(b) fiscal planning shall include a medium-term growth path of government expenditure net of discretionary revenue measures and consistent with the medium-term objective or the time-frame for convergence towards it. That path shall be set as soon as a new government takes office in the Member State, for the term of the legislature as established by the constitutional legal order of that Member State, and shall be respected by the annual budgets throughout that period.’</td>
<td>(b) fiscal planning shall include a medium-term growth path of government expenditure net of discretionary revenue measures and consistent with the medium-term objective or the time-frame for a rapid convergence towards it. The progress towards the medium-term objective shall be in line with the SGP. The corresponding expenditure path shall be set as soon as a new government takes office in the Member State, for the term of the legislature as established by the constitutional legal order of that Member State, and shall be respected by the annual budgets throughout that period. The expenditure growth targets may need to be adjusted in the light of updated macroeconomic developments and if deviations from the government expenditure path referred to in this paragraph need to be compensated for in accordance with point (b) of paragraph 2.’</td>
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**Explanation**

These amendments aim to align the provisions of the proposed directive with the provisions of the fiscal compact, with a view to enhancing legal clarity as to the interaction between the two. In particular, the fiscal compact imposes an obligation on Member States to have a budgetary position of the general government that is balanced or in surplus, and to have an upper limit of the structural deficit of 0.5% of the gross domestic product, except in cases where the debt level is significantly below 60% of gross domestic product.
domestic product and there are low risks to sustainability where the structural deficit does not exceed 1% of gross domestic product. In addition, the fiscal compact provides that progress towards the medium-term objective should be evaluated on the basis of an overall assessment with the structural balance as a reference, including an analysis of expenditure net of discretionary revenue measures, in line with the Stability and Growth Pact. However, these are not clearly reflected in the proposed directive. Therefore, by making explicit reference to the obligations contained under Council Regulation (EC) No 1466/97 and the Stability and Growth Pact, the obligations of the Member States in respect of the proposed directive are further clarified.

It is noted that the fiscal compact contains an upper limit of a structural deficit of 0.5% of gross domestic product, which is lower than that contained in Council Regulation (EC) No 1466/97, which is set at 1% of gross domestic product. If this needs to be aligned completely, Council Regulation (EC) No 1466/97 would need to be amended.

In addition, it is proposed that Member States should adjust their annual expenditure targets in the event of the economy developing differently from the assumptions made by the Member States when they set their multiannual expenditure targets, as well as if deviations from the government expenditure path referred to in this paragraph need to be compensated for in accordance with the correction mechanism introduced in the proposed directive.

See paragraphs 2.1.2, 2.2.1 and 2.2.3 of the Opinion.

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<th>Amendment 3</th>
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<td>Article 3(2)(b) of the proposed directive</td>
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‘(b) a correction mechanism shall be automatically activated in the event of a significant observed deviation from the medium-term objective or the adjustment path towards it. That mechanism shall include the obligation to implement measures to correct the deviation over a defined period of time and taking account of the nature and size of the deviation, in particular by compensating for deviations from the government expenditure path referred to in point (b) of paragraph 1.’

Explanation

The requirement to take into account the nature and size of a deviation is vague, and may result in correction measures that are very broad and lacking in substance. It is therefore proposed to change this...
provision by explaining the elements of the correction mechanism in an annex to the proposed directive. It is also proposed to implement the Common principles on national fiscal correction mechanisms\(^3\) into another annex to the proposed directive. See paragraph 2.3.2 of the Opinion.

<table>
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’4. Member States shall designate independent bodies for monitoring compliance with the provisions in paragraphs 1 and 2. The independent bodies shall provide public assessments to ascertain:

(a) adequacy of the medium-term objective under point (a) of paragraph 1 and of the government expenditure path referred to in point (b) of paragraph 1. That assessment shall take into account in particular the plausibility of the underlying macroeconomic forecast, the degree of specification of the planned government expenditure and revenue and the potential direct long-term positive budgetary effects of major structural reforms;

(b) compliance with the medium-term objective and the government expenditure path, including the existence of a serious risk of occurrence of a significant deviation from the medium-term objective or the adjustment path towards it;

(c) occurrence or cessation of any exceptional circumstances as referred to under paragraph 3.’

’4. The independent bodies designated by Member States pursuant to Article 5 of Regulation (EU) No 473/2013 shall be responsible for monitoring compliance with the provisions of paragraphs 1 and 2. Member States shall designate independent bodies for monitoring compliance with the provisions in paragraphs 1 and 2. The independent bodies shall provide public assessments to ascertain:

(a) adequacy of the medium-term objective under point (a) of paragraph 1 and of the government expenditure path referred to in point (b) of paragraph 1. That assessment shall take into account in particular the plausibility of the underlying macroeconomic forecast, the degree of specification of the planned government expenditure and revenue and the potential direct long-term positive budgetary effects of major structural reforms;

(b) compliance with the medium-term objective and the government expenditure path, including the existence of a serious risk of occurrence of a significant deviation from the medium-term objective or the adjustment path towards it;

(c) occurrence or cessation of any exceptional circumstances as referred to under paragraph 3.’

\(^3\) COM(2012) 342 final.
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<td>Regulation (EU) No 473/2013 already provides for independent bodies for the purposes of monitoring compliance with fiscal rules. It is therefore proposed to amend this provision in order to avoid a duplication of legal texts at Union level and to ensure legal clarity. See paragraph 2.4.1 of the Opinion.</td>
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<td>(a) are established by a statutory regime grounded in national laws, regulations or binding administrative provisions;</td>
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<td>(b) do not take instructions from the budgetary authorities of the Member State concerned or from any other public or private body;</td>
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<td>(c) have the capacity to communicate publicly in a timely manner;</td>
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<td>(d) are made up of members who are nominated and appointed on the basis of their experience and competence in public finances, macroeconomics and budgetary management, and by means of transparent procedures;</td>
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<td>(e) have adequate and stable own resources to carry out their mandate in an effective manner;</td>
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<td>The definition of ‘independent bodies’ in Regulation (EU) No 473/2013 already contains similar language to that set out in Article 3(7) of the proposed directive, with the exception of the last requirement on access to information. In order to avoid duplication of legal provisions, it is proposed to delete the other requirements and maintain only the requirement contained in point (f). See paragraph 2.4.1 of the Opinion.</td>
<td>The definition of ‘independent bodies’ in Regulation (EU) No 473/2013 already contains similar language to that set out in Article 3(7) of the proposed directive, with the exception of the last requirement on access to information. In order to avoid duplication of legal provisions, it is proposed to delete the other requirements and maintain only the requirement contained in point (f). See paragraph 2.4.1 of the Opinion.</td>
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