

harsh result for certain small insurance companies that have suffered losses. The proposed change provides relief for losses in those cases where the losses and deductions of prior years exceeded a company's reserves.

Insurance Policy Loan Interest

Loan Interest Paid in 1978 and Subsequent Years

Two changes are proposed relating to life insurance policy loans. The first relates to the deductibility of interest. A policy holder who uses the proceeds of a policy loan to earn income can deduct the interest he pays from his income for tax purposes. However, he must have the insurance company verify that such interest has not been added to the cost of the policy. A change is needed to ensure that such verification is made for loans taken before April 1, 1977 as well as after.

Loan Interest Paid Prior to 1978

The Income Tax Act also provides that all interest paid prior to 1978 is included in the cost basis of an insurance policy. Because the records needed to establish amounts paid in previous years frequently do not exist, a change is required to ignore this interest paid before 1978.

Loans to Shareholders

Amendments were made in 1977 to broaden the rules relating to the inclusion in income of certain loans by corporations to shareholders. An exception was provided for loans to an employee of a corporation where the funds were to be used to acquire shares of the corporation. A further technical amendment is to be made to provide a similar exception for loans made after March 31, 1977 to an employee to assist him in acquiring shares of a related corporation.

Northwest Territories

Effective in 1978, the Northwest Territories introduced its own income tax. Consequential changes are introduced in this budget to provide for a corresponding reduction of the federal tax. The changes ensure that the Northwest Territories is treated on the same basis as the provinces, which already impose their own taxes. This does not result in any change in the level of tax paid by individuals or corporations in the Northwest Territories.

Penalties

The Act will be changed to correct a technical deficiency in the wording of Section 163 that leaves some categories of unreported income outside the