Alberta Is Cutting Oil and Gas Taxes: Who Wins?

Description

On July 11, the Alberta government introduced two revised rules that reduce royalty rates on many oil and gas projects. According to the *Globe and Mail*, the new regulations aim to "encourage the energy sector to spend more on developments in their early stages and squeeze more oil and gas from underutilized existing operations."

If successful, the moves could have a substantial impact on the market. Alberta has the third-largest oil reserves in the world after of Venezuela and Saudi Arabia.

Which companies will benefit the most?

Suncor Energy Inc. (TSX:SU)(NYSE:SU)

A major developer of Alberta's oil sands, Suncor has a major presence in the Athabasca region, drilling in an area that potentially holds trillions of barrels of petroleum. Lately, Suncor has been going all in on oil sands.

In February the company announced that it would acquire Canadian Oil Sands Ltd. for $6.9 billion, including the assumption of $2.6 billion in debt. The buyout upped Suncor's stake in the Syncrude oil sands project to 48.7%. Then in April Suncor made another announcement that it would buy **Murphy Oil Corporation's** 5% Syncrude stake for $937 million.

The two acquisitions boosted Suncor's output by about 146,000 barrels a day. Suncor now holds a majority 53.7% position in the Syncrude project, the largest oil sands operation in the world.

Cenovus Energy Inc. (TSX:CVE)(NYSE:CVE)

Here is another company with major projects in the Athabasca sands region. Headquartered in Calgary, Cenovus owns half of Foster Creek and half of the Christina Lake reservoir, both of which are in eastern Alberta.

According to CEO Brian Ferguson, "even if Brent crude prices remain in the $40-per-barrel range through 2016, we believe we can continue to fund our sustaining capital program, growth projects that are nearing completion, and our current dividend level." Still, only 15% of production is hedged this year, allowing for significant swings in earnings based on changes in oil prices. Any break in royalty costs could help the company mitigate any future pricing impacts.

Not so fast

While the royalty tax breaks aim to ramp up oil and gas spending, other Albertan regulators are making it harder for companies to invest in the region.

Last month, the Alberta Energy Regulator opted to toughen rules that make it more difficult to complete mergers and acquisitions in the province. The new regulations set stricter standards on the financial strength an acquirer must have to execute a business deal. For example, companies seeking to buy oil and gas properties will need assets twice the size of its liabilities after the purchase is complete. Previously, assets only needed to equal liabilities.

According to *Reuters*, "More than 200 companies that met the prior standard were ruled out as buyers by the stricter financial solvency test, a move that industry reps say will limit the number of companies allowed to buy oil and gas assets."

Still, Suncor and Cenovus look good

For energy bulls, both of these companies are great picks to ride out the storm.

For every $10 increase in oil prices, Cenovus will see its cash flow increase by a whopping $620 million. That gives you massive upside to rising prices. Suncor, on the other hand, now controls 30% of Canada's total oil sands production capacity, making it a cash flow juggernaut if oil prices continue to climb.

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