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Ohio Supreme Court Declines to Recognize a Separate Implied Covenant to Explore Further

On January 3, 2018, in a 6–1 decision in the case of *Alford v. Collins–McGregor*, Slip Opinion No. 2018–Ohio–8, the Ohio Supreme Court answered a resounding **NO** to the question of whether Ohio recognizes a separate implied covenant to explore further. That is, when a lessee/operator is reasonably producing a shallow formation (e.g. the Gordon Sandstone formation) on a lease with no specific provisions regarding number of wells or formations to be produced, Ohio **does not** imply a further requirement on the lessee/operator to explore deeper formations (e.g. the Utica Shale).

Alford involved a 1980 lease that contained no specific provisions regarding the number of wells, the formations to be produced, and contained no express disclaimer of implied covenants. *Alford*, ¶¶ 4, 14. One well was drilled in 1981 into the Gordon Sand formation—a shallow formation. *Alford*, ¶ 5. This well has been productive from inception to present. No additional wells were drilled, nor was any exploration done into the deep formations such as the Utica or Marcellus Shale. *Id.* The landowners (the lessors of the 1981 lease), seeing activity in the Utica Shale on nearby property, sued claiming Collins–McGregor Operating Company (the lessee of the 1981 lease) breached the implied covenant of further exploration because it failed to explore deeper formations. *Alford*, ¶¶ 5, 6. As a remedy, the landowners sought termination of the lease as to these deep formations to allow them to lease (a “partial horizontal forfeiture” of the lease). *Alford*, ¶ 6. Collins–McGregor moved to dismiss the complaint and the trial court agreed, holding that the lease was valid per its plain terms. *Alford*, ¶ 8. The Fourth District Court of Appeals agreed, holding that Ohio law does not recognize partial horizontal forfeiture as an available form of relief. *Id.*

In affirming the Fourth District Court of Appeals, the Supreme Court of Ohio held that whether a lessee/operator must explore additional formations is subsumed by the implied covenant of reasonable development, which Ohio has long recognized. *Alford*, ¶¶ 17, 23.

Because this implied covenant better accounts for the overall circumstances, the interests of both the lessor and lessee, and overall profitability of development, there is simply no need to recognize a separate implied covenant of further exploration. *Alford*, ¶¶ 22, 23.

This decision serves as critical confirmation of the basic premise upon which millions of acres of deep leasehold rights have been acquired in eastern Ohio: that a well producing from a shallow formation generally holds the entire lease as to all depths. However, before a producer takes solace in the *Alford* decision, a thorough review of the terms of the lease at issue must be undertaken, as this case, like all cases dealing with lease interpretation, turn on the specific words used in the lease.

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