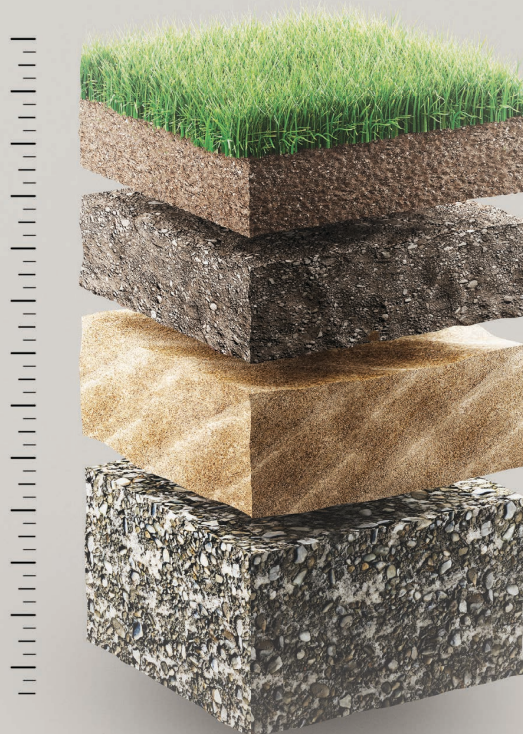


Expanding the Pugh Clause

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by/ **KIMBERLY A. WURTZ**

Is it time to expand the traditional Pugh clause? With the growing trend of horizontal drilling and use of hydraulic fracturing, oil and gas exploration is starting to impact land in various ways. Is the standard Pugh clause enough to protect the correlative rights of others, and is it time for the industry to consider a Pugh clause that encompasses more than “100 feet below the deepest producing formation” to fully enjoy the protections of the clause, whether it is statutory or not?

In 1947, Lawrence G. Pugh, a Louisiana lawyer, drafted an oil and gas lease, tailored with provisions to prevent the holding of nonpooled acreage.¹ The rationale behind such a provision was to bar lessees from keeping or holding acreage beyond the term of the lease if the acreage was not in fact producing. The exact terminology encompassed within the clause has varied throughout

the development of drilling, frequently altered to meet the needs of the parties. A common provision would either read as “this lease shall terminate as to all acreage not in a producing unit” or “this lease shall terminate as to all depths 100 feet below the deepest drilled formation.”²

Historically, the Pugh clause has commonly been added to oil and gas leases in an attempt to limit the rights of the lessee, permitting them to hold only particular depths or amounts of the leased acreage from which production is actually taking place. Generally, lessors want to incorporate the clause, while operators would prefer its absence, or at the most, the least restrictive version of the clause, permitting them to hold and explore the maximum amount of acreage.

With the use of the clause, the nonproducing land is essentially severed, based generally on defined criteria and

1 See “Pugh Clause” located at <https://www.mineralweb.com/owners-guide/lease-proposals/pugh-clause/>.

2 See Phillip E. Norvell, *Extending the Oil & Gas Lease into the Secondary Term on Outside Acreage by Production Within the Unit*, Annual of the Arkansas Natural Resources Law Institute (1981).

terms found within the clause. While generally used as part of the contract and determined through party negotiations, in some states, statutory Pugh clauses have been enacted. Oklahoma's statutory Pugh clause, 52 O.S. §87.1(b), states: "In case of a spacing unit of 160 acres or more, no oil and/or gas leasehold interest outside the spacing unit involved may be held by production from the spacing unit more than 90 days beyond expiration of the primary term of the lease." The Oklahoma statutory Pugh clause went into effect May 27, 1977, and requires that "acreage outside of a drilling and spacing unit be released if not developed"³ within 90 days.⁴

In states where no statutory provision is available, a contractual Pugh clause is commonly used by the mineral owner as a defense mechanism. But in today's drilling and development climate, and as the industry shifts, operators may also find unexpected protection from the use of a Pugh clause.

Areas in the Permian Basin of West Texas have shown signs of subsidence due to extensive development of the land resources. As drainage continues,⁵ the lands may continue to sink, causing concerns for the subsurface structures. If an existing formation is producing at a level that is causing the ground to sink, what happens to the land if lower formations are hydraulically fractured? Would adding deeper releases to the Pugh clause benefit all parties?

In recent cases in Oklahoma,⁶ where the hydraulic fracturing of a horizontal well allegedly damaged

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- 3 Joseph R. Dancy and Victoria A. Dancy, "Regulation of the Oil and Gas Industry by the Oklahoma Corporation Commission," *Tulsa Law Review*, Article 1 (Vol. 21, Issue 4) (Summer 1986).
- 4 See 52 O.S. §87.1(b).
- 5 Reference made to drainage in this context is not limited to the oil and gas resource only; drainage may also include removal of the groundwater supply.
- 6 See *H&S Equip. Inc. v. Devon Energy Prod.*, No. CIV-15-1244-HE, 2017 BL 470900 (W.D. Okla. Oct. 11, 2017). See also *Max Oil Company Inc. v. Range Production Company LLC*, 681 Fed. Appx. 710 (2017), and *Singer Oil Co. v. Newfield Exploration Mid-Continent Inc.*, No. CIV-16-768-M, 2017 BL 385976 (W.D. Okla. Oct. 27, 2017).

the existing vertical well above,⁷ operators may find themselves wishing the Pugh clause they are subjected to had put more distance between them and the subsequent operator.⁸ If a lease calls for the traditional “100 feet below the deepest producing formation,” maybe this purported damage is evidence that 100 feet is no longer enough. Would putting an additional 100 feet — or 200 feet total — prevent damage to the formations for all parties?

In the near future, operators and lessors alike may find themselves benefiting from a more expansive Pugh clause. In states that have statutory Pugh clauses as well as states that do not, legislatures and courts may also find themselves acting as the rope in a vicious game of tug of war between landowners and operators, as well as operators and subsequent operators. Regardless of what the future may hold, both lessors and operators can

address not only protections through a broadened Pugh clause, but also risks and impacts of subsidence, leaving all parties better off.

Perhaps when it comes to the Pugh clause, more is better than less. ▲

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7 Parent-child well interference occurs when there is a “fracture interference between existing production wells (parent wells) and newly fractured infill wells (child wells).” “Parent-Child Fracture Interference: Explanation and Mitigation of Child Well Underperformance,” located at <https://www.onepetro.org/conference-paper/SPE-189849-MS> (2018).
 8 It should be noted that the theories expressed in this article may also apply in the context of interference between one horizontal well and another, either laid down next to each other or stacked on top of each other.

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