

Locke Lord QuickStudy: The Texas Supreme Court Holds Interest Must Be Simple Absent an Express, Clear, and Specific Provision for Compounding

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The Texas Supreme Court has clarified Texas law concerning how to calculate interest that is being paid pursuant to an agreement or statute. *Samson Exploration, LLC v. Bordages*, No. 22-0215, 2024 WL 2869049 (Tex. June 7, 2024). A requirement for compounding cannot be implied. Instead, “because Texas law disfavors compound interest, an agreement for interest on unpaid amounts is an agreement for simple interest absent an express, clear, and specific provision for compound interest.”

Background

The agreement at issue was an oil and gas lease that specified, all “past due royalties ... shall be subject to a Late Charge...” The late charges were “based on the amount due” and “calculated at the maximum rate allowed by law.” The late charge was payable on the last day of the month. The plaintiffs asserted that, when the late charge was not paid at the end of the month, it triggered another late charge on both the past due royalties and the past due late charge. All parties agreed that the late charges were a form of interest and that the applicable rate was 18%. The plaintiffs’ arguments called for monthly compounding. Samson argued that the interest should be measured by a simple, non-compounding, formula.

Texas Law Disfavors Compound Interest

The Texas Supreme Court held that “the default rule in Texas is that simple interest applies in the absence of an express stipulation—with clear and specific language—to a compound rate of interest.” The Court traced interest laws from antiquity to the modern day, noting compounding was forbidden for millennia and remains disfavored. Exceptions are rare. A line of authority from Texas courts in the nineteenth century confused the issue by suggesting that temporal language such as “per annum” or “annually” could suffice as an express stipulation for compounding. As the Court noted, that language is commonly used even when describing simple interest. The Court disapproved of that line of authority.

The Court chose not to provide a particular formula or magic words that would call for compounding. It specified, instead, what would *not* call for compounding. A mere temporal reference, such as “per annum” is insufficient. Likewise, a periodic rest, such as a due date for paying interest, does not meet the specificity requirement for

compounding. If, however, the agreement uses the word “compounded” along with a periodic rest, it would be sufficiently clear to require compound interest.

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