

Booklet 03

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# Revenue Framework: Royalties, DMF, NMEDT & Mineral Exchanges

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# Revenue Framework: Royalties, DMF, NMEDT & Mineral Exchanges

Royalty Computation, Second Schedule Rates, District Mineral Foundation, NMEDT, Dead Rent and Mineral Exchanges

*Booklet III of VI — Indian Mining Sector Legal Series*

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## CHAPTER ONE

# Royalty: Legal Character, Computation and Payment

*Nature of Royalty Under the MMDR Act, Second Schedule Rates, ASP Methodology, Payment Procedure and Disputes*

*Royalty is the centrepiece of India's mining revenue framework — the financial consideration paid by the mining lessee to the state government (on behalf of the mineral owner, which is typically the state) for the extraction and removal of minerals from the leased area. The legal character, computation methodology, and payment procedures for royalty generate more mining sector litigation than any other financial obligation.*

## 1.1 Legal Character of Royalty: Tax or Contract Payment?

The legal character of mining royalty in India — whether it constitutes a "tax" subject to constitutional constraints on taxation, a "price" for the mineral resource (analogous to a contractual payment for goods), or a regulatory levy sui generis — has been a contested question in Indian constitutional law for decades. The distinction matters commercially because: if royalty is a tax, it must be imposed by law and only by the legislature (Article 265 of the Constitution — no tax shall be levied or collected except by authority of law); if it is a price or fee

for services, it can be fixed by executive order within the parameters of the enabling statute; and if it is a regulatory levy, it must bear a rational nexus to the regulatory purpose and cannot be purely revenue-generating. The Supreme Court's decision in *India Cement Ltd. v. State of Tamil Nadu* (1990) characterised royalty as a "tax" for the purpose of determining whether states could impose an additional state-level cess on top of the MMDR Act's royalty — holding that since royalty was a tax, and since Parliament had "occupied the field" of royalty under Entry 54, states could not impose a separate cess that effectively doubled the mining tax burden. However, the *MADA v. SAIL* nine-judge bench decision of 2024 significantly qualified this characterisation, distinguishing between royalty (which remains Parliament's domain under Entry 54) and taxes on mineral-bearing land (which remain the states' domain under Entry 49), effectively creating space for state governments to impose land taxes on mining that are distinct from the MMDR Act's royalty framework.

The Second Schedule to the MMDR Act specifies the royalty rates for all major minerals, expressed either as a percentage of the "average sale price" (ASP) of the mineral or as a fixed amount per unit of quantity extracted. The ASP-based royalty system — under which royalty is computed as a percentage of the average price at which the mineral is sold by the lessee in the relevant month — ensures that royalty revenue tracks the commodity price cycle: when mineral prices are high, state royalty revenue increases automatically without requiring legislative amendment, and when prices fall, the royalty burden decreases proportionately, providing natural stabilisers for mining project economics. The royalty rates in the Second Schedule are periodically revised by the Central Government through gazette notification — revisions typically occur every three to four years, with rates generally increased in line with inflation and improving commodity market conditions. The states do not have independent authority to vary royalty rates above the Second Schedule maximum — royalty rates are centrally fixed, and a state government that wishes higher effective royalty must rely on the bid premium mechanism of the auction process rather than on unilateral rate enhancement. The Second Schedule rates are: iron ore 15% ASP; manganese ore 7.5% ASP; limestone 10% ASP; bauxite 0.5% per tonne (fixed); copper ore 4.2% of London Metal Exchange (LME) price; chromite 13% ASP; diamonds 11.5% ASP; gold 4% ASP; rock phosphate 16% ASP; and similar rates for other specified minerals.

## **1.2 Average Sale Price: Computation and Disputes**

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The Average Sale Price (ASP) is the foundation of royalty computation for ASP-based minerals, and its computation methodology is the most frequently disputed aspect of royalty compliance. MMDR Rule 64A and the MCDR 2017 specify that the ASP for a mineral in a given month is the weighted average of all sale prices realised by the lessee for the mineral dispatched from the mine in that month, computed as the total revenue from mineral sales divided by the total quantity sold. The critical questions in ASP computation disputes include: what components of

the realised price should be included in "sale price" for ASP purposes (whether freight, handling charges, and beneficiation costs that are charged to buyers should be included or excluded); what price is applicable for captive transfers (where the mineral is transferred to the lessee's own downstream processing plant at a transfer price that may differ from the arm's length market price); and what reference price applies when a portion of the mineral production is sold at prices below the applicable state government's benchmark price (a price floor below which royalty must be paid even if actual sale prices are lower). The IBM periodically issues Show Cause Notices to mining lessees for apparent shortfalls in royalty payments, typically arising from disputes about ASP methodology — and the adjudication of these disputes occupies significant administrative and judicial resources in the states with major mining operations.

### **1.3 Royalty Payment Procedure**

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Royalty is payable monthly by the mining lessee through a self-assessment system: the lessee prepares a monthly Royalty Return specifying the quantity of mineral dispatched in the month, the applicable ASP, the royalty rate, and the royalty amount due; and remits the computed royalty to the state government's account within the prescribed period (typically by the 15th of the following month for the previous month's dispatches). The state government's Mining Department reviews the Royalty Returns and cross-checks the declared quantities against the production and dispatch records, the Weighbridge or truck count records at the mine gate, and the e-way bill and GST data for mineral dispatches. Where the Mining Department finds discrepancies between the declared royalty and the assessed royalty, it issues a demand notice for the balance amount with interest at the prescribed rate. Persistent or substantial royalty evasion — including under-reporting of production quantities, manipulation of dispatch records, or false claims about mineral quality that lower the applicable ASP — constitutes an offence under Section 21 of the MMDR Act and is a ground for ML termination under Section 4A. The introduction of digital mining surveillance systems — including GPS tracking of dump trucks, CCTV at mine gates, and integration of mine production data with the National Mining Regulation and Monitoring System (NMRMS) — has significantly improved the state governments' ability to detect and deter royalty evasion, though evasion remains a problem in some states with weak enforcement capacity.

# District Mineral Foundation: Trust Structure and PMKKKY

*Section 9B, DMF Trust Framework, PMKKKY Expenditure Guidelines, Governance and Beneficiary Communities*

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## 2.1 DMF: Statutory Framework and Trust Structure

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The District Mineral Foundation (DMF), established under Section 9B of the MMDR Act (inserted by the 2015 Amendment), is a statutory trust created in every district where mining operations are conducted, with the mandate to work for the interests and benefit of persons affected by mining-related operations. The DMF is constituted as a non-profit trust by the state government for each mining district, with a Governing Council (chaired by the District Collector or a senior state government official) responsible for the overall oversight of the DMF's activities, and a Management Committee responsible for the day-to-day administration. The DMF's corpus is built from mandatory contributions by mining lessees — 10% of the royalty payable for concessions granted after 12 January 2015 (post-2015 leases), and 30% of the royalty payable for pre-2015 legacy leases — the higher rate for legacy leases reflecting the government's recognition that these lessees had historically benefited from below-market concession terms and should therefore contribute more to community benefit. The DMF's aggregate national corpus has grown substantially since the 2015 Amendment: as of financial year 2022-23, total DMF contributions nationwide exceeded Rs. 6,000 crore annually, with Odisha (a major iron ore and coal mining state) having one of the largest individual DMF balances. The scale of the DMF corpus creates both significant opportunity (for meaningful community development investment) and significant accountability risk (for misuse or misallocation of funds) — and the governance quality of individual district DMFs has been uneven, with CAG audits identifying deficiencies in project selection, fund utilisation, and outcome monitoring in several states.

The Pradhan Mantri Khanij Kshetra Kalyan Yojana (PMKKKY), notified by the Ministry of Mines in 2015, provides the operational framework for the DMF's expenditure. PMKKKY specifies that DMF funds must be applied exclusively in mining-affected areas for: high-priority areas — drinking water supply, environment, health care, education, welfare of women, and elderly persons (60% of DMF funds); and other priority areas — physical infrastructure, irrigation, energy and watershed development, skill development, and environmental quality (40% of DMF funds). The DMF's expenditure must comply with PMKKKY guidelines and the specific state DMF rules framed by each state government, and must not be diverted to non-mining-related purposes or to areas outside the designated mining-affected zone. Despite the PMKKKY framework's clear mandate, the DMF's actual expenditure record has been mixed — substantial

proportions of DMF balances in several states remain unspent years after the funds were received, reflecting weaknesses in project identification, tendering, and implementation capacity at the district level. Civil society organisations and the CAG have repeatedly pointed to the under-utilisation of DMF funds as a governance failure that is denying communities affected by mining the benefits that the MMDR Act intended them to receive.

## **2.2 Affected Persons and Benefit Identification**

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The MMDR Act's definition of "persons affected by mining-related operations" — the target beneficiaries of the DMF — encompasses a broad spectrum of communities including: persons whose land is within the leased area; persons within a specified distance of the mining lease boundary; persons whose livelihoods are dependent on the land or water resources within or near the lease area; and displaced persons who have been resettled on account of the mine. The geographic definition of the "mining-affected area" — within which DMF benefits must be concentrated — is specified in the state DMF rules and typically includes all villages within a radius of 0 to 25 km from the lease boundary, with the PMKKKY guidelines creating a priority structure that targets the most immediately affected communities (those within the lease area and its immediate periphery) for the highest proportion of DMF expenditure. For practitioners advising mining companies on their DMF obligations, the key compliance questions are: whether the DMF contributions are being computed on the correct royalty base (avoiding under-computation arising from disputed royalty assessments); whether the company has any statutory obligations to participate in the DMF's governance processes; and whether there are any legal risks arising from the state government's DMF expenditure decisions that could affect the company's licence to operate (for instance, if DMF funds are directed to address grievances that also provide the basis for anti-mining agitation or writ petitions challenging the ML).

## **2.3 DMF Contribution Disputes**

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Mining lessees have disputed DMF contribution obligations on several legal grounds: that the MMDR Act's DMF contribution mechanism is effectively a tax on mining (rather than a regulatory charge), which requires it to be imposed by Parliament rather than by executive order, and which is not constitutionally permissible as an additional burden on mining beyond the royalty rate fixed by Parliament; that the DMF contribution rate (particularly the 30% rate for pre-2015 leases) is disproportionately high relative to the regulatory purpose of community benefit, and constitutes an unreasonable condition that transforms the mining concession from an economically viable project to an unviable burden; and that the DMF contribution obligation for pre-2015 leases was not part of the original concession terms and constitutes an impermissible alteration of vested contractual rights. The Supreme Court has generally upheld the constitutional validity of the DMF mechanism and the 30% contribution rate for pre-2015 leases, recognising that the retrospective application of higher DMF rates to legacy leases is a policy choice within Parliament's legislative competence under Entry 54 — and that the mining

industry's previous under-contribution to community benefit justifies the higher rate as a corrective policy measure rather than a punitive imposition.

# National Mineral Exploration Trust and Exploration Financing

*NMET Purpose, Contribution Rate, Project Portfolio, GSI-MECL Interface and Exploration Investment Framework*

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## 3.1 NMET: Statutory Basis and Funding

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The National Mineral Exploration Trust (NMET), established under Section 9C of the MMDR Act (inserted by the 2015 Amendment), receives mandatory contributions of 2% of the royalty payable by all major mineral mining lessees and applies these funds for the development of India's mineral exploration infrastructure and the promotion of regional mineral exploration. The rationale for the NMET mechanism is that India's mineral exploration investment has historically been grossly inadequate relative to the country's geological endowment — with the GSI's long-term geological mapping programme chronically under-funded and the private sector's willingness to invest in speculative mineral exploration limited by the absence of a clear route from exploration discovery to development rights. The NMET's 2% royalty contribution creates a dedicated, self-replenishing fund that grows with the mining sector's production — in a Rs. 30,000 crore annual royalty payment environment, the NMET receives approximately Rs. 600 crore annually. NMET funds are deployed through the Ministry of Mines to agencies including the GSI, MECL, state geological departments, and private sector exploration companies under competitive grant arrangements, for detailed geological mapping, geophysical surveys, deep drilling programmes, and mineral resource assessment in designated areas of high geological prospectivity. The NMET's project portfolio is intended to increase the "drill-ready" mineral blocks available for auction — blocks with sufficient geological data (resource estimates, drill hole data, metallurgical characterisation) to enable informed bidding — thereby improving the competitiveness and revenue performance of subsequent mineral block auctions.

## 3.2 Private Sector Mineral Exploration

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Beyond the state-funded exploration conducted by GSI and MECL using NMET and government budget resources, private sector mineral exploration in India operates through the Composite Licence mechanism (under which private explorers can bid for CL blocks and conduct their own exploration) and through the reconnaissance permit system (which allows registered exploration companies to conduct remote sensing and surface geological surveys over large areas without conducting drilling, to identify priority targets for subsequent CL applications). The private sector exploration ecosystem in India has historically been limited, reflecting: the absence of a secure route from exploration discovery to development rights under the pre-2015 first-come-first-served system (which made exploration investment risky, since a successful explorer could

be displaced by a competing applicant in the discretionary ML grant process); the lack of a developed mining capital market (such as the TSX Venture Exchange in Canada or the ASX in Australia) that provides exploration financing for junior mining companies; and the geological complexity of India's mineral-bearing terrains, which require sophisticated exploration technology that is concentrated in a few global exploration companies. The 2015 Amendment's CL mechanism — and the NMET's gradual improvement of India's pre-competitive geological data base — are intended to attract more private exploration investment by providing the combination of improved geological data (reducing exploration risk) and guaranteed development rights (reducing the commercial risk that exploration success benefits a different party).

# Mineral Exchanges and Market Infrastructure

*Mineral Exchange Framework, MSTC, Price Discovery, Forward Contracts and Mineral Market Governance*

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## 4.1 Mineral Exchange Framework

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India's mineral exchange framework — providing organised platforms for price discovery and trading of major minerals — has been progressively developed since the MMDR Act's 2021 Amendment encouraged the establishment of mineral exchanges to improve market transparency and price efficiency. The National Mineral Policy 2019 identified the development of a robust mineral exchange as a policy priority, recognising that the absence of transparent market pricing for major minerals (particularly iron ore, bauxite, and manganese ore) creates inefficiencies in the royalty computation system (where ASP disputes reflect the lack of a universally accepted market price reference) and prevents the development of financial risk management tools (hedging instruments, forward contracts) that mining companies and downstream users could use to manage commodity price risk. MSTC Limited's metal and mineral exchange operations — initially focused on facilitating mineral block auctions and now expanding to include spot trading of major minerals — provide an electronic platform for buyers and sellers of major minerals to transact at transparent, market-determined prices, with MSTC providing the matching, settlement, and dispute resolution infrastructure. The Mineral Auction Rules provide the regulatory framework for exchange-based trading of auctioned minerals, and the Ministry of Mines is working on comprehensive mineral exchange regulations that will specify the eligible commodities, participant categories, price discovery mechanisms, settlement procedures, and regulatory oversight arrangements for a full-scale organised mineral exchange.

## 4.2 Iron Ore Price Benchmarking

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Iron ore — India's highest-value major mineral in terms of production and royalty revenue — has been the focus of the most active discussion about mineral exchange price benchmarking, given the significant royalty revenue implications of the ASP at which royalty is calculated. State governments with major iron ore production (Odisha, Jharkhand, Chhattisgarh, Goa) have periodically attempted to establish state-level benchmark prices for iron ore that set a floor for ASP computation — ensuring that royalty is paid at market-representative prices even where individual sale transactions may be at negotiated prices below the benchmark. The interaction between state benchmark prices, the national and international iron ore market prices (referenced through indices such as the Platts IODEX or the NMDC published prices), and the actual transaction prices in individual sale contracts has been a persistent source of disputes between mining companies and state royalty authorities. The development of a transparent, universally recognised mineral exchange price for Indian iron ore — based on actual market

transactions at a defined quality specification — would resolve many of these benchmark price disputes by providing an objective reference that neither the state government nor the mining company could manipulate. The challenge of establishing such a benchmark is that Indian iron ore is heterogeneous in quality (with widely varying grades, sizes, and alumina content) and is sold in both domestic and export markets at prices that reflect these quality differences — requiring the development of a multi-grade, multi-market price framework rather than a simple single-price benchmark.

# Dead Rent, Surface Rent and Other Financial Obligations

*Dead Rent Rates, Surface Rent, Stamp Duty on ML Deeds, GST on Mining Activities and Financial Compliance*

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## 5.1 Dead Rent

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Dead Rent — specified in the Second Schedule to the MMDR Act — is a minimum area-based payment that every mining lessee must pay to the state government regardless of whether any mineral is actually extracted in a given period. Dead Rent is calculated on the area of the mining lease (in hectares) at rates specified in the Second Schedule, which vary by mineral and are structured on a tiered basis (higher rates per hectare for larger lease areas). The primary commercial function of Dead Rent is to prevent lessees from "parking" mining leases — holding concessions in perpetuity without developing them — by imposing a financial carrying cost that escalates with the unproductive period. In periods where the mine is in production, the lessee pays whichever is higher — the Dead Rent or the royalty — so Dead Rent effectively provides a minimum revenue floor for the state government even when mine production is low or zero. For prospective mining investors, the Dead Rent obligation must be modelled carefully in the pre-production period (from ML grant through the regulatory clearance and construction phases to first production) — this period can extend to 3–7 years for large mining projects, during which Dead Rent accrues on the full lease area as a non-revenue-generating cost. The Dead Rent liability in the pre-production period is one of the financial planning parameters that mining project finance lenders examine closely when assessing the project's viability.

## 5.2 GST on Mining Activities

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The Goods and Services Tax (GST) applies to mining activities through multiple channels, each with distinct compliance implications. Royalty payments by mining lessees to state governments are subject to GST under the Reverse Charge Mechanism (RCM): the mining lessee (the recipient of the mining service, which is the state government's provision of extraction rights) is required to pay GST on the royalty amount at the applicable rate (currently 18% IGST for most major minerals) under RCM, and can claim ITC for this GST payment against its output tax liability on mineral sales. The DMF and NMET contributions are also subject to GST under RCM, applying the same rate as royalty to these statutory levies. The extraction and sale of minerals attracts GST at 5% (for most minor minerals and marble/granite blocks) or 18% (for coal and other specified minerals) on the sale price; and mining services provided by contractors to mining companies (blasting, drilling, overburden removal, ore transportation within the mine) attract GST at 18%. For mining companies, the total GST burden (on royalty, DMF, NMET, and

mining services) represents a significant working capital outlay that must be managed through efficient ITC utilisation — ensuring that the GST paid on inputs and statutory levies is credited against the output GST collected on mineral sales within the minimum possible time to avoid cash flow pressure.

**Booklet III Key Takeaways:** India's mining revenue framework — comprising royalty (computed on ASP at Second Schedule rates), bid premium (committed in the auction), Dead Rent (area-based minimum payment), DMF contribution (10% or 30% of royalty), and NMET contribution (2% of royalty) — creates a layered financial obligation structure that must be carefully modelled in mining project financial analysis. Royalty disputes (ASP methodology, captive price, benchmark price) are the most active area of mining sector litigation. The DMF's Rs. 6,000+ crore annual corpus is a significant community development resource that is under-utilised due to governance weaknesses at the district level. NMET's 2% royalty contribution funds critical exploration infrastructure. The mineral exchange framework, while still developing, will eventually provide the price discovery infrastructure needed to reduce royalty disputes and enable sophisticated financial risk management for the sector.

## Revenue Framework: Advanced Issues

*Royalty Litigation Strategy, DMF Governance Reforms, NMET Portfolio Analysis, Mineral Taxation Post-MADA and GST Compliance*

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### C.1 Royalty Litigation: Strategic Considerations

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Royalty disputes between mining lessees and state governments are endemic in the Indian mining sector — virtually every large mining operation is simultaneously managing a portfolio of royalty demand notices at various stages of adjudication before the state Mining Department, the state Mines Tribunal (where constituted), and the High Court. The strategic management of royalty litigation requires: a comprehensive audit of all pending royalty demands (identifying the legal issues at stake, the quantum involved, and the strength of the lessee's position on each demand); prioritisation of disputes for active contest versus those for negotiated settlement (balancing litigation cost and management distraction against the financial exposure and precedent implications of each demand); proactive engagement with ASP methodology disputes (where the core legal question of what should be included in "sale price" remains unsettled across states, creating opportunities for consistent across-the-board interpretation that reduces the lessee's aggregate liability); and participation in the Mining Tribunal or High Court proceedings to establish binding precedents on ASP methodology questions that resolve the underlying uncertainty rather than merely contesting individual demand notices. In states where royalty disputes are most acute (Odisha, Jharkhand, and Goa for iron ore; Rajasthan for cement-grade limestone and marble; Chhattisgarh for iron ore and dolomite), mining companies with large royalty exposure should consider engaging with the state government at the policy level — through industry associations such as the Federation of Indian Mineral Industries (FIMI) and state mining industry associations — to seek gazette clarification of the disputed ASP methodology issues rather than pursuing case-by-case litigation that creates adversarial dynamics without resolving the underlying legal uncertainty.

### C.2 DMF Governance: Accountability Mechanisms

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The DMF's governance quality — which directly determines whether the significant funds collected from mining companies are actually deployed for the benefit of mining-affected communities or diverted to non-priority uses or wasted on poorly planned projects — is one of the most important public interest issues in the Indian mining sector. Several mechanisms have been proposed or implemented to improve DMF governance: the Ministry of Mines' establishment of the National DMF Portal (which provides public visibility of each district DMF's receipts, allocations, and project expenditure data); the Ministry's annual DMF performance rankings (which publicly grade each district DMF based on utilisation rate, project quality, and

outcome data, creating reputational pressure on underperforming districts); mandatory social audits by beneficiary communities (required under the PMKKKY guidelines to verify that DMF-funded projects are being implemented as approved and are delivering the stated benefits); and CAG performance audits of specific state DMF frameworks (which have identified specific weaknesses in project selection, fund utilisation, and outcome measurement and have recommended governance reforms). For mining companies whose DMF contributions fund the DMF — and whose "social licence to operate" in mining-affected communities depends in part on whether the DMF is seen to be delivering tangible benefits — proactive engagement with the DMF governance process (participating in DMF Governing Council meetings where invited, providing technical inputs for project selection in mining infrastructure, and supporting DMF transparency initiatives) serves both compliance and stakeholder relationship objectives.

### **C.3 Post-MADA Taxation: Planning Implications**

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The MADA v. SAIL nine-judge bench ruling's validation of state authority to impose taxes on mineral-bearing land under Entry 49 of List II has fundamental implications for the financial planning and project economics of mining operations across India. In the immediate aftermath of the ruling, several state governments have announced their intention to review and potentially increase their existing mineral-bearing land taxes or to introduce new levies — creating an uncertain financial landscape that mining project investors and lenders must account for in their financial models. The key questions for mining project financial planning in the post-MADA environment are: which existing state cesses and levies on mining are now clearly constitutional (and at what quantum); what additional taxes are states likely to introduce in response to the ruling's empowering effect; how do these taxes interact with the royalty, bid premium, and DMF/NMET obligations already factored into the financial model; and what is the aggregate effective tax rate on mineral extraction after all applicable taxes and levies are considered? Legal practitioners advising mining sector investors in the post-MADA environment must provide integrated advice that covers not just the MMDR Act's royalty framework but the complete state-specific taxation landscape applicable to each mining operation — including mineral-bearing land taxes, mineral transport levies, and any new taxes announced in state budgets following the MADA ruling.

**Booklet III — Complete Summary:** India's mining revenue framework creates a multi-layered financial obligation structure that extends far beyond the headline royalty rate to encompass bid premiums, dead rent, DMF contributions, NMET contributions, surface rent, and (following MADA v. SAIL) potential state mineral-bearing land taxes. The ASP methodology for royalty computation is the most litigated aspect of mining financial compliance. DMF governance quality — which determines whether community benefit obligations translate into real community development — remains uneven and requires active monitoring. NMET's exploration investment programme is gradually improving the geological data base that supports competitive mineral

block auctions. Post-MADA, comprehensive state-specific mining taxation analysis is an essential input to mining project financial modelling.