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SUPREME COURT ON MINING ROYALTY

On July 25, 2024, the Supreme Court ("**SC**"), in the *Mineral Area Development Authority* case[1] held that royalty does not fulfil the characteristics of tax or impost and hence overturned its own observation in the *India Cement* case[2] ("***Cement*** **Case**") to the effect that royalty is a tax is incorrect.

Brief Facts

Mines and mineral development regulation is covered under both the Union List (Entry 54, List I) and the State List (Entry 23, List II) of the Seventh Schedule of the Constitution of India ("**Constitution**").
The state legislature's authority under Entry 23 of List II is subject to the provisions of Entry 54 of List I.
The Parliament enacted the Mines and Minerals (Development and Regulation) Act, 1957 ("**MMDR Act**") under Article 246 of the Constitution, which serves as a comprehensive code for regulating mines and mineral development, including the requirement for mining leaseholders to pay royalties.
In the *Cement* Case, a seven-Judge Bench of the SC had held that royalty is a tax and that states cannot impose taxes on mineral rights, as they are governed by the MMDR Act.
In the *Kesoram Industries* case[3] ("***Kesoram*** **case**"), a Constitution Bench of the SC later clarified that royalty is not a tax, allowing state legislatures to impose taxes on mineral-bearing lands, using mineral value or royalty as the measure.
The constitutional validity of such state-imposed taxes was challenged in various high courts, with the Patna High Court ruling that such taxes were beyond the legislative competence of the state.
The SC noted the conflicting decisions between the *Cement* case and the *Kesoram* case and had referred the matter to a nine-judge bench for resolution.

SC's Judgement and Reasoning

The SC observed:
Section 9 of the MMDR Act mandates that holder of a mining lease is liable to pay royalty in respect of any mineral removed or consumed by him or by his agent, manager, employee, contractor or sub-lessee from the leased area at the rate specified in the Second Schedule of the MMDR Act.
The rates of royalty payable in respect of minerals in the Second Schedule are computed either on an *ad valorem* basis at a specified percentage of the average sale price or at specific rates on per tonnage basis.

It differentiated between royalty and tax by stating that:
Royalty is generally understood as compensation paid for rights and privileges enjoyed by the grantee whereas taxation is a mode of raising revenue to fund public expenditure.
The essential characteristics of royalty are that: *"(i) it is a consideration or payment made to the proprietor of minerals, either the government or a private person; (ii) it flows from a statutory agreement (a mining lease) between the lessor and the lessee; (iii) it represents a return for the grant of a privilege (to the lessee) of removing or consuming the minerals; and (iv) it is generally determined on the basis of the quantity of the minerals removed.*"[4]

[1] *Mineral Area Development Authority and Anr. v. Steel Authority of India and Anr.*, 2024 SCC OnLine SC 1796.
[2] *India Cement Ltd. v. State of T.N.*, (1990) 1 SCC 12.
[3] *State of West Bengal v. Kesoram Industries Ltd.*, (2004) 10 SCC 201.
[4] Paragraph 98 of the Judgement.

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The essential characteristics of tax are: *"(i) it is a compulsory exaction of money by a public authority; (ii) it is imposed under statutory power without the consent of the tax payer; (iii) the demand is enforceable by law; (iv) it is an imposition made for public purposes to meet the general expenses of the state without reference to any special benefit to be conferred on the payer of the tax; and (v) it is part of the common burden*."[5]

The SC overturned its judgement in the *Cement* case, upheld the *Kesoram* case and opined that: "*On first principles, royalty is a consideration paid by a mining lessee to the lessor for enjoyment of mineral rights and to compensate for the loss of value of minerals suffered by the owner of the minerals. The marginal note to Section 9 states that royalties are "in respect of mining leases." The liability to pay royalty arises out of the contractual conditions of the mining lease. A failure of the lessee to pay royalty is considered to be a breach of the terms of the contract, allowing the lessor to determine the lease and initiate proceedings for recovery against the lessee.*"[6]

It also clarified that, "*There are major conceptual differences between royalty and a tax : (i) the proprietor charges royalty as a consideration for parting with the right to win minerals, while a tax is an imposition of a sovereign; (ii) royalty is paid in consideration of doing a particular action, that is, extracting minerals from the soil, while tax is generally levied with respect to a taxable event determined by law; and (iii) royalty generally flows from the lease deed as compared to tax which is imposed by authority of law.*"[7]

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[5] Paragraph 104 of the Judgement.
[6] Paragraph 123 of the Judgement.
[7] Paragraph 126 of the Judgement.