

SHARE TRANSFER  
RESTRAINTS IN THE  
ARTICLES OF ASSOCIATION  
UNDER TURKISH LAW

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In Turkish law, the articles of association is an agreement prepared in accordance with the principles and mandatory provisions regulating joint stock companies set forth in the Turkish Commercial Code (“TCC”) and signed by the founders to incorporate a joint stock company. Pursuant to the TCC, the internal organization, powers and duties of the branches and rights and responsibilities attached to the ownership of shares shall be stated in the articles of association. Provisions included in the articles of association in accordance with the principles and mandatory provisions of the TCC, called real provisions, bind not only the founders who signed the articles of association but also the existing and future shareholders as well as the company and its branches. However, the articles of association may also include provisions the regulation of which the TCC does not require. These provisions are not considered mandatory provisions of the articles of association; therefore, rights arising out of these provisions will not bind the company, its branches or the existing and future shareholders, therefore, they cannot be enforced by the instrumentalities set forth in the TCC even though such provisions are included in the articles of association. Such provisions only create contractual obligations and bind the parties who have consented to their terms under the Code of Obligations.

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#### LEGAL STATUS OF SHAREHOLDERS’ AGREEMENTS AND THEIR RELATIONSHIP WITH THE ARTICLES OF ASSOCIATION

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Pursuant to Article 405 of the TCC, with some exceptions, the only obligation of the shareholders can be the capital contribution undertaken by the respective shareholder to the company and this obligation is limited to the amount of capital that each shareholder has undertaken to contribute. Under this principle, shareholders are not obliged to pay any amount other than their capital contribution and also, they cannot be instructed how to exercise their rights arising from their ownership of the shares, even by the articles of association. For this reason, shareholders who wish to bind each other with different types of commitments or set up a system in which they wish the company to operate have to do so by entering into shareholders’ agreements. Shareholders’ agreements are contracts concluded by and between shareholders in accordance with the principles of the Code of Obligations. Under the principle of freedom of contract set forth in the Code of Obligations, issues that cannot be handled within the articles of association, such as, inter alia, personal representations and undertakings of the shareholders towards each other, performance of the company, contractual penalties, voting arrangements, and share sale and/or purchase obligations, may be regulated in a shareholders’ agreement. However, since the obligations arising from shareholders’ agreements are contractual in

nature, those obligations will only bind the parties to such agreements and the remedies which can be imposed in case of breach will be the ones provided under the Code of Obligations.

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## LINKAGE SYSTEM

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Pursuant to Article 461/1 of the TCC, unless otherwise provided for in the articles of association, registered shares shall be transferred to the other shareholders or third parties without being subject to any restriction. Under the TCC, the transfer of registered shares can be prohibited or restricted by setting up a linkage system (bağlam sistemi) in the articles of association. The linkage system targets the balance between the needs for the transfer of shares unrestrainedly and the protection of the company. If a linkage system is provided for in the articles of association, the company shall have the obligation or discretion to refuse to register the transfer of linked registered shares (bağlı nama yazılı hisse senetleri) to the share ledger of the company with no reason, if stated thusly in the articles of association or for the reasons listed in the articles of association. Since rights arising out of the ownership of shares such as voting can only be used by the shareholders who are listed as such in the share ledger of the company, this refusal will not affect the validity of transfer but the title of the shares shall remain with the existing shareholder while the ownership rights are transferred to the other party, unless otherwise provided for in the agreement.

As mentioned earlier, shareholders may enter into shareholders' agreements with other shareholders and undertake obligations other than their obligation to pay their capital contribution. Such undertakings may include a right of first option (öncelik hakkı), pre-emption rights (önalım hakkı) or put or call options (alım ve satım hakları). If those rights are envisaged in a shareholders' agreement, they will only be asserted and enforced against the other parties to the agreement. The unavailability of enforcement for such rights against the company and its branches may interrupt the shareholders' main purpose in granting such rights. For this reason, shareholders may try to have the company adopt the provisions of their shareholders' agreement into the articles of association in order to provide for enforcement by the instrumentalities set forth under the TCC. Before examining the validity of such rights when listed in the articles of association, we will give information with respect to their characteristics below.

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## FIRST OPTION

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According to the first option right, if a shareholder wishes to sell his/her shares, he/she has to communicate this intention to the other shareholders and shall offer to sell these shares thereto for the price determined or to be determined

in the agreement using the method set forth in the agreement in which the first option is granted before selling these shares to third parties. Terms of the first option can be determined in two ways. If a shareholder grants first option, thus undertaking to first offer the shares for sale to the holder of this option, but is not obliged to sell his/her shares to the holder, such first option will be defined as a right of first proposal (teklifte öncelik). Then, the shareholder's communication of his/her intent to sell will not be considered an offer and will not prevent the shareholder from negotiating the sale with third parties. In other words, the only obligation of a shareholder who granted first option is not to sell the shares to third parties if the holder of such option is ready to conclude the sale on the same terms. If the terms of a first option oblige its grantor to make an irrevocable offer for the sale of shares to the holder of first option first when he/she wishes to sell his/her shares, such first option right will be defined as a right of first refusal (icapta öncelik). In this case, the holder of the first option can conclude the contract by accepting the offer, and unlike the situation with the right of first proposal, the shareholder who granted first option in the form of a right of first refusal cannot revoke his/her offer after it has been accepted by the holder of this right. If the holder of the first option as a right of first refusal rejects the offer, the shareholder who granted first option as a right of first refusal will not be able to sell his/her shares to third parties for a lower price.

Instead of a right of first refusal, first option can be granted as a right of first acceptance (kabalde öncelik). In this case, the grantor of such option will be obliged to accept the offer made by the holder of such right as long as its terms are not worse than the terms of third parties' offers.

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## PRE-EMPTION RIGHT

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The pre-emption right provides the opportunity to its owner to buy the shares of a shareholder with a unilateral statement if such shares are offered for sale or sold to third parties. It can be decided in shareholders' agreements that the pre-emption right shall not be implied in cases of the sale of the respective share to some persons determined in the shareholders' agreement and also a person to whom a share is sold shall be party to the shareholders' agreement. The exercise of the pre-emption right is conditional upon the occurrence of an event which can be defined as the shareholder's voluntary conclusion of a valid sales agreement with a third party for the sale of the shares. The pre-emption right can be exercised with the arrival of a unilateral statement that establishes a legally binding sales agreement between the holder of the right and the shareholder for the sale of shares obligating the shareholder to transfer the shares to the holder of such a right. If the shares are transferred to third parties regardless of

the exercise of the pre-emption right by its lawful holder, the transfer will be valid and the transferred shares cannot be retrieved. However, the shareholder in breach will be liable for damages.

As mentioned earlier, the pre-emption right can only be exercised upon the shareholder's voluntary conclusion of a sales agreement with a third party. Even if such a sales agreement is cancelled or terminated, the exercise of the pre-emption right remains valid and enforceable.

If all shareholders give each other the pre-emption right reciprocally, each holder of the right can obtain an amount of the shares subject to the pre-emption right in proportion with their share ratio. If some of the shareholders do not use their pre-emption right, the shares which they are otherwise entitled to obtain may be bought by other shareholders, provided that the legitimate interests of all shareholders are kept in balance.

Under the TCC, when new shares are issued in accordance with the procedures set forth for the capital increase of the company, the shareholders are provided with a statutory pre-emption right to buy newly issued shares, which gives them the ability to buy a number of newly issued shares in proportion with their share ratio. However, under the TCC, this pre-emption right can be restricted or eliminated in the articles of association or by a general assembly resolution and the newly issued shares can be left to third parties wholly or partially. However, such elimination or restriction of the pre-emption right may not treat the shareholders with the same rights and responsibilities differently.

On the other hand, since shareholders' agreements are contracts entered into by and between shareholders in accordance with the principles of the Code of Obligations, unless their provisions are also adopted into the articles of association, shareholders' agreements do not have to treat the shareholders with the same rights and responsibilities equally.

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## PUT OPTION AND CALL OPTION

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The purpose of the put option and call option granted in shareholders' agreements is generally leaving the company or the exclusion of a shareholder from the company. If a shareholder is provided with a put option, that shareholder will have the right to force the other party to buy its shares. If a shareholder is provided with a call option, that shareholder will have the right to buy the shares of the other party. The agreements granting such options will also include a sales price or a method which will be used to determine the sales price.

Put option and call option can be exercised with an arrival of a unilateral statement of a party that establishes a sales agreement to the other party. When the person who granted a put option receives a unilateral statement from a holder of the option exercising such option, he/she is obligated to buy the

shares subject to the option. On the other hand, upon the exercise of a call option with a unilateral statement, the person who granted the option will be obligated to transfer the shares subject to the option. In order to form a valid sales agreement by exercising put or call options, the terms of the sale, such as quantity of shares and the sales price, have to be determined in advance or be determinable. While the sale price or the method which will be used to determine the sales price can be set forth in the shareholders' agreement, the duty to determine the sales price may be left to a third party in the agreement. If the sales price is not determined or made determinable in the shareholders' agreement, such determination should be made taking the unilaterally exercisable nature of these options into consideration. It should be borne in mind that the main purpose for granting such options in shareholders' agreements is to provide the shareholders with the opportunity to transfer their shares or to buy other shareholders' shares upon the occurrence of the events set forth in the agreement, not to maximize the profit which will be obtained by the sale of the share.

If a first option, pre-emption right or call option is granted in favor of the company in the shareholders' agreement, the company can take over its own shares by exercising such right only if such take-over is included in one of the exceptions set forth in Article 329 of the TCC.

The Issue with the Regulation of Restraints on Transfer of Shares Set Forth in the Shareholders' Agreements and the Articles of Association

As mentioned above, under the TCC, transfer of shares can be restricted by providing a linkage system in the articles of association which gives the company the right to refuse to register the transfer of linked registered shares to the share ledger of the company with no reason if stated thusly in the articles of association or for the reasons stated in the articles of association. In order to constitute a real provision of the articles of association which can be asserted and enforced against the company and its branches, the provisions setting forth restraints on transfer of shares shall not restrict the transfer of shares more than the statutorily allowed linkage system does, because doing so would create an obligation other than paying capital contribution. It would cause liability for damages and violate the core principles of the TCC.

First option, pre-emption right and all versions of put and call options are similar to a linkage system in the sense that all of them limit the right to choose the other party to the agreement. If the regulation of the first option is envisaged in the articles of association, it will constitute one of the real provisions of the articles of association and will bind all existing and future shareholders, the company and its branches. Therefore, even if the company refuses to register the transfer of shares to the share ledger of the company, the other party to the transfer will not be able to hold the shareholder liable for damages. This means

that the regulation of first option in the articles of association will not impose an obligation on shareholders other than paying capital contribution like damages. Therefore this will not violate the core principles set forth in the TCC.

However, since pre-emption rights and all versions of put and call options can be exercised unilaterally, imposing an obligation to buy, sell or transfer shares and restrict the alienability of shares more than the statutorily allowed linkage system does, even if these rights are regulated in the articles of association, they will not be recognized as real provisions of the articles of association and will not have the ability to bind either the shareholders or the company or its branches and cannot be asserted against third parties. Since these rights remain contractual in nature even if regulated in the articles of association, in the event that the company refuses to register the transfer of registered shares to the share ledger of the company, the shareholders who granted those rights may fail to fulfill their obligations to the holders of such rights and can be held liable for damages. Since imposition of additional obligations other than payment of capital contribution, such as liability for damages, is prohibited under the TCC, these rights violate the core principles set forth in the TCC.

As a result, these regulations will only constitute an agreement between shareholders who manifested an intention to be bound with their terms even if regulated in the articles of association and since the company or its branches cannot be forced to act in conformity with these regulations, most of the time, specific performance will not be available as a remedy in the event of breach.

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### THE ISSUE WITH ASSERTION OF CLAIMS AGAINST THIRD PARTIES

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As mentioned above, even if shares that are subject to first option, pre-emption or put and call options are transferred to third parties in breach of these obligations, the transfer remains valid and the shares cannot be retrieved from a third party by claiming such a violation. The shareholders might wish to have the ability to retrieve the shares in the event of breach by regulating these rights in the articles of association and registering the articles of association with the Trade Registry. However, regulation of these rights in the articles of association does not make it possible to assert them against third parties, since only the provisions of the articles of association whose regulation in the articles and registration and declaration by the Trade Registry is required pursuant to Article 300 of the TCC may be asserted against third parties. It should be borne in mind that even first option rights, which bind the existing and future shareholders of the company and the company and its branches when regulated in the articles of association, cannot be asserted against third parties because its regulation in the articles of association and

registration and declaration by the Trade Registry is not mandatory pursuant to Article 300 of the TCC.

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## CONCLUSION

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**A**lthough first option rights can be regulated in the articles of association, pre-emption rights and put and call options cannot be regulated independently in the articles of association and such rights can be made enforceable against the company and its branches when regulated within the framework of the statutorily allowed linkage system. As mentioned above, since by setting forth a linkage system in the articles of association, the company can be obligated not to register the transfer of shares in the share ledger for the reasons listed in the articles of association, in the event that a violation of provisions set forth in the shareholders' agreements is listed as a reason not to register the share transfer to the share ledger, the company can be obligated not to register share transfers violating such provisions. Although this solution does not give the opportunity to retrieve shares transferred in violation of the shareholders' agreements it at least gives the opportunity to prevent the transfer of ownership rights arising out of the ownership of the shares and lets shareholders' agreements stand with the articles of association.

