

## ABSTRACT

### **RIGHTS OF FIRST REFUSAL (ROFR) AND TRANSFERABILITY OF SHARES – A CONUNDRUM**

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Right of First Refusal (hereinafter referred as “ROFR”) clause is one of the key terms in the shareholders agreement between the existing shareholders. In Shareholders agreements, ROFR are often used in favour of shareholders, where one shareholder proposes to transfer its shares. Legally speaking, ROFR is a contractual right that obliges the existing shareholder not to sell its shares in the company to a third party without offering his shares to another party (usually the other existing shareholders). If the existing shareholder(s) does not accept the offer, the selling shareholder is free to sell his stake to a third party, provided the sale is not on more favorable terms than those offered to the existing shareholders. In a nutshell, ROFR forms an integral part to investor’s protection in a shareholders contract. However, there are certain hurdles imposed by the ROFR clauses in shareholder agreement with regard to transfer of shares in public companies. This paper thus analyses the judicial trends for the past 25 years (1991-2016) regarding the enforceability of clauses in shareholders agreements (especially ROFR clause) that restricts the transfer of shares in Public companies.

**Key Words: - Right of first refusal, shareholders agreement, contractual rights, enforceability**

### **STATEMENT OF PROBLEM**

The problem that would be dealt under this project is the conflict between the right of first refusal and the free transferability of shares in public companies as laid down in Section 58(2) of the Companies Act, 1956. ROFR (among other shareholders’ rights such as Right to First Offer<sup>2</sup>, Tag Along<sup>3</sup>, Drag Along<sup>4</sup>), is also viewed as a hindrance to the principle of ‘free transferability’ of shares of a public limited company laid down in Section 58(2) of the

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<sup>2</sup> A right of first offer or ROFO requires owners to tell the holder first when they plan to sell an asset.

<sup>3</sup> The non-selling shareholder has a right to sell its shares along with the shares of the selling shareholder and on the same terms as those of selling shareholder. Simply put as “if you sell, I will have the right to sell along with you”.

<sup>4</sup> Shareholder seller’s right to compel the non-selling shareholder to sell its shares on the same terms as its own shares. Simply put as “if I sell, you will be required to sell with me”

Companies Act, 2013 (corresponding to Section 111-A of the Companies Act, 1956). Such preemptive rights, though legally recognized in case of private limited companies, are highly debatable in case of listed and unlisted public limited companies. Considering this, it becomes imperative to analyse enforceability of ROFR in case of public limited companies vis-a-vis Section 58(2) of Companies Act 2013 (Corresponding Section 111-A of Companies Act, 1956).

### **SCOPE, OBJECTIVES AND SIGNIFICANCE**

The paper title “RIGHTS OF FIRST REFUSAL AND FREE TRANSFERABILITY OF SHARES IN PUBLIC COMPANIES – A CONUNDRUM” will help to understand the concept of Right to first refusal in shareholders’ agreement and will compare it with Section 111A(2) of the Companies Act, 1956 to decide upon the enforceability of share transfer restrictions in Articles of Association.

The basic objectives as here under:

- To understand the concept of free transferability as laid down in S.111A(2) of companies Act, 1956
- To understand the concept of right to first refusal
- To examine the concept of ROFR and free transferability of shares in a company
- To study on the applicability of ROFR in public companies

The research is doctrinal based on the information collected from various secondary sources. Articles published in leading journals, newspapers, and websites have been referred to in proceeding with the research.