

# Minnesota's Revised Limited Liability Company Act: What it Means for Bankers

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The Minnesota Revised Uniform Limited Liability Company Act was signed into law in April, 2014, with a delayed effective date of August 1, 2015. Banks will likely see customers operating under the New LLC Act shortly after August 1, 2015, as all LLCs formed after that date will be organized under the New LLC Act. Existing LLCs may continue to operate under the current law for another two and one-half years, but all LLCs are required to be in compliance with the New LLC Act by January 1, 2018.

The New LLC Act incorporates many partnership concepts and aligns Minnesota law with the LLC structures in many other states. The overall shift in the New LLC Act to a less formal, more flexible regime may increase the prevalence of the LLC as the business entity of choice in Minnesota. Further, by bringing Minnesota law into alignment with that of other states (most notably Delaware), Minnesota businesses may find less of a need to organize under the laws of another state.

## What has changed?

The most significant change under the New LLC Act is to make partnership-style management the standard for all LLCs. Most Minnesota LLCs are currently governed by a board of governors (similar to the board of directors in a corporation) and managers (similar to officers in a corporation). Under the New LLC Act, an LLC would need to affirmatively choose to be managed by a board and managers. Without such an election, an LLC will be member-managed, meaning each member (analogous to a shareholder of a corporation) has management rights and can act on behalf of the LLC. The choice in management style will have a significant impact on who is authorized to enter into credit arrangements and other banking transactions on behalf of an LLC.

To help outsiders understand which members and managers have the authority to act on behalf of an LLC, the New LLC Act allows (but does not require) an LLC to make a filing with the Secretary of State designating which members or managers have authority to enter into transactions on behalf of the LLC. A bank may want to require member-managed or manager-managed LLC customers to file a statement of authority before entering into transactions with the bank.

## Member-Managed

How Created? Standard

Authorized Signer: Any Member

**Manager-Managed**

How Created? Affirmative Election

Authorized Signer: Any Manager

**Board-Managed**

How Created? Affirmative Election

Authorized Signer: Chief Manager (or other designated manager)

**What remains the same?**

The New LLC Act will also change the due diligence materials and other supporting documentation to be obtained in connection with a transaction involving an LLC customer. Under the New LLC Act, rights and duties previously addressed in bylaws or a member control agreement will be combined into a single operating agreement. An operating agreement under the New LLC Act can be informal and does not necessarily need to be in writing or even called an "operating agreement." Banks may want to require an LLC customer to reduce its operating agreement to writing as part of the normal due diligence process.

With the help of the Minnesota Bankers Association, the New LLC Act retains important provisions related to an LLC's ability to provide third-party support for the extension of credit to another party. An LLC can currently guaranty the obligations of, or provide other financial support to, a related party – including a member – if the LLC has a financial interest or business relationship with the related party and the guaranty or financial support is approved by the LLC's board of governors. The original version of the New LLC Act passed in April, 2014, did not contain these provisions, calling into question whether an LLC could provide third-party support to other parties. The Minnesota Bankers Association worked with the Legislature during the 2015 session and secured the passage of a new provision reinstating language that does allow an LLC to provide third-party support.

Unfortunately, another important banking provision has not been reinstated by the Legislature at this time. Under current law, an LLC may grant a security interest in all or substantially all of its assets upon approval by the board of governors, regardless if the grant of the security interest is in the LLC's normal course of business. The New LLC Act does not contain a similar provision. If granting a blanket security interest might be considered to be outside the ordinary course of the LLC's activities in a particular case, then, under the New LLC Act, all members would have to consent before the LLC could grant that security interest. Depending on the number of members, this could greatly increase the complexity faced by customers in securing approvals to grant a security interest. It could also give a member owning a very small share of an LLC a disproportionately large say in lending transactions.

The New LLC Act does not change the nature of a member's ownership interest in an LLC. A member's ownership interest (called a "transferable interest" under the New LLC Act) is personal property that may or may not be certificated. Generally, a secured party will perfect a security interest in a membership interest of an LLC as a general intangible by filing a financing statement with the appropriate filing office. Under certain circumstances, however, a transferable interest will continue to be a security governed by Article 8 of the UCC, with perfection accomplished through

possession.

Good practice has always been to verify that an LLC customer is in good standing on a periodic basis. That practice has not changed under the New LLC Act. LLCs will need to continue filing annual reports with the Secretary of State to avoid administrative dissolution and the Secretary of State will continue to issue certificates verifying that an LLC remains in existence, though the name of these certificates may change to conform to minor language changes in the New LLC Act.

### **Conclusion**

The New LLC Act represents a significant shift in how Minnesota LLCs are governed. The LLC entity will continue to mix aspects of corporations and partnerships, with the balance shifting more towards the partnership model under the New LLC Act. Banks may need to shift as well. Practices and procedures designed to accommodate formalized structures should be examined to assess whether they adequately capture necessary authorizations in the less formal world of the New LLC Act. Further, a bank may need to require LLC customers to go beyond the minimalist structure of the New LLC Act in order for the bank to be adequately protected. Ultimately, however, the New LLC Act should have only a limited impact on how bankers interact with LLC customers.

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