

Minnesota's Revised Limited Liability Company Statute

Spring 2015 Firm Newsletter
03.20.2015

In April 2014, Minnesota Governor Mark Dayton signed into law the “Minnesota Revised Uniform Limited Liability Company Act” (New Act). The New Act, which appears in Chapter 322C of the Minnesota Statutes, goes into effect on August 1, 2015, and all limited liability companies organized on or after that date will need to comply with the new law. The New Act replaces the current Minnesota Limited Liability Company Act, found in Chapter 322B of the Minnesota Statutes. Existing LLCs are not immediately affected by the change in the law, although they may elect to be subject to the New Act by amending their governing documents accordingly. However, on January 1, 2018, 322B will be repealed and all then existing LLCs in Minnesota will be required to comply with the New Act.

It is important for existing LLC owners and anyone considering organizing or investing in a Minnesota LLC to understand some of the significant changes the New Act will bring, including:

- **Governance and Management Structure** – The New Act changes the management of an LLC toward the partnership model utilized in most states. Currently, most Minnesota LLCs are governed by a board of governors and managers (similar to the board of directors and officers in a corporation) with their members being analogous to shareholders. The New Act changes the default to a “member-managed” structure, which means that unless provided otherwise in an operating agreement, the management of the LLC is vested in the members and each member has equal rights in the management and conduct of the company’s activities. However, the New Act also permits “manager-managed” and “board-managed” governance, which should allow existing LLCs to maintain their current structures.
- **Operating Agreement** – Under the New Act, the rights and duties previously contained within the articles, bylaws, and member control agreement are combined into a single “operating agreement.” The operating agreement is a contract between the members that govern the LLC’s member relationships, governance structure, and activities, among other things. Unlike 322B’s current requirement of a written member control agreement, an operating agreement can be informal and does not necessarily need to be in writing or even called an “operating agreement.” The operating agreement gives the members substantial flexibility to define their relationship and direct the operation of the LLC, with certain exceptions and restrictions.
- **Voting** – The default rule under 322B is that the voting power of members is proportional to the value of their respective capital contributions. Under the New Act, voting is “per capita,” which means that each member will have equal voting rights in the management and conduct of the LLC’s activities unless the operating agreement provides otherwise. There is, however, already a bill of proposed amendments (which will be considered in the current Minnesota legislative

session) that would grandfather in the current voting allocation provisions for an existing LLC formed before August 1, 2015.

- **Standards of Conduct and Other Duties** – Those in charge of managing an LLC — whether members, managers, or governors — have a “duty of loyalty” and a “duty of care” to the LLC. These duties may not be waived under 322B. The fiduciary duties of loyalty and care still apply under the New Act to those with management responsibility and cannot be eliminated. However, they may be modified or limited to the extent not “manifestly unreasonable.” The additional requirement of “good faith and fair dealing” among members also cannot be eliminated. However, the operating agreement can “prescribe the standards by which to measure the performance of the contractual obligation of good faith and fair dealing.”
- **Distributions** – Under the New Act, unless the operating agreement provides otherwise, the default rule is that operating distributions are per capita rather than proportionate to capital contributions (as is the case in 322B) and must be distributed in equal shares among the members. However, a pending bill of proposed amendments would grandfather in the provision for distributions in proportion to capital contributions for any LLC formed before August 1, 2015. Upon dissolution and wind up of the LLC, unless the operating agreement provides otherwise, the New Act requires that distributions first be made to each member in an amount equal to the value of any unreturned contributions, and then in equal shares (per capita) among the members. Owners who currently receive distributions based upon their respective capital contributions to an LLC formed prior to August 1, 2015, will want to be sure that, prior to January 1, 2018, the LLC’s operating agreement expressly maintains proportional distributions based on those contributions. Otherwise, the New Act will require that distributions be made on a per capita basis.
- **No Preemptive Rights** – Under 322B, the members of an LLC automatically have preemptive rights (the right of a member to maintain his/her proportional ownership of the LLC) unless the governing documents or board provide otherwise. However, the New Act does not address preemptive rights. If the members wish to maintain their preemptive rights under the New Act, this will need to be specifically addressed in the operating agreement.
- **No Dissenters’ Rights** – Under 322B, a member may dissent and obtain payment for the fair value of the member’s interest in an LLC in the event of certain company actions. The New Act does not provide for statutory dissenters’ rights or appraisal rights. Accordingly, the current statutory rights of dissenting members will be eliminated on January 1, 2018, with the expiration of 322B. LLC owners should consider whether they wish to retain dissenters’ rights and make plans to expressly include such rights in the LLC’s operating agreement.
- **“Dissociation” of a Member** – The New Act allows members to dissociate (resign) from the LLC “at any time, rightfully or wrongfully.” However, the New Act provides no obligation for the LLC or other members to buy out the dissociating member, nor does it trigger a judicial dissolution of the LLC.
- **Derivative Claims and Direct Action by a Member** – 322B provides members with the right to file a derivative action on behalf of an LLC alleging certain kinds of misfeasance on the part of the LLC’s management. However, 322B does not provide a direct right of action against the LLC on behalf of a member. Under the New Act, a member can bring a direct action for injuries to that member as well as a derivative action to enforce a claim on behalf of an LLC.

- **Merger, Conversion, and Domestication** – The New Act has comprehensive provisions authorizing LLCs to merge or convert into another type of entity and also authorizes other types of entities to merge and convert into an LLC. The default rule for each type of transaction requires there be unanimous approval of all members unless the operating agreement provides otherwise. The New Act also authorizes a Minnesota LLC to domesticate in another state and also authorizes a foreign LLC to domesticate in Minnesota.
- **Judicial Intervention and Oppressive Conduct** – 322B has extensive provisions detailing when and how a court may become involved in disputes among members, what considerations it may take into account, and how it may go about imposing equitable remedies, including voluntary dissolution or forced buy-outs. The New Act is more expansive and permits a court to order dissolution or some remedy shy of dissolution (including a forced buy-out).
- **Authority to Bind LLC and Statements of Authority** – Unlike under 322B, the New Act permits an LLC to file a “statement of authority” with the Minnesota Secretary of State to provide notice as to which members or managers have authority to transfer real estate or bind the LLC to persons that are not members. The statement can also describe any limitations on the authority of the person to enter into certain transactions. This option allows LLCs to provide clarity to its members and others as to which members or managers have authority.
- **Shelf LLC** – The New Act includes a reference to a “Shelf LLC,” which is what exists after the organizer has filed the articles of organization and before the LLC has any members. A Shelf LLC is typically created in anticipation of a pending deal or while prospective members negotiate and document the LLC’s terms of membership, governance, and operations. However, until such time that it “has at least one member,” the Shelf LLC “lacks the capacity to do any act or carry on any activity” except: making certain filings with the Minnesota Secretary of State, admitting a member, and/or dissolving.

Considerations for Our Clients

If you have an interest in an existing LLC that is organized under 322B, you should plan to review its structure and governing documents to determine what changes may be needed in order to bring your LLC into compliance with the New Act starting in 2018. The governing documentation for some LLCs will require little or no modification, while the need for modification will be greater in other situations. In certain circumstances, including in the event of a merger or recapitalization, members under existing LLCs may desire to elect into the New Act early to ensure that only one set of statutes (*i.e.*, the New Act) will apply.

As noted, there is already a proposed bill for the next Minnesota legislative session that would make both technical corrections and substantive changes to the New Act, including grandfathering in the existing voting allocation and distribution provisions in 322B. Additional amendments may be proposed, so it will be important to monitor for legislative adoption of any amendments and to consider their effect on LLCs, whether formed before or after the August 1, 2015 effective date of the New Act.

For additional information on the New Act, including information on additional changes under the New Act not discussed here, or for assistance in assessing why you may want to consider an early adoption of the New Act, contact your attorney at Moss & Barnett.

Practice Areas

Business Law

