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THE NEW MINNESOTA LLC ACT: FLEXIBILITY AND CONTROL FOR MINNESOTA BUSINESS OWNERS

Leanne Fuith*

In April 2014, the Minnesota legislature introduced the Minnesota Revised Uniform Limited Liability Company Act (herein “the New Act”) which became effective on August 1, 2015 for all new LLCs formed on or after that date.¹ LLCs already in existence prior to August 1, 2015, will be governed by the New Act as of January 1, 2018, or sooner if they so elect.²

The New Act provides LLC member owners with a greater ability to create the business that they want by agreement (rather than being subject to statutorily set restrictions) while maintaining the key benefits of LLCs such as limited liability and pass-through partnership taxation. The introduction of the New Act allows for greater flexibility and less formality in the formation and management of the LLC than the corporate-based model to which Minnesota LLC owners had become accustomed and it is also a step toward achieving great uniformity with LLC law in other states.

The actual impact of the New Act on Minnesota businesses, however, is yet to be determined. Attorney practitioners across the state of Minnesota are closely evaluating how these changes should be implemented within their clients’ businesses and when the right time is to do so. For many clients, the introduction of the New Act will bring increased flexibility in being able to manage their business, but may also increase cost in making the transition from the current corporate-like model to a more partnership-based model.

This article will highlight some of the key changes in the Minnesota Revised Uniform Limited Liability Company Act and discuss the reasons for the change and how some of those changes may impact Minnesota business owners.

A Brief History of the Limited Liability Company

The Limited Liability Company (LLC) was first introduced as a business form in Wyoming in 1977.³ It was a hybrid form of an unincorporated business organization that, over time, brought together the best of two worlds – the limited liability that was typically available to the owners of a corporation and the pass-through taxation and member’s management rights that usually signified a partnership.⁴

By 1996, all states had adopted the use of the LLC as a form of business organization, but because no uniform law existed for much of this time, the individual state statutes governing LLCs varied greatly from

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¹ MINN. STAT. § 322C.1204, subdiv. 1 (2015).

² MINN. STAT. § 322C.1204, subdiv. 1 (2015).

³*LLCs: Is the Future Here? A History and Prognosis*, GP|SOLO LAW TRENDS & NEWS, AMERICAN BAR ASSOCIATION (Oct. 2004),

http://www.americanbar.org/newsletter/publications/law_trends_news_practice_area_e_newsletter_home/llc.html.

⁴*Id.*; see also Rev. Rul. 88-76, 1988-38 I.R.B. 14.

state to state, including in Minnesota.⁵ In 1994, The Uniform Law Commission introduced the Uniform Limited Liability Company Act in an effort to bring clarity and stability to the varied ways in which LLCs were being formed and governed across the United States.⁶ However, because many states had already been operating under their own individually developed LLC statutes, this first generation Uniform Limited Liability Company Act was not widely adopted.⁷

In July 2006, the Uniform Law Commission introduced the Revised Uniform Limited Liability Company Act.⁸ It is this second generation statute upon which Minnesota's New LLC Act is based.

Legal Landscape of Minnesota LLCs

In 1993, Minnesota first recognized LLCs as a business form and in each year since 2007, more LLCs have been formed in Minnesota than all other business forms combined.⁹ In 2015, more than 31,000 LLCs were formed in Minnesota and made up more than 78% of all new Minnesota business filings.¹⁰

Until the introduction of the New Act, the Minnesota Limited Liability Company Act codified as Minnesota Statute Chapter 322B (herein "Chapter 322B") was the sole governing law for all LLCs formed in the state of Minnesota. Chapter 322B is unique in the sense that it has strong foundations in the Minnesota Business Corporation Act codified as Minnesota Statute Chapter 302A (herein "the Minnesota Business Corporation Act"). Only North Dakota had an LLC statute with a similar foundation in corporate law.¹¹ Notably, North Dakota also introduced a revised LLC Act in July 2015, just one month before the introduction of Minnesota's New Act.¹²

⁵ *LLCs: Is the Future Here? A History and Prognosis*, *supra* note 3.

⁶ REVISED UNIF. LTD. LIAB. CO. ACT (2006) [hereinafter RULLCA],

http://www.uniformlaws.org/shared/docs/limited%20liability%20company/ullca_final_06rev.pdf.

⁷ *Legislative Fact Sheet - Limited Liability Company* (2006) (Last Amended 2013), NAT'L CONF. OF COMMISSIONERS ON UNIFORM LAWS,

[http://uniformlaws.org/LegislativeFactSheet.aspx?title=Limited%20Liability%20Company%20\(2006\)%20\(Last%20Amended%202013\)](http://uniformlaws.org/LegislativeFactSheet.aspx?title=Limited%20Liability%20Company%20(2006)%20(Last%20Amended%202013)).

⁸ RULLCA, *supra* note 6.

⁹ Brett M. Larson & Nathan J. Nelson, *Minnesota's LLC Makeover: Increased Certainty Heightens LLCs' Appeal*, BENCH & BAR OF MINNESOTA, Feb. 9, 2015, <http://mnbenchbar.com/2015/02/minnesotas-llc-makeover/>

¹⁰ <http://www.sos.state.mn.us/index.aspx?page=3>.

¹¹ Jessica D. Manivasager, *New LLC Acts in Minnesota and North Dakota*, Dec. 2, 2015,

http://www.fredlaw.com/news__media/2015/12/02/1067/new_llc_acts_in_minnesota_and_north_dakota.

¹² *Id.*

The corporate-like structure of Chapter 322B allows for members, a board of governors and managers – similar to shareholders, boards of directors and officers.¹³ The corporate-based model of Chapter 322B also requires more formalities in terms of documentation and organization and appointment of leadership and ownership and voting power within the organization is allocated based on an individual’s capital contribution.¹⁴

The more formalistic approach of Chapter 322B was familiar to many businesses and attorneys who had become accustomed to working under the Minnesota Business Corporation Act, but it was rigid and more prescriptive particularly for single owner and family owned businesses with the need to create deals tailored to the unique nature of their businesses and lives. Enter the Revised Uniform Limited Liability Act and the New Minnesota LLC Act.

The New Minnesota LLC Act

In April 2014, the Minnesota legislature adopted the New Minnesota LLC Act and codified it as Minnesota Statute Chapter 322C.¹⁵ The New Act is based upon the Revised Uniform Limited Liability Act or “second generation statute” as established by the Uniform Law Commission in 2006 and includes some Minnesota-specific modifications as well.¹⁶ As of the time of the writing of this article, the following states have enacted the Revised Uniform Limited Liability Company Act: Alabama, California, District of Columbia, Florida, Idaho, Iowa, Minnesota, Nebraska, New Jersey, South Dakota, Utah, Vermont, Washington and Wyoming.¹⁷ The states of Connecticut, Illinois, Pennsylvania and South Carolina have further plans to introduce the Revised Uniform Limited Liability Company Act in 2016.¹⁸

¹³ MINN. STAT. §§ 322B.03, subdiv. 30; 322B.606; 322B.67 (2015).

¹⁴ Examples of the more formalistic nature of Chapter 322B includes the prescriptive descriptions for member voting and control agreements (MINN. STAT. §§ 322B.366, 322B.37 (2015)), the requirements for annual financial statements and other detailed record-keeping (MINN. STAT. §§ 322B.373, 322B.376 (2015)), the requirements for organizational meetings or written action following the filing of the Articles of Organization (MINN. STAT. § 322B.60 (2015)). Likewise, Chapter 322B specifically establishes that voting and sharing of distributions will be in proportion to the value of the contributions of individual members. MINN. STAT. §§ 322B.50, 322B.356, subdiv. 2 (2015).

¹⁵ MINN. STAT. § 322C (2015).

¹⁶ *Why States Should Adopt RULLCA*, NAT’L CONF. OF COMMISSIONERS ON UNIFORM LAWS, <http://www.uniformlaws.org/Narrative.aspx?title=Why%20States%20Should%20Adopt%20RULLCA>

¹⁷ *Legislative Fact Sheet - Limited Liability Company*, *supra* note 7.

¹⁸ *Id.*

In Minnesota, the New Act went into effect on August 1, 2015 for all LLCs formed on or after that date.¹⁹ LLCs already in existence as of July 31, 2015, may elect to remain governed by current Chapter 322B or to be governed under the New Act (Chapter 322C).²⁰

On January 1, 2018, Chapter 322B will be repealed and all Minnesota LLCs, including those Chapter 322B LLCs that did not previously elect to follow the New Act, will automatically be governed by the New Act.²¹ The challenge for attorneys and businesses between now and January 2018 will be to determine whether and when a business should proactively choose to be governed by the New Act prior to the January 2018 deadline.

The introduction of the New Act is a step towards a partnership model of formation and governance for Minnesota LLCs from the corporate-based model of Chapter 322B while still maintaining the key benefits of limited liability and pass-through (partnership) taxation. As with partnership law, the New Act allows for greater flexibility and less formality in the formation and management of LLCs than the current model and may better recognize the interests of minority owners. The language of the New Act loosens many of the statutorily set restrictions that previously gave the courts wide latitude in enforcement and instead encourages LLC owners to create, by agreement between the owners, the company structure most appropriate for their businesses. Owners are likely to have more control over the formation and governance of their business on key issues than has been seen in Minnesota LLC law previously. For this and other reasons to be discussed, written agreements between the owners of LLCs formed under the New Act will become more critical than ever.

As noted, Chapter 322B takes a corporate approach to governance that is inconsistent with nearly every other LLC act in the United States.²² As a result, when business transactions involve parties outside of Minnesota, the lawyers for the non-Minnesota parties rarely agree to adopt Chapter 322B as the governing law.²³ Instead, the parties agree to use the Delaware LLC Act, which can add significant complexities and cost for Minnesota businesses⁷ in terms of understanding Delaware law and litigating disputes in Delaware.²⁴ Among its other benefits, the introduction of the New Act is also designed to remedy this issue as the New Act is more consistent with the LLC law of other states.

More Flexible Formation

The New Act provides more flexibility in the formation of a LLC from who can form an LLC to the information required to do so. First and foremost, the New Act provides that one or more persons may act as organizers to form a limited liability company and it goes on to broadly define “persons” as not just individuals, but also corporations, partnerships, trusts, joint ventures and other legal or commercial

¹⁹ Larson & Nelson, *supra* note 9.

²⁰ MINN. STAT. § 322C.1204, subdiv. 1 (2015).

²¹ MINN. STAT. § 322C.1204, subdiv. 2 (2015).

²² Manivasager, *supra* n. 11 (North Dakota was the only other state to follow this corporate-based model and in July 2015, North Dakota also elected to follow the Revised Uniform Limited Liability Act).

²³ William D. Klein, *Overview of the New Minnesota Revised Uniform Limited Liability Company Act*, in THE NEW MINNESOTA LLC ACT §§ 1-2 (Jan. 2015).

²⁴ *Id.*

entities.²⁵ With this revised language, the New Act recognizes some of the unique business transactions of today in a way that Chapter 322B, and its requirement that an organizer be a “natural person,” does not.²⁶ As with Chapter 322B, the New Act requires that Articles of Organization be filed with the Minnesota Secretary of State in order to properly form a Minnesota LLC.²⁷ However, the Articles of Organization are further simplified under the New Act requiring only the name of the LLC (which must comply with Minnesota Statute § 322C.0108), the street address of the initial registered office, the name of the agent for service of process (if the LLC has one) and the name and street address of each organizer.²⁸ Information regarding the planned duration of the LLC and any statements regarding statutory provisions that the LLC owners intend to modify that were previously required under Chapter 322B are no longer required in the Articles of Organization under the New Act.²⁹

Simplified Corporate Documentation; Broader Definition of Operating Agreement

Prior to the enactment of the New Act, an LLC had any number of governing documents many of which utilized terminology carried over from the corporate structure, including bylaws, member voting control agreements and shareholder voting and control agreements and all of which are referenced in Chapter 322B and the Minnesota Business Corporation Act.³⁰

The New Act contemplates a simpler approach in which the primary governing document is the Operating Agreement (although the language of the New Act is also broad enough to encompass something other than an Operating Agreement including multiple documents).³¹ This approach, not surprisingly, mirrors the partnership model where the primary governing document is the partnership agreement and is also consistent with that of other states that follow the Revised Uniform Limited Liability Company Act – lending to greater understanding of business formation forms and procedures from state-to-state.³²

²⁵ MINN. STAT. §§ 322C.0201, subdiv. 1, 20 (2015).

²⁶ MINN. STAT. § 322B.105 (2015).

²⁷ MINN. STAT. §§ 322C.0201, subdiv. 1; 322B.17 (2015).

²⁸ MINN. STAT. § 322C.0201, subdiv. 2(2015).

²⁹ MINN. STAT. §§ 322B.115, subdiv. 2-3, 322C.0201 (2015); Note that the New Act does allow for other statements to be included in the Articles of Organization as optional information; MINN. STAT. 322C.0201, subdiv. 3 (2015).

³⁰ MINN. STAT. §§ 302A.181, 302A.455, 302A.457, 322B.603, 322B.366, 322B.37 (2015).

³¹ MINN. STAT. §§ 322C.0110; 322C.0102, subdiv. 17 (2015). *See also* MINN. STAT. § 322C.1204, subdiv. 3(2) (2015) (noting that the language in the articles of organization, and any bylaws, operating agreement, or member control agreement of a limited liability company formed before August 1, 2015 will operate as if that language were in the operating agreement subject to the New Act.)

³² Minnesota’s Uniform Partnership Act, MINN. STAT. §§ 323A.0103 (2015); Minnesota’s Uniform Limited Partnership Act, MINN. STAT. § 321.0110 (2015); RULLCA, *supra* note 6, §§ 102, 110.

In a LLC formed under the New Act, the Operating Agreement addresses relations among members as members and between members and the LLC; the rights and duties of persons acting in the capacity of manager or governor; the activities of the LLC and conduct of those activities and the means and conditions for amending the operating agreement. ³³ The Operating Agreement is a critical document under the New Act because to the extent that an Operating Agreement does not otherwise provide for one of the above-mentioned matters, the New Act will be found to govern the LLC in that regard.³⁴ The New Act provides a very limited number of ways in which the LLC owners, through the mechanism of the Operating Agreement, may *not* vary the default rules of the New Act.³⁵ These exceptions are narrow in both nature and scope and are detailed in Minnesota Statute § 322C.0110, subdivision 3.³⁶

Importantly, the New Act also significantly broadens the definition of Operating Agreement describing it as an “agreement, whether or not referred to as an operating agreement and whether oral, in a record, implied or in any combination thereof, of all the members of a limited liability company, including a sole member....”³⁷ Notably, “record” is further defined as information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.³⁸ In contrast, Chapter 322B requires that the agreements governing an LLC be made in writing.³⁹

The New Act’s broader definition of Operating Agreement has one of the earliest and most significant practical effects on Minnesota LLCs. The language of the New Act is a direct nod to the demands of modern day businesses for more flexibility and less formality. Yet, for the unsuspecting business owner, one or a series of emails, voice mails or even text messages could be interpreted to be an Operating Agreement resulting in a difficult consequence for LLCs who adopt the New Act without proper counsel, preparation and documentation including a rock solid integration clause.

Finally, the language of the New Act provides that not only can the member owners of an LLC bring an action to enforce an Operating Agreement, but the LLC itself can do the same even if the LLC is not a party to the Operating Agreement.⁴⁰ By contrast, Chapter 322B provides that a valid member control agreement is only enforceable by persons who are parties to it.

³³ MINN. STAT. § 322C.0110, subdiv. 1 (2015).

³⁴ MINN. STAT. § 322C.0110, subdiv. 2 (2015).

³⁵ MINN. STAT. § 322C.0110, subdiv. 3 (2015).

³⁶ *Id.*

³⁷ Minn. Stat. § 322C.0102, subdiv. 17 (2015).

³⁸ MINN. STAT. § 322C.0102, subdiv. 22 (2015).

³⁹ MINN. STAT. § 322B.30, subdiv. 2 (2015) (requiring statements of membership interest in writing), MINN. STAT. § 322B.37, subdiv. 2 (2015) (requiring member control agreements in writing), MINN. STAT. § 322B.42, subdiv. 1 (2015) (requiring contribution agreements in writing), MINN. STAT. § 322B.373, subdiv. 1(4) (2015) (requiring written bylaws), MINN. STAT. § 322B.366, subdiv. 1 (2015) (requiring written voting agreements).

⁴⁰ MINN. STAT. § 322C.0111, subdiv. 1 (2015).

Three Flexible Governance Structures and a New Default

The New Act provides for three flexible governance structures and importantly, a default structure that for many existing LLCs may be quite different in practical effect from what they are currently accustomed. The governance structure of an LLC is critical because it affects the voting rules and members' ability to bind the LLC and it affects the duties between the members. In reframing its approach to LLC governance, the New Act turns the management structure of an LLC on its head putting the default control of an organization back into the hands of the owners.

The New Act contemplates member-managed, manager-managed or Board of Governors-managed LLCs.⁴¹ The default structure for an LLC formed under the New Act is member managed, but the member owners may elect one of the two alternate governance structures choosing to be either manager-managed or managed by a board of governors.⁴² The choice to be governed by one of these alternate structures must be specifically stated in the LLC's Operating Agreement.⁴³

By contrast, Chapter 322B assumes that the business and affairs of an LLC will be managed by or under the direction of a Board of Governors.⁴⁴ This is again consistent with the corporate "board of directors" model familiar to many Minnesota businesses and attorneys. Chapter 322B still rests authority in the member owners of the LLC to take actions that would otherwise be the responsibility of a Board of Governors by a unanimous, affirmative vote of the members, but it does not contemplate a manager-managed structure as an option.⁴⁵

The New Act's retention of the Board of Governors structure is a significant departure from the Revised Uniform Limited Liability Act as drafted by the Uniform Law Commission in 2006. The drafters of the New Act recognized the reality that many Minnesota LLCs have already established themselves under the corporate-like Board of Governors structure that was provided for in Chapter 322B.⁴⁶ For many of those businesses that structure is working well and so the drafters of the New Act modified the language of the Revised Uniform Limited Liability Act to maintain the board-of-governors management model and provide Minnesota LLCs with a choice in governance structures that may better reflect their preferences.⁴⁷

For current LLCs that have operating or member control agreements that specify either a member-managed or a board-of-governors managed governance structure, the New Act should bring few significant changes in terms of the day-to-day management of the LLC. However, LLCs that have not specified a governance arrangement within their organizational agreements and have instead relied on the board-managed statutory default of Chapter 322B will need to be aware as the January 1, 2018 deadline approaches and make arrangements to select the governance structure that best suits their business needs.

⁴¹ § 322C.0407, subdiv. 1 (2015).

⁴² MINN. STAT. § 322C.0407, subdiv. 1, 3 and 4 (2015).

⁴³ MINN. STAT. § 322C.0407, subdiv. 1 (2015).

⁴⁴ MINN. STAT. § 322B.606, subdiv. 1 (2015).

⁴⁵ MINN. STAT. § 322B.606, subdiv. 2 (2015).

⁴⁶ Klein, *supra* note 23, at 3.

⁴⁷ *Id.*

On January 1, 2018, Minnesota LLCs will convert to member-managed organizations unless their preferred governance arrangement is formalized before then either through a new Operating Agreement (as defined under the New Act) or their earlier governance documents.⁴⁸ Looking ahead, it will be worth noting how many and which types of Minnesota LLCs elect to follow the Board of Governors management structure and how many opt for either member-managed or the new manager-managed structure.

Voting and Distributions Shared Equally on a Per Capita Basis

Similar to partnership law, the Revised Uniform Limited Liability Company Act recognizes an equal need for management and control over the LLC for minority members who have contributed to the LLC in terms of sweat equity rather than in monetary contributions.⁴⁹ The New Act mirrors the Revised Uniform Limited Liability Company Act in this regard and the default rules of the New Act provide that voting is shared equally among members on a per capita basis.⁵⁰ In contrast, the default rules of Chapter 322B provide that voting power is in proportion to the value of the contributions of individual members as reflected in the required records.⁵¹

Again consistent with partnership law and the Revised Uniform Limited Liability Company Act, the New Act also provides that distributions are also shared equally among members on a per capita basis.⁵² Not surprisingly, Chapter 322B notes that distributions are shared in proportion to the value of the contributions of individual members.⁵³

The rules contained in the New Act regarding voting and sharing of distributions are, with most of the other provisions of the New Act, simply default rules and can be modified and customized by agreement giving members the control needed to create the business they want. For Minnesota LLCs originally formed under Chapter 322B, the New Act offers a carve out stating that both the voting power and distribution share of each member will continue to be in proportion to the value of the contributions of the members providing it is reflected as such in the Operating Agreement.⁵⁴

⁴⁸ MINN. STAT. §§ 322C.1204, subdiv. 2; 322C.0407, subdiv. 1 (2015); *See also* MINN. STAT. § 322C.1204, subdiv. 3(2) (2015) (noting that the language in the articles of organization, and any bylaws, operating agreement, or member control agreement of a limited liability company formed before August 1, 2015 will operate as if that language were in the operating agreement subject to the New Act).

⁴⁹ RULLCA, *supra* note 6, § 407, subdiv. b(2); *See also* MINN. STAT. § 323A.0401, subdiv. F. (2015).

⁵⁰ MINN. STAT. § 322C.0407, subdiv. 2(2) (2015).

⁵¹ MINN. STAT. § 322B.356, subdiv. 2 (2015).

⁵² MINN. STAT. § 322C.0404, subdiv. 1 (2015); RULLCA, *supra* note 6, § 404, subdiv. a; *See also* MINN. STAT. § 323A.0401, subdiv. b (2015) (noting specifically that partners share profits equally and losses in the same manner as profits).

⁵³ MINN. STAT. § 322B.50 (2015).

⁵⁴ MINN. STAT. §§ 322C.1204, subdiv. 3(3)(v)-(vi) (2015).

Standards of Conduct That Can Be Modified

Chapter 322B and the New Act both impose upon members, managers and governors, the fiduciary duties of loyalty and care and both establish standards of conduct for each of these fiduciary duties as articulated within the statutes.⁵⁵ Under the New Act, how and to whom these duties apply depends on whether the LLC is member-managed, manager-managed or board-of-governors managed.⁵⁶

These duties are statutorily set in Chapter 322B and are not subject to variation. The New Act, conversely, allows LLC owners some latitude to modify these fiduciary duties – adjusting the standards for each duty upwards or downwards or even eliminating the duty — according to the wishes of the parties as long as the decision to do so is not “manifestly unreasonable.”⁵⁷ The New Act does not provide a precise definition of what constitutes a “manifestly unreasonable” decision, but suggests that a court would make such a determination

...as of the time the challenged term became part of the operating agreement and by considering only circumstances existing at that time; and (2) may invalidate the term only if, in light of the purposes and activities of the limited liability company, it is readily apparent that: (i) the objective of the term is unreasonable; or (ii) the term is an unreasonable means to achieve the provision's objective.⁵⁸

How courts will apply this guidance to questions regarding manifestly unreasonable decisions remains to be seen.

Notably, the duty of good faith and fair dealing is also provided for in the New Act, but is not addressed in Chapter 322B.⁵⁹ Unlike the duties of loyalty and care, the duty of good faith and fair dealing cannot be eliminated under the New Act, but the parties may establish (by agreement) standards by which performance under the duty of good faith and fair dealing will be measured.⁶⁰

Clarifies Agency Relationship of Member; Statements of Authority Permissible

Chapter 322B does not specifically address the agency of members, but it does require that an LLC have one or more natural persons exercising the functions of the offices, of chief manager, and treasurer and delegates the general power to manage the LLC to the chief manager.⁶¹

⁵⁵ MINN. STAT. §§ 322B.663, subdiv. 1; 322C.0409, subdiv. 1-3 (2015).

⁵⁶ MINN. STAT. §§ 322C.0409, subdiv. 1, 7, 8 (2015).

⁵⁷ MINN. STAT. §§ 322C.0110, subdiv. 3(4), 4 (2015).

⁵⁸ *Id.*, subdiv. 8.

⁵⁹ MINN. STAT. § 322C.0409, subdiv. 4 (2015).

⁶⁰ MINN. STAT. § 322C.0110, subdiv. 4(5) (2015).

⁶¹ MINN. STAT. §§ 322B.67; 322B.673, subdiv. 2 (2015).

The New Act clearly states that a member is not an agent of an LLC solely by virtue of being a member of the LLC.⁶² The provision effectively eliminates the notion of apparent statutory authority and instead leaves questions of agency liability and a member's ability to bind an LLC to agency law and the terms of the operating agreement that the members negotiate between themselves.

The New Act also permits an LLC to file Statements of Authority similar to those that may be filed under the Uniform Partnership Act of 1994 (codified as Minnesota Statute § 323A).⁶³ Statements of Authority must be filed with the Secretary of State and can be used to clarify, or limit the power of any person holding a position within the LLC to bind the LLC to persons that are not members of the LLC.⁶⁴ This mechanism did not exist in Chapter 322B.

Defines Transferable Interest; Provides For More Control Over Transfers

The New Act defines "transferable interest" as a member's financial rights within the LLC and excludes the member's rights to manage or govern the company.⁶⁵ Unless restricted by an operating agreement, the New Act provides that a member may transfer his or her transferable interest freely to a non-member with appropriate notice to the LLC.⁶⁶ A member may transfer his governance and information rights only with the consent of all other members.⁶⁷

By contrast, Chapter 322B permits a member to transfer his or her financial rights freely.⁶⁸ Governance rights may be transferred to anyone who is already a member without consent.⁶⁹ Any other transfers are effective only if all members approve the transfer.⁷⁰

Provides Guidance on Oppressive Conduct That Recognizes Member Agreement

In the event of a dispute between the members of the LLC, the New Act permits a court to order dissolution or other remedies (including a forced buy-out).⁷¹ The New Act defines oppressive conduct as conduct that frustrates an expectation of an LLC member that was reasonable in light of the reasonable expectations of the other members, material in the member's decision to become a member of the limited liability company, or for a substantial time has been material during the member's continuing membership and was not contrary

⁶² MINN. STAT. 322C.0301, subdiv. 1 (2015).

⁶³ MINN. STAT. §§ 322C.0302, subdiv. 1; 323A.0303 (2015).

⁶⁴ MINN. STAT. §§ 322C.0302, subdiv. 1, 3 (2015).

⁶⁵ MINN. STAT. §§ 322C.0501; 322C.0502, subdiv. 3(i) (2015).

⁶⁶ MINN. STAT. §§ 322C.0502, subdiv. 1, 5 (2015).

⁶⁷ *Id.*

⁶⁸ MINN. STAT. § 322B.31 (2015).

⁶⁹ MINN. STAT. § 322B.313, subdiv. 2 (2015).

⁷⁰ *Id.*

⁷¹ *Id.*

to the operating agreement.⁷² The intent of the language is to recognize the importance of the agreement between the members and assist courts in resolving the disputes in a way that is consistent with that agreement.

By contrast, Chapter 322B is much more prescriptive in describing when a court may become involved in a dispute and how it may impose equitable remedies.⁷³

Shelf LLCs Permitted; Series LLCs Not

The New Act also brings with it the introduction of Shelf LLCs to Minnesota allowing organizers to formally create LLCs and then leave them to sit inactive (“on a shelf”) to age. Shelf LLCs are an extension of corporate law, which similarly provides for shelf corporations.

Shelf LLCs may be useful because they may save business owners the time involved in creating a new business entity at the moment it is needed. It may also be useful in demonstrating business longevity for the purpose of attracting consumers or investors or positioning a business in the context of a negotiation. Under the New Act, until a LLC has or has had at least one member, the company lacks the capacity to do any act or carry on any activity except filing certain statutorily prescribed filings to the secretary of state, admitting a member and dissolving.⁷⁴ LLCs with at least one member may ratify an act or activity that occurred when the company lacked capacity. The introduction of Shelf LLCs under the New Act (with limitations on what actions that LLC can take prior to having a member) may provide greater flexibility for advance planning for the use of LLCs in business transactions.⁷⁵

Series LLCs were not previously and are still not permitted in Minnesota under the New Act. In a series LLC, a single limited liability company may establish and contain within itself separate series which are each treated as an enterprise separate from one another and from the LLC itself – essentially establishing internal shields so that neither the LLC or the individual series are responsible for the obligations of any one series.⁷⁶ The concept of the Series LLC was introduced in Delaware LLC law and has been adopted by other states, but it is not part of the Revised Uniform Limited Liability Company Act (as promulgated by the Uniform Law Commission in 2006) nor is it part of Minnesota’s New Act.⁷⁷

The Practical Impact of the New Act

The practical impact of the New Act is yet to be realized for many Minnesota LLCs. Critics of the Revised Uniform Limited Liability Company Act, upon which the New Act is based, have expressed concern with, among other things, the overly broad definition of operating agreement, broader fiduciary duties than the traditional duties of loyalty and care and uncertain boundaries on how far those fiduciary duties can be

⁷² MINN. STAT. § 322C.0102, subdiv. 18(3) (2015).

⁷³ MINN. STAT. §§ 322B.833, 322B.836 (2015).

⁷⁴ MINN. STAT. § 322C.0105, subdiv. 2 (2015).

⁷⁵ MINN. STAT. § 322C.0105, subdiv. 3 (2015).

⁷⁶ RULLCA, *supra* note 6.

⁷⁷ *Id.*

modified and unclear rules on the agency power of members and managers.⁷⁸ In Minnesota, the departure from a Board of Governors default management structure (under Chapter 322B) to a member-managed default structure under the New Act raises questions about how many businesses will continue to utilize the Board of Governors structure in the future.

The New Act provides LLC members with more flexibility and less formality in the formation and management of the LLC and a greater ability to customize the business they want by agreement between the members. Yet, LLC's originally established under Chapter 322B may encounter unanticipated problems with the introduction of the New Act. In short, LLC owners may find that their LLC articles, bylaws, operating agreements, and member control agreements, originally formed under Chapter 322B, no longer accomplish precisely what the owners had originally intended.

No two businesses are the same nor are the governing documents for those businesses. The impact of the changes associated with the New Act and how and when those changes should be implemented will, without question, depend on the types of business clients that attorneys practicing in this area represent and what type of governing documents, if any, the LLC has. Attorneys representing majority owners of LLCs may still attempt to draft around the defaults of the New Act because the one owner/one vote principle may seem inequitable to member owners who are contributing the most financially. Yet, for minority owner members of LLCs the default rules in the New Act level the playing field some and provide access to management, voting and increased share of distributions that did not previously exist under the defaults of Chapter 322B. These changes may come at a cost for many Minnesota businesses that may be both financial and operational. Whether most businesses will be inclined to pay those costs or whether the costs are too prohibitive remains to be seen. For clients where cost is an issue, they may choose to continue under Chapter 322B until a change in structure is absolutely necessary for other reasons or until they are automatically converted to the New Act in January 2018. Some businesses may choose not to update any of their governing documents even beyond January 2018 despite the significant changes in the New Act. These businesses should proceed with caution as the default rules of the New Act may have an impact on the day-to-day operations of their business.

Next Steps for Minnesota LLCs and their Attorneys

Minnesota LLCs currently existing under Chapter 322B have a number of choices. Some existing LLCs may require significant revisions to their governance documentation and some may require very little. LLCs may choose to take no action and continue operating under Chapter 322B until January 1, 2018 at which time they will automatically be converted to the New Act or they may choose to be governed by the New Act now either under their existing governance agreement or more likely, an amended operating agreement that accounts for the changes in default rules between Chapter 322B and the New Act.

Attorneys should counsel their client owners of Minnesota LLCs to review and update the documents that govern their business prior to January 1, 2018 to avoid unintended consequences that may impact the day-to-day operations of their business and their legal and financial rights. The timing of those updates will vary by the type of business and the status and specificity of the governing documents that may already be in place.

Prior to January 1, 2018, attorneys should work with their clients to eliminate reliance on the statutory defaults of Chapter 322B that may currently exist within a business' governing documents and

⁷⁸ Larry E. Ribstein, *An Analysis of the Revised Uniform Limited Liability Company Act*, 3 VA. L. & BUS. REV. 35 (2008), <http://ssrn.com/abstract=1003805>.

simultaneously identify and draft for the rights under Chapter 322B that a business wishes to preserve and the elements of the New Act that a business owner wishes to tailor for their business.

Attorneys should also advise clients to create a single operating agreement that consolidates the substantive provisions of previous bylaws, member control agreements and other governing documents as well as any handshake agreements and takes into account the more expansive definition of Operating Agreement in the New Act by including a strong and sound integration clause.

The New Act may also present opportunities for Minnesota businesses that previously opted for a sole proprietorship or general partnership structure (often viewed as among the most informal and flexible), but which did not come with the limited liability or taxation benefits of the LLCs.