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Minnesota's "New" LLC Statute

Way back "in the day", 1992, the Minnesota Legislature rolled the dice betting on the long term success of a limited liability company statute modeled on the Minnesota's existing corporation statute with a few flexible "partnership" type features. The statute worked well, for a time, much like Sony's Betamax videotape. Unfortunately, most of the rest of the country adopted a limited liability company statute modeled more on a partnership structure with a few "corporation" type features. The two statutes battled it out for about two decades. Unfortunately, in 2014 Minnesota threw in the statutory towel and agreed to deep six its corporate oriented LLC statute (i.e., Betamax) in favor of the more popular and accepted partnership oriented LLC statute (i.e., VHS). The old law officially sinks to the bottom of the lake on January 1, 2018, a scant five months from now. What remains is the new "partnership" type statute.

So what? Well, there are hundreds, maybe thousands of Minnesota LLCs organized under the old law which operated just fine for 10 ... almost 20 years. Those LLCs will need their organizational and operational documents (if any) reviewed closely and, if necessary, revised to jive with the owners' existing practices and expectations. Why? Because many old law LLC's were thinly documented relying significantly on the robust fill-in provisions of Minnesota's old law. That old law provided many handy default provisions which usually meshed well with the owners' expectations regarding distributions, voting, indemnification and conflicts of interest. Good times, no more. Those statutory backstops disappear on January 1, 2018. The far less robust, but more flexible, new law will either not have any backstop or will have backstop provisions opposite of the owners' understanding, expectations and practices. For example, if an LLC had bare bones organization with no bylaws, member control agreements or other documentation, the old law filled in a "corporate" style board of governors, a proportionate share of profits and losses based on the number of shares, proportional voting, fairly strict conflict of interest provisions and sweeping indemnification for governors and officers, among other things.

When you wake up on January 1, 2018 and your LLC documents under the old law don't have specific written provisions relating to those items, the new law and the new backstops could vastly change the color of your world. For example, if your old documents are silent about the owner with the most units having the "biggest" vote (proportional voting) or the right to profits/losses (proportional distributions) you are in for some discomfort. Under the new law,



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in the partnership style, every owner has one vote and one share of the profits, no matter how many units that owner owns. So if you formerly were a 90% owner with one 10% co-owner, you ruled the roost. However, on January 1, with respect to voting and profits you two may now be 50%/50% partners. Yikes! Those are the real “day to day” type of changes floating in with the new law.

Under the category of “might be important, might not”, the new law alters several other backstop items as well. For example, the new law ignores pre-emptive rights (previously such rights were included), ignores dissenters rights (ditto) and gives “disassociating” owners no rights to a buy out or a judicial dissolution (again, this was an old law backstop). In addition, the new law eliminates an owner’s strict duty of loyalty to the LLC. The new law allows owners to define the parameters of loyalty; what’s loyal and what’s not. This means that under the old law if an owner of an LLC went to work for a potentially competing business, doing so likely violated the owner’s duty of loyalty. No more. An owner may now be free to do so if the old documents didn’t prohibit it. Backstop gone. It’s not all chaos, however. The new law still imposes a duty of loyalty on managers and owners who must still deal with each other with “good faith and fair dealing.” However, owners may now define exactly what loyalty means as long as it’s not “manifestly unreasonable.”

Winding through these many changes is the new law’s increase tolerance for what constitutes an “operating agreement.” The old law required such an agreement to be in writing. Now, however, almost anything the owners agree to relative to governance, conduct, voting, financial rights and other items relative to the LLC can become part of the operating agreement. Gone is any requirement that the owners’ agreement be written down. Therefore, an “operating agreement” under the new law can be verbal, ticked out in Morse code, exhibited by conduct or glued all together in a wonderful shifting mosaic of paper napkins, emails, voice mails, text messages and open physical behavior. In legal terms, “holy nightmare, Batman.” Really, this is a trial lawyer’s dream and the LLC owners’, well, nightmare.

What to do, what to do? The new law forcibly prods LLC owners to shore up their organizational and operational documents. Therefore, do the following:

1. Determine what your LLC documents currently provide. If they cover everything you do, accurately addresses everything you expect and are signed by everyone, then the LLC might (might!) be okay to “keep calm and carry on.” Many single owner LLC’s fall into this category.



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2. However, in the more likely event the existing documents don't specifically address all those things or aren't signed by all the owners, then the owners will want to sit down and thoroughly go through their reasonable expectations, how the LLC operates, how it addresses management, voting, distribution and governance among many things. With all that done, the owners should create a written "operating agreement" to address everything. And, have everyone sign that agreement.
3. Or, you can take the professional approach and have a professional spend some of her time and some of your money to talk with the owners, the governors (if any), the managers (if any), the accountants and other advisors to create a wonderful, creative, useful, functional, shining star on the horizon "Operating Agreement" to use moving forward. Then, the LLC can get back to business.

Unless you are fond of chaos and thrive on crushed expectations, Minnesota's new law, especially after creating a written operating agreement, should benefit your business. It will address many of the issues the LLC should have addressed in the first place. Owners can formally adopt those things which work well and toss out those that don't. The new agreement will add fair and meaningful boilerplate to address those things that might become really, really important when an owner wants out, acts nuts, disappears, gets sued, dies, gets greedy, takes unreasonable advantage or who knows what else. This new operating agreement will allow the company to run in a businesslike manner with everyone in agreement with the new playbook.

Summed up, spend some time now to carefully look over, or have a knowledgeable professional look over, your LLC documents. Fortify them as necessary, get them in writing, and get everyone to sign off. Don't allow text messages and scribbles on napkins change what you created. Provide a sensible way to change them, if necessary. Protect your LLC from future uncertainty and chaos. Then act like you said you would.

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