

DERIVATIVE ACTIONS AS CODIFIED BY THE RULLCA



By Samantha Buckman

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Counsel faced with potential claims that may be either direct or derivative have always had to use caution to overcome procedural and substantive hurdles. The Minnesota legislature replaced the prior LLC Act (the MLLCA) with the Minnesota Revised Uniform Liability Company Act (RULLCA) in 2014. While the RULLCA preserved many rules, it also codified some longstanding Minnesota LLC common law. One such codification is found in Minn. Stat. § 322C.0902 – Derivative Action.

The old MLLCA did not explicitly grant members of an LLC the right to bring derivative claims on behalf of the LLC. Minnesota courts overcame this statutory deficit by turning to the Minnesota Business Corporations Act, and regularly used both Minn. Stat. Ch. 302A and its supporting case law to guide decisions regarding LLC derivative actions. The RULLCA, particularly §§ 322C.0901 – 322C.0906, is the

codification of this common law.

§ 322C.0902 is now the operative statute governing LLC derivative actions. Its language is both familiar and consistent with prior decisions. It states that an LLC's member is permitted to bring a derivative action to enforce the rights of an LLC if they first make a demand on either the members of a member-managed LLC, the managers of a manager-managed LLC, or the board of governors of a board-managed LLC. *Id.* The action may be maintained if the member, managers, or board do not "bring the action within a reasonable time," or if making such a demand would be futile. *Id.* Although this statute has been effective for nearly a decade, its practical application has been limited, with only two unpublished cases currently citing it.

§ 322C.0902 was first cited by *Poultry Borderless Co., LLC v. Froemming*, No. 20-CV-1054 (WMW/LIB), 2021 WL 354087 (D. Minn. Feb. 2, 2021). Here, the Court analyzed whether an LLC member's claims were direct or derivative, because if derivative, the LLC would have to be joined as an indispensable party. *See id.* The Court affirmed that the RULLCA "permits an LLC member to bring a derivative action to enforce a right of a limited liability company." *Id.* at *4. The Court then assessed the nature of the alleged injury using the substantive test laid out by the Minnesota Supreme Court in 2017. *Id.* at *5 (citing *In re Medtronic, Inc. Shoulder Litig.*, 900 N.W.2d 401 (Minn. 2017)). Using this test, the Court held that the member's claims relating to mismanagement of the LLC and breaches of fiduciary duties were derivative claims. *Id.* at *6. Because the LLC would then be indispensable party, diversity jurisdiction was destroyed, and the claim was dismissed for lack of subject matter jurisdiction. *Id.* at *7.

The next—and latest—case to use § 322C.0902 is *Novak v. Miller*, No. A22-1164, 2023 WL 2847207 (Minn. Ct. App. Apr. 10, 2023). Here, the LLC was not named as a party in the complaint, and the Plaintiff-member never made a demand on the LLC

before commencing the action. *See id.* The Court in *Novak* then clarified the requirements to bring a claim under the RULLCA: just as with corporate derivative actions, and as with LLC derivative actions prior to the RULLCA, Plaintiff-members must still comply with the derivative action pleading requirements of Minn. R. Civ. P. 23.09. *Id.* at *3. The Court found that not only did the parties try the case as though the pleading requirement had been met—thus adequately meeting the pleading standard as described in *Winter v. Farmers Educ. & Co-op. Union of Am.*, 107 N.W.2d 226, 232 (Minn. 1961)—but the Plaintiff-member made sufficient allegations to demonstrate a demand on the LLC's sole other member would have been futile. *Id.* The Court concluded "the parties litigated this case as if the conditions for a derivative claim had been met," under both § 322C.0902 and Minn. R. Civ. P. 23.09. *Id.*

These cases, limited though they may be, indicate that the RULLCA and § 322C.0902 are interpreted consistent with previous common law rules. The substantive question of whether a claim is direct or derivative has not changed, and the facts are assessed using the test enunciated in prior Minnesota case law. Further, a member must either make a demand on the proper party or indicate that a demand would be futile, and this process should be reflected in the pleadings per the requirements of Rule 23.09. The RULLCA thus far appears to be a source of consistency and certainty that mirrors prior case law, and it is also a fresh reminder for counsel to ensure that LLC derivative actions comply with the now-codified procedural requirements and the long-standing substantive requirements.

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