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## Non-compete agreements: Wisconsin Supreme Court rules that continued employment is lawful consideration

On April 30, 2015, the Wisconsin Supreme Court ruled that continued at-will employment constitutes lawful consideration to support an otherwise reasonably drafted restrictive covenant agreement signed by a current employee. *Runzheimer International, Ltd. v. David Friedlen and Corporate Reimbursement Services, Inc.*, 2015 WI 45. Thus, if an employee is told he/she will be terminated unless he/she signs a non-competition agreement, valid consideration exists for the restrictive covenant agreement if the employee executes the agreement. No additional monetary payments or other consideration is necessary. This case was successfully argued by Godfrey & Kahn, S.C. and represents a big win for employers.

### Background

The Defendant in this case was David Friedlen. Friedlen was an at-will employee at Runzheimer International, Ltd. Runzheimer hired Friedlen in 1993. Throughout his career, Friedlen participated in Runzheimer's yearly bonus incentive plan.

In 2009, Runzheimer required all employees to sign a restrictive covenant. Friedlen's supervisor permitted Friedlen to review the restrictive covenant for two weeks, but told him that if he did not sign the agreement by the end of that time, his employment would be terminated. Friedlen's participation in Runzheimer's bonus incentive plan for that year also was contingent on his signing the restrictive covenant. Friedlen signed the restrictive covenant on June 15, 2009. He received more than \$20,000 in 2009 from Runzheimer's incentive plan in addition to his regular compensation. Runzheimer employed Friedlen for 29 months after he signed the restrictive covenant.

Following his termination, Friedlen was hired by a competitor, and Runzheimer filed an action against Friedlen and his new employer to enforce the terms of the restrictive covenant agreement. Friedlen and his new employer defended the claim by arguing that the agreement was otherwise unenforceable because it was not supported by adequate consideration.

On May 14, 2013, the Circuit Court granted the defendants' motion for summary judgement related to the breach of the restrictive covenant agreement. The Circuit Court held that an employer's offer of continued at-will employment to support a non-competition agreement with an existing employee was "illusory" and thus invalidated the agreement.

Runzheimer appealed this decision on June 19, 2013. Recognizing that this issue has not been squarely addressed in Wisconsin and citing potentially conflicting case law, the Court of Appeals certified the case to the Wisconsin Supreme Court on the narrow, but

immensely important, issue of whether “consideration in addition to continued employment [is] required to support a covenant not to compete entered into by an existing at-will employee.”

## The decision

The Supreme Court drafted a very thorough and thoughtful response. In its decision, the Court began its analysis by confirming existing precedent that establishes that the promise of new employment at the beginning of the employment relationship is lawful consideration even though the employer is free to terminate the employment relationship at any time thereafter. The Court then acknowledged the practical differences between a new employment relationship and an existing employment relationship, which was the focus of the case.

The Supreme Court went on to clarify existing Wisconsin case law regarding lawful consideration to support a covenant not to compete entered into with a current employee. The Court rejected the defendants’ argument that the 2009 decision in *Star Direct, Inc. v. Dal Pra*, 2009 WI 76, already established that continued employment is not sufficient consideration. The Court emphasized that the discussion in *Star Direct* regarding requiring current employees to execute restrictive covenants merely reiterated existing case law that required additional consideration to support such a covenant; however, the *Star Direct* decision did not address whether continued at-will employment satisfied the additional consideration requirement in such a context.

After establishing the absence of precedent regarding the issue at hand, the Court evaluated how other jurisdictions have addressed this issue. Currently, the states are split as to whether continued employment alone will support a restrictive covenant. The Court pointed out that the states that do not find continued employment to form sufficient consideration are in the “distinct minority.” In siding with the *majority*, the Court held that an employer’s promise to continue to employ an at-will employee is lawful consideration in Wisconsin. Specifically, the Court asserted that:

[A]n employer’s forbearance in exercising its right to terminate an at-will employee constitutes lawful consideration for signing a restrictive covenant.

The Court specifically rejected the Circuit Court’s analysis that continued employment is “illusory consideration,” and therefore not lawful consideration, merely because an employer can terminate the employee in the future pursuant to the principles of at-will employment. Rather, the Court reasoned that the promise not to fire an existing at-will employee at that time in exchange for an employee immediately signing a restrictive covenant is forbearance in exercising a legal right and therefore lawful consideration.

Although the Court could have ended its analysis there, the Court continued on and asserted that it is of no consequence whether the duration of continued employment is expressly stated and/or whether the employment relationship, in fact, continues on for a period of time. The Court likely included this clarification in recognition of Justice Abrahamson’s concurrence. The Court distinguished that its analysis is related to the question of whether *lawful* consideration has been provided to support a contract—not whether the consideration is *adequate*. In fact, early on in its decision, the Court clarified via footnote that it would use the term “lawful consideration” instead of “sufficient consideration” to differentiate the existence of consideration from the adequacy of consideration.

Thus, continued at-will employment, without more (*i.e.*, without additional monetary or non-monetary benefits), is lawful consideration. The sufficiency of consideration; however, is an issue that the courts left to the parties to the contract to evaluate for themselves.<sup>1</sup>

## Additional guidance

The decision also included two important directives to employers and employees. First, in Wisconsin, an employee may bring a “wrongful discharge” claim if the discharge is contrary to “a fundamental and well-defined public policy as evidenced by

existing law.” The Court made clear that an employee who is terminated for failing to sign a restrictive covenant will not have a claim for wrongful discharge on that basis. As explained by the Court, employers may respond to and reduce the risk of employees competing and taking business from the employer by requiring employees to sign reasonable restrictive covenants. Thus, employers may lawfully terminate an employee for failing to sign a restrictive covenant.

Second, the Court emphasized that employers remain subject to the long-standing principles of contract formation, such as fraudulent inducement and the covenant of good faith and fair dealing. Accordingly, employers may not misrepresent their intention to continue to employ the employee. An agreement signed by an employee who is terminated by the employer shortly thereafter could constitute a breach and make the agreement unenforceable.

## Pending legislation

The Wisconsin legislature is currently considering legislation that would repeal and recreate Wisconsin Statute 103.465, the law currently governing restrictive covenant agreements in the state. If passed, the rewritten statute would implement broad, sweeping changes to Wisconsin non-competition law. For example, the bill creates rebuttable presumptions relating to the reasonableness of time restriction periods placed on the restrictive covenants.

Both the Senate bill and the companion Assembly bill are pending consideration in their respective committees. It is unclear what effect the *Runzheimer* decision will have on the status of this legislation. However, this decision has effectively addressed a key component of the new legislation which specifically provides, via statute, that continued employment is lawful consideration. While it was originally anticipated that the legislation would be a priority for passage, this decision could reduce the momentum behind the bill.

## The takeaways

- Employers who wish to rely solely on continued employment to support a restrictive covenant agreement with an active employee must: (1) condition continued employment on the signing of the agreement; and (2) be prepared to immediately carry out the employee’s termination if they fail to sign. To ensure that all parties understand that continued employment is conditioned upon execution of a restrictive covenant agreement, employers should communicate the consequences of not signing to the employee, preferably in writing.
- Before an employer rolls out new restrictive covenants to its entire workforce, the possible business implications of employees’ refusal to sign such covenants should be considered. If an employer is not prepared to fire an employee for refusing to sign a non-competition agreement, it should consider offering additional consideration to incentivize execution.
- The *Runzheimer* decision did not address the enforceability of the underlying restrictions and Wisconsin courts continue to maintain very high standards of reasonableness with respect to the scope and duration of restrictive covenants. Accordingly, it continues to remain imperative that employers thoughtfully draft covenants with reasonable restrictions.
- Employers should not require employees to sign agreements shortly before a planned termination or reduction in force without providing consideration in addition to the promise of continued employment.
- Employees who have signed agreements based solely on continued employment may be emboldened to bring traditional contract claims to challenge the agreement once they are terminated. For example, an employee may argue that the employer never intended to “forebear” their right to terminate and required the employee to sign it knowing all along that the employee would be terminated in the near future.
- Additional issues will likely be raised in circuit courts in the years to come. For example, the Court intentionally did not provide a bright line rule as to the length of time an employee must be employed after signing the agreement to avoid the aforementioned contract claims, stating only that such claims would exist if the employee is fired a short time after signing the agreement.
- Although new legislation would likely broaden the protections an employer may seek, the legislation may be stalled or not pass. As a result, employers should balance their need for entering into an agreement against the potential benefits of waiting for the legislation to pass.

The *Runzheimer* decision has provided long-awaited and much-needed clarity to the issue of whether continued at-will employment (without the promise of additional benefits) can be used as lawful consideration. The Court's decision provides employers additional freedom to enter into restrictive covenant agreements with current employees who may have developed specialized skills in knowledge throughout their career with the employer. However, as noted above, this decision is not a green light for employers to implement non-competition agreements with *all* active employees. Careful consideration must be given to such decisions.

Please contact a member of the Godfrey & Kahn Unfair Competition & Trade Secrets or Labor, Employment & Immigration Practice Groups with questions or for more information.

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<sup>1</sup>As the lower court invalidated the Runzheimer restrictive covenant agreement based only on its determination that the agreement was not supported by adequate consideration, the Supreme Court remanded the case so that the Circuit Court could determine if the terms of the agreement were reasonable.

*The information in this article is based on a summary of legal principles. It is not to be construed as legal advice. Individuals should consult with legal counsel before taking any action based on these principles to ensure their applicability in a given situation.*