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NOTICE TO DEALERS

RE: ***Guidance Regarding Compliance with the Department of Labor's New Overtime Rule Effective December 1, 2016***

As dealers are aware through communications from multiple sources, earlier this year the Department of Labor finalized its Regulations updating and implementing exemptions from minimum wage and overtime pay for executive, administrative and professional employees ("White Collar Workers"). Since all employees are entitled to be paid the minimum wage, this Notice will not address that topic. Rather, it will only address guidance on what dealers need to do to comply with the new Overtime Requirements Rule prior to its effective date of December 1, 2016.

OVERVIEW OF THE NEW RULE

The Final Rule focuses primarily on updating the salary and compensation levels needed for White Collar Workers to be exempt. Specifically, the Final Rule:

1. Sets the new standard salary level at the 40th percentile of earnings of full-time salaried workers in the lowest region of the country, which is $913.00 per week or $47,476.00 annually (an increase from the current $455.00 per week or $23,660.00 annually). For those dealers who pay employees biweekly, the required amount is $1,826.00 per pay period; for those dealers who pay semi-monthly it is $1,978.00 per pay period; and for those dealers who pay monthly, the new salary level is $3,956.00 per month.

2. Sets the total annual compensation requirement for highly compensated employees to $134,004.00 (previously $100,000.00). These employees must also receive at least $913.00 per week.

3. Establishes a mechanism by which the salary and compensation levels above will be automatically updated every three (3) years to maintain the levels of the above percentiles, commencing on January 1, 2020.

4. Amends the salary basis test to allow employers to use nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10% of the new standard salary level ($91.30 per week). This requirement must be met quarterly.

5. Permits a "CATCH-UP" payment at the end of each quarter to ensure compliance.

MYTHS ABOUT THE NEW OVERTIME RULE

Based on our conversations with some of our clients, there are some apparent misunderstandings as to the effect of this Rule on dealership employees.

MYTH NO. 1: The Rule changes how I must pay salespersons, partsmen and mechanics.

NOT TRUE. The new Rule only affects white collar salaried workers. It does not change the other overtime exemptions dealerships have long claimed such as those for salespeople, service writers, partsmen and mechanics/technicians. It also does not change the dealer's ability to claim the overtime exemption for those employees who receive more than half (½) their earnings through commission and are paid at least one and a half (1½) times the minimum wage (commonly known as the Retail Commission Exemption).

The Rule also does not affect the Business Owners Exemption which provides that an employee that owns at least a bona fide twenty percent (20%) equity interest in a business is exempt from overtime requirements provided he/she is actively engaged in the management of the business.

MYTH NO. 2: Employees who receive a salary are automatically exempt.

NOT TRUE. Salaried status and exempt status are SEPARATE concepts. Paying an employee a salary does not mean the employee is automatically exempt. The employee must still meet the duties test described below **and** also receive a salary of at least $913.00 per week.

MYTH NO. 3: Supervisors and managers are automatically exempt.

NOT TRUE. An employee's job title is irrelevant in terms of complying with the overtime rule. The fact that an employee is a manager or supervisor does not mean the dealer can automatically claim an exemption for that employee. As with salaried personnel, the supervisor/manager must still meet the duties test **and** be paid at least $913.00 per week in salary.

MYTH NO. 4: Outside salespersons must be paid in compliance with the new Rule.

NOT TRUE. An exempt outside salesperson must be customarily and regularly engaged away from the dealership and have a primary duty of making sales or obtaining orders or contracts. There are no salary or fee requirements for exempt outside sales employees.

MYTH NO. 5: The Rule only applies to full time employees.

NOT TRUE. Whether an employee is full-time or part-time, the standard salary level to qualify for the exemption is $913.00 per week. The salary level may not be prorated for part-time employees. However, dealers may prorate the required salary if an employee works less than the full week of his/her first and/or last week of employment.

MYTH NO. 6: Paying an employee $913.00 per week in salary satisfies the exemption.

NOT TRUE. While payment of $913.00 per week is one (1) part of the equation, standing alone, it does not satisfy the exemption. Dealers must also "guarantee" that the employee will receive that amount weekly **and** the employee must meet the duties test outlined below.

MYTH NO. 7: Dealers will have to change the job descriptions of White Collar employees to comply with the new Rule.

NOT TRUE. The revised Rule does not make any changes to the duties tests under which dealers have been operating since the Rule was last amended in 2004. Salaried workers who are guaranteed and earn at least $913.00 a week will be exempt from overtime pay if they meet the appropriate test for the two (2) classifications most common at dealerships: Executive and Administrative.

- ***Executive Exemption.*** To qualify for executive employee exemption, **all** the following tests must be met:

    - The employee must be compensated on a salary basis at a rate not less than $913.00 per week;

    - The employee's primary duty must be managing the enterprise or managing a customarily recognized department or subdivision of the enterprise;

    - The employee must customarily and regularly direct the work of at least two (2) or more other full-time employees or their equivalent; and

    - The employee must have the authority to hire or fire other employees or the employee's suggestions and recommendations as to the hiring, firing, advancement, promotion or any other change of status of other employees must be given particular weight.

    - This exemption would normally include General Managers and Department Managers.

- ***Administrative Exemption.*** To qualify for the administrative employee exemption, **all** the following tests must be met:

    - The employee must be compensated on a salary basis at a rate not less than $913.00 per week;

    - The employee's primary duty must be performance of office or non-manual work directly related to the management or general business operations of the employer or the employer's customers;

    - The employee's primary duty includes the exercise of discretion and independent judgment with respect to matters of significance; and

- This exemption would normally apply to dealership assistant managers and office managers but not to clerks, cashiers, secretaries or other office personnel involved in bookkeeping, payroll or clerical matters.

➢ A third exemption for highly compensated employees will also apply to dealerships. To qualify for this exemption, all the following must be met:

- Highly compensated employees must perform office or non-manual work;

- The employee must be paid total annual compensation of $134,004.00; and

- The employee must be paid at least $913.00 per week in salary.

IMPACT OF THE RULE

While experts may debate how the Final Rule impacts dealers, there are two (2) effects upon which everyone agrees:

1. Fewer employees will qualify for exempt status and will need to be converted to non-exempt status and paid overtime; and

2. In order to preserve some exempt classifications, dealers will need to increase employees' salaries to meet the new salary thresholds.

PRACTICAL RECOMMENDATIONS FOR DEALERSHIP COMPLIANCE WITH THE NEW RULE

The Final Rule goes into effect on December 1, 2016. Therefore, dealers have less than three (3) months to ensure they are in compliance with the revised Rule. The overtime changes will apply to you if you have any employees who are paid on a salary basis and for whom either of the following statements is true:

➢ Their salary falls between $23,660.00 and $47,476.00 per year and they meet the job duties exemption requirements; or

- ➢ Their salary/compensation falls between $100,000.00 and $134,004.00 per year and they meet the highly compensated employee job duties exemption requirements.

Beginning December 1st, employees who receive less than $913.00 per week in salary are considered non-exempt and must be paid at least the minimum wage and overtime. Employees who are paid a salary of at least $913.00 per week and perform job duties that fall within either the administrative or executive category may be classified as "exempt." If an exemption no longer applies (i.e., the employee no longer performs certain job duties or earns less than $913.00 per week), the employee should be promptly reclassified as "non-exempt" and paid overtime in accordance with Federal and State law. For employees who are properly classified as exempt, dealers should make sure that their job description accurately reflects current responsibilities.

To prepare for the Final Rule, dealers should:

- ★ Audit all currently exempt positions to determine whether they will meet the new salary requirements (as well as well as the unchanged duties tests). Start by answering these questions:
  - How many of your employees will be newly classified as non-exempt?
  - How many of them routinely work more than 40 hours a week?
  - What would it cost you if they continue to work more than 40 hours per work week and are eligible for overtime?
  - What systems do you need to put in place to monitor employees' hours carefully after the new Rule goes into effect? The Department of Labor permits any method employers choose for tracking and recording hours as long as it is complete and accurate.
- ★ If, after your audit is complete you determine that any of the positions will fail to be exempt under the Final Rule, you need to decide whether changes are needed:
  - If a currently exempt position does not typically work more than 40 hours in a work week, there may be no practical need to adjust the position's salary. The loss of the exemption – and the corresponding need to pay

workers in that position at overtime rates when they work more than 40 hours in a work week – should be consequential only occasionally – if at all. If this position NEVER works overtime, the Final Rule will have no impact on their pay even though they become overtime protected. They can continue to be paid on a salary basis as before;

- Similarly, if a dealer is concerned that some employees will be unhappy losing their status as "salaried," the dealer can continue to treat the employees as "salaried non-exempt." This means they can continue to receive their fixed salaries for working up to 40 hours in a work week but they also must receive pay at overtime rates when they work more than 40 hours in a work week (using their salaries and other compensation to determine their overtime rate); and

- If, however, the position typically works more than 40 hours in a work week, then the dealer must increase the compensation to meet the new salary thresholds in order to remain exempt.

★ Dealers have a range of options for responding to the updated salary level. For each affected employee newly entitled to overtime, dealers may:

1. Increase the salary of an employee who meets the duties test to at least the new salary level ($913.00 per week) to retain his/her exempt status. For most dealerships, only a lucky few should expect this outright raise.

   a. Determine whether you want to take advantage of the provision of the Rule which allows nondiscretionary bonuses and incentive payments (including commissions) to satisfy up to 10% of the standard salary test requirement. Such bonuses include, for example, nondiscretionary bonuses tied to profitability and commission payments based on a fixed formula. The payments must be made on a quarterly or more frequent basis.

   b. If you determine the bonus/commission payments apply to a given employee, you may take advantage of the provision by paying the employee 90% of the standard salary level (approximately $822.00 per week) and the remaining 10% of the standard salary level (approximately $91.00 per week) in the form of a bonus or commission payment.

c. If you choose this method of payment, the Rule also allows you to make a "Catch-Up" payment in the event the employee does not receive enough in nondiscretionary bonuses/commissions in a given quarter to remain exempt. The dealer can make the "catch-up" payment at the end of the quarter. The dealer has one (1) pay period to make up for the shortfall (up to 10% of the standard salary level for the preceding 13 week period). That catch-up payment will only count toward the prior quarter's salary amount. If the dealer chooses not to make the catch-up payment, the employee would then be entitled to overtime for any overtime hours worked during the quarter.

2. Pay an overtime premium of one and a half (1½) times the employee's regular rate of pay for any overtime hours worked. This is done by converting the salaried worker to hourly work at a rate determined by dividing the current salary by 40 hours. If these employees work overtime, their overall compensation will rise;

3. Reduce or eliminate overtime hours by reorganizing workloads, adjusting schedules or spreading work hours;

4. Reduce the amount of pay allocated to base salary (provided that the employee still earns at least the minimum wage of $8.50 per hour) and add pay to account for overtime hours worked over 40 in the work week, to hold total weekly pay constant; or

5. Use some combination of these responses.

The circumstances of each affected employee will likely impact how dealers respond to the rule.

★ Clearly communicate any compensation and classification changes to affected employees in advance. It will not be easy telling an employee who has long been salaried, never had to punch a timecard and often worked after hours that this is all going to change. It is also a safe bet that your employees will have heard about the impending Rule change and they will be looking for you to answer questions about how it will affect them. For most dealers, it is probably wise to begin engaging employees on the topic now even if you have not mapped the details of how you will respond. An honest "We're figuring this out" answer can be better than silence since there may be discussion among workers about the changes and how the changes impact them. Therefore, communication strategies must be considered to minimize morale problems (or worse) as a result of, for example, workers being moved from salary to hourly positions.

Many people attach great importance to their status as salaried exempt workers. In addition, depending on the new hourly approach views, the formerly exempt workers who work long hours may be quite surprised to learn their new hourly rate is lower than they expected. Also, as workers compare notes with each other about their old and new compensation, there is a risk that people in protected classes (race, color, religion, national origin, gender, age, etc.) may believe that their pay is unfair or discriminatory. These changes therefore present dealership management an opportunity to review their company's payroll practices to minimize existing risk as well as future risk. Now is the time to plan for these changes.

★ Train employees whose positions were converted from exempt to non-exempt on timekeeping and overtime procedures and policies. Many exempt employees have been used to coming and going from the dealership without ever punching a clock or recording their time. That will change if a dealer determines that a formerly exempt employee is now non-exempt. Employees must be advised of that change and trained in the use of either a timeclock or timecards.

★ Make changes in payroll processing and information technology systems to properly convert employees to non-exempt.

PENALTIES FOR NONCOMPLIANCE

If a dealership fails to pay overtime in accordance with the new Rule, the Department of Labor may bring suit for back wages and an equal amount of liquidated damages, going back two (2) Years. If the dealer's violation is willful, the back pay period is three (3) years. Depending on the severity of the dealership's violations, it may also be subject to substantial civil penalties. In addition, in recent years, FLSA cases have become very attractive to plaintiffs' employment lawyers. The employee can retain an attorney to file a private lawsuit for back pay and liquidated damages plus attorney fees and court costs. And, depending upon the employer and the number of employees involved, the dealership could be subject to an expensive class action.

CONCLUSION

Dealers have until December 1, 2016 to comply with the new Overtime Rules. Dealers should begin to implement the necessary changes in order to comply with the Rule and be prepared to address questions employees may have related to timekeeping and pay. We have attached an Overtime Rule Flow Chart to help you to initially prepare for the Overtime Rule. If you need assistance determining how to comply with the new salaried overtime requirements, please do not hesitate to contact a member of our Dealer Practice Group.

Very truly yours,

COLOMBO & COLOMBO

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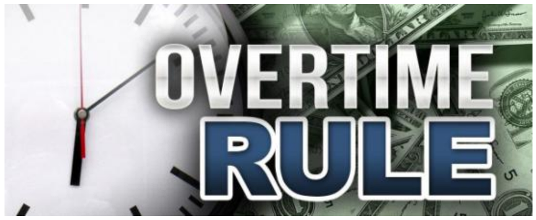
September 2016



HOW TO PREPARE FOR THE FINAL OVERTIME RULES

Is the employee currently classified as non-exempt or exempt from overtime under the FLSA?*

- **NON-EXEMPT**
  - No action required
- **EXEMPT**
  - Is the employee classified under the highly compensated employee exemption or the administrative, professional, or executive employee exemption?
    - **ADMINISTRATIVE, PROFESSIONAL OR EXECUTIVE EMPLOYEE**
      - Does the employee meet the [duties tests] for the exemption? While the final rules did not make changes to the duties tests, now is a good time to confirm the employee still meets the duties tests
        - **YES**
          - Does the employee earn a weekly salary of at least $913?
            - **YES**
              - No action required
            - **NO**
              - To comply, generally you will need to either: (1) raise their salary to at least $913 per week; or (2) reclassify the employee as non-exempt and pay overtime when due
        - **NO**
          - Reclassify the employee as non-exempt and pay overtime whenever he/she works more than 40 hours in a workweek
    - **HIGHLY COMPENSATED EMPLOYEE**
      - Does the employee meet the [duties tests] for the exemption? While the final rules did not make changes to the duties tests, now is a good time to confirm the employee still meets the duties tests
        - **YES**
          - Is the employee's total annual compensation at least $134,004?
            - **YES**
              - No action required
            - **NO**
              - To comply, either: (1) raise their total compensation to $134,004 per year; or (2) reclassify the employee as non-exempt and pay overtime when due
        - **NO**
          - Reclassify the employee as non-exempt and pay overtime whenever he/she works more than 40 hours in a workweek

*Under the FLSA, non-exempt employees must be paid at least the minimum wage for each hour worked and overtime whenever they work more than 40 hours in a workweek. To be classified as exempt from these requirements, an employee must generally: (1) be paid on a salary basis; (2) meet the minimum salary requirement; and (3) satisfy certain duties tests. Note: The outside sales employee exemption is not impacted by the final rules.