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NOT TO BE PUBLISHED

Commonwealth of Kentucky

Court of Appeals

NO. 2006-CA-001702-MR

KROGER LIMITED PARTNERSHIP I, d/b/a
KROGER L-347 APPELLANT

v.

APPEAL FROM FAYETTE CIRCUIT COURT
HONORABLE THOMAS L. CLARK, JUDGE
ACTION NO. 05-CI-03324

CABINET FOR HEALTH AND FAMILY
SERVICES, COMMONWEALTH OF
KENTUCKY APPELLEE

OPINION
AFFIRMING

** ** ** ** **

BEFORE: COMBS, CHIEF JUDGE; NICKELL AND WINE, JUDGES.

NICKELL, JUDGE: Kroger Limited Partnership I, d/b/a Kroger L-347 ("Kroger"), appeals from a July 26, 2006, opinion and order of the Fayette Circuit Court upholding an order of the Secretary ("Secretary") of the Cabinet for Health and Family Services ("Cabinet") which disqualified Kroger from participating as a vendor in the Special Supplemental Nutrition Program for Women, Infants and Children ("WIC") for one year.

The disqualification resulted from Kroger cashiers allowing WIC participants to redeem food instruments for unauthorized items on five separate occasions. We now affirm.

WIC is a federally funded program providing nutrition services to eligible pregnant, breast-feeding and postpartum women, infants and children. A staple of the program is a system of food instruments issued to participants through local health departments. These food instruments are used by participants in lieu of cash to purchase specified foods from vendors who have entered into a one-year contract with the Cabinet. Vendors submit redeemed food instruments to a centralized bank account from which they are reimbursed. The vendor agreement, renewable annually, sets forth the responsibilities of both the vendor and the Cabinet. By signing the contract, the vendor agrees to: comply with all state and federal policies, procedures and regulations;[1] dispense "only approved food items in the quantities and sizes which have been specified" on the food instruments; not redeem vouchers for "unauthorized foods"; permit monitoring and inspection of "store premises and all documents necessary to ensure compliance with the Agreement and State and Federal WIC Program rules, regulations and policies"; send employees to annual training; and be accountable for the actions of its employees in the handling of WIC food instruments. Attached to the vendor agreement is a list of WIC "approved" food items; a list of specific foods and minimum quantities each vendor must keep in stock (including "Carnation Good Start, Follow-Up or Alsoy in 13-

[1] 7 Code of Federal Regulations ("C.F.R."), Part 246; 902 Kentucky Administrative Regulations ("KAR") 4:040, Section 10.

ounce size concentrate"); and a copy of 902 KAR 4:040 which explains the application, participation, sanction and hearing processes utilized by the WIC program. Under the vendor agreement, the Cabinet must monitor vendor performance, inform vendors of monitoring results, and provide vendors "training and written instructions on the Program's operations."

Kroger L-347 is located at 4104 Tates Creek Pike in Lexington, Kentucky. On September 13, 2002, Peggy Thorndale, the store's Assistant Customer Service Manager, attended statewide WIC training conducted in Lexington by Cabinet representatives Nancy Sullivan and Cindy Sullivan. This training stressed the recurring problem of vendors across Kentucky allowing WIC participants to purchase powdered infant formula when concentrate formula[2] was specified on the food instrument. As borne out by the printed materials distributed during training, vendors are to redeem food instruments only for the item(s), sizes and quantities specified on the vouchers; no substitutions are allowed.

On October 1, 2002, Kroger L-347 executed a vendor agreement indicating its desire to be a WIC vendor during the October 1, 2002 through September 30, 2003 Fiscal Year and its willingness to be bound by the terms of the WIC Program. Twice in October 2002, at Kroger's request, Nancy Sullivan, the Vendor Monitor assigned to the store by the Cabinet, conducted in-store cashier training. This request was prompted by Kroger's receipt of a letter notifying the store it had overcharged the WIC Program for

[2] Since 1983 the Cabinet has equated "concentrate formula" with liquid formula.

redeemed food items on two occasions. In addition to the annual training Thorndale attended in September 2002, and the in-store cashier training Nancy Sullivan conducted in October 2002, Kroger Customer Service Manager DeLee Craycraft testified that all Kroger cashiers are retrained on WIC procedures every 28 days. Part of the in-house training includes the directive that food substitutions are forbidden. Upon receiving a food instrument, cashiers are to verify the date; locate the Kentucky WIC agency stamp on the instrument; verify that the foods selected by the participant are authorized by the food instrument; if the types and quantities of foods selected are authorized, enter the "pay exactly amount" on the instrument and have the participant sign the food instrument. Participants are allowed to purchase less than the quantity listed on the food instrument but never more.

Despite the foregoing training, Kroger overcharged the Cabinet for food instruments redeemed in September 2001, January 2002, and May 2002. As a result of these overcharges, by February 12, 2003, the Cabinet referred the store to the Office of the Inspector General ("OIG") for investigation.[3] After receiving instructions and "decoy" food instruments from the Cabinet, Rebecca Rose, a Program Investigative Officer with the OIG, visited Kroger L-347 on April 14, 2003; April 25, 2003; May 6, 2003; May 16, 2003, and May 30, 2003. Each time she attempted to make a compliance buy and each time she was successful. A compliance buy is "a covert, on-site

[3] Kroger L-347 was one of sixty-five stores referred for investigation by the Cabinet in FY 2003.

investigation in which a representative of the WIC Program: (a) Poses as a participant; (b) Engages in a transaction involving one (1) or more food instruments; and (c) Does not reveal before, during, or after the visit, that he or she is a program representative." 902 KAR 4:040 Section 1(5). Pursuant to 7 C.F.R. Section 246(l)(iv), any vendor failing five compliance buys must be disqualified from the WIC Program for one year for engaging in "a pattern of providing unauthorized food items in exchange for food instruments. . . ."

During each of the five compliance buys, Rose presented the cashier a food instrument allowing her to purchase multiple cans of "13 oz. Concentrate Good Start or Alsoy" infant formula and multiple containers of infant juice. Three of the food instruments also allowed Rose to purchase infant cereal. Each time a cashier permitted Rose to substitute 12-ounce or 14-ounce cans of powdered infant formula for the "13 oz." cans of concentrate formula specified on the food instrument.[4] This substitution was allowed even though vendors and cashiers were trained to compare the quantity and type of foods selected with the items specified on the food instrument as well as on the WIC approved food list that is placed at every cash register. Cashiers were also trained not to make any substitutions. Nancy Sullivan testified she believed two of the cashiers who redeemed the food instruments for unauthorized items during the compliance buys had

[4] During the May 16, 2003, compliance buy, Rose signed the food instrument before the "pay exactly" amount was entered on the instrument. This is inconsistent with the WIC Program redemption protocol which requires the "pay exactly" amount to be entered on the food instrument before obtaining the signature of the person redeeming the food instrument. The Cabinet has chosen not to take any action regarding this error.

participated in the additional training she personally conducted in the store in October 2002.

On October 1, 2003, citing 902 KAR 4:040 Section 12(1)(n), the Cabinet notified Kroger it had failed five compliance buys and was being disqualified from the WIC Program for one year beginning November 3, 2003.[5] Thereafter, Kroger timely requested an administrative hearing which was held January 20 and 21, 2005. Live testimony was offered by both the Cabinet and Kroger. The Administrative Law Judge ("ALJ") sought to resolve two issues: did Kroger redeem WIC instruments for unauthorized food items and would Kroger's disqualification from the WIC Program for one year be consistent with 902 KAR 4:040.

After both parties filed proposed findings of fact, conclusions of law and recommended orders, the ALJ issued his own findings, conclusions and recommended order. He concluded in relevant part: the Cabinet must conduct compliance investigations of its vendors to determine whether they are adhering to WIC Program requirements and to collect evidence of wrongdoing, if any; the Cabinet must establish a violation by a preponderance of the evidence; 902 KAR 4:040 Section 12(1)(n) mandates a one-year disqualification from the WIC Program for any vendor who on five occasions provides unauthorized food items in return for a food instrument; intent is irrelevant in determining whether a violation has occurred; before disqualifying a vendor, the Cabinet

[5] The disqualification has been stayed pending appeal.

must assess whether such disqualification would result in inadequate access to the WIC Program by participants; pursuant to 7 C.F.R. 246.18(a)(1)(iii)(B) and 902 KAR 4:040 Section 11(2)(b), the Cabinet's determination of adequate participant access is not subject to administrative review; Kroger was not denied due process by the Cabinet's classification of it as a high-risk vendor[6] since all vendors, whether designated high-risk or not, are subject to compliance buys at any time; as part of the vendor contract Kroger signed, it agreed to be liable for the actions of its cashiers and therefore was responsible for their scanning of groceries and allowing participants to purchase unauthorized food items with food instruments; and finally, Kroger employees who attended the mandatory annual training provided by the Cabinet were obligated to return to the store and train all other cashiers on how to distinguish a thirteen-ounce can of infant formula from twelve-ounce and fourteen-ounce cans of formula. The ALJ declined to address several arguments raised by Kroger because they were without merit. He also rejected as unpersuasive Kroger's assertion of several affirmative defenses, namely, lack of notice,

[6] A high-risk vendor is "a vendor having a high probability of violating a WIC Program requirement, as identified by use of criteria established by federal regulation or the state agency." 902 KAR 4:040 Section 1(9). Kentucky assigns points to vendors for WIC violations. These include ten points for each overcharge letter sent during a single fiscal year, one point for each letter or notice sent for redeeming a food instrument outside its date of issuance, and one point for redeeming more than $2,000 in food instruments from "outside its contract area." There was also testimony about points being issued for a "high variance"; however, the number of points issued and the conduct triggering assessment of such points was not explained on the record. Thirty points in a fiscal year is the threshold for being designated a high-risk vendor in Kentucky. High-risk vendors, in descending order of points, are the most likely to be investigated during the Cabinet's monitoring efforts. Kroger was assessed thirty points for receiving three overcharge letters and one point for redeeming more than $2,000 in food instruments from outside its contract area.

civil entrapment, equal protection and equitable estoppel.

Ultimately, the ALJ concluded the Cabinet had established by a preponderance of the evidence that Kroger had violated 902 KAR 4:040 Section 12(1)(n) by failing five compliance buys in which cashiers allowed an undercover officer to buy food that was not authorized by food instruments. Further, since the Cabinet had determined removing Kroger as a WIC vendor for one year would not result in inadequate participant access, imposition of the one-year disqualification was appropriate. As a result, the ALJ recommended the one-year disqualification be imposed. The final paragraph of his recommended order stated, "[p]ursuant to KRS 13B.110(4), the parties shall have fifteen (15) days from the date of this recommended Order in which to file exceptions" with the Secretary. On June 22, 2005, Kroger timely filed the following exceptions:

> 1. The Findings of Fact on which the Recommended Decision is based are defective, in whole or in part, in that they are without the support of substantial evidence on the whole record.
>
> 2. The Conclusions of Law on which the Recommended Decision is based are defective in that they do not accurately reflect the applicable legal principles involved or are not based upon substantial evidence of record.
>
> 3. The record establishes that the action of the Cabinet for Health Services, Department of Public Health ("Cabinet") was in excess of its statutory authority and that the Cabinet failed to follow its own procedures and those provided under applicable Federal regulations, as a result of which Kroger was deprived of its right to equal protection of the laws.

> 4. The record establishes that Kroger was deprived of its right to due process, as guaranteed by the Federal and Kentucky Constitutions.
>
> 5. The record establishes that the Findings of Fact, Conclusions of Law and Recommended Decision defy reasonable business practice standards.
>
> 6. The Recommended Decision is in violation of federal and state constitutional, statutory and regulatory provisions.
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> 7. The Recommended Decision is in excess of the Cabinet's authority.
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> 8. The Recommended Decision is without support of substantial evidence on the whole record.
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> 9. The Recommended Decision is arbitrary, capricious and represents an abuse of discretion.
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> 10. The Recommended Decision is deficient and contrary to established federal and state law.
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> 11. The Compliance Buys on which the Recommended Decision is based violated the Cabinet's own regulations.
>
> 12. The Federal and State regulations utilized by the Cabinet and relied upon in the Findings of Fact, Conclusions of Law and Recommended Decision exceed the authority and language of the enabling legislation and are void.

Kroger did not submit a memorandum or other documentation in support of its exceptions. On July 6, 2005, the Secretary issued his final opinion and order adopting the ALJ's findings, conclusions and order as his own. Thereafter, Kroger sought judicial review in Fayette Circuit Court arguing: the ALJ's findings of fact are unsupported by substantial evidence; the ALJ misapplied the law; the Secretary's final order exceeded his

statutory authority; the Cabinet ignored its own procedures as well as state and federal regulations; the Cabinet deprived Kroger of due process and equal protection; the Cabinet improperly used an internal policy to impose a sanction; the federal and state regulations applied to Kroger are void because they exceeded the authority and language of the enabling legislation; the Secretary's final order defied reasonable business standards; and the Secretary's final order was arbitrary and capricious and amounted to an abuse of discretion. The Cabinet filed a brief in the circuit court arguing judicial review should be denied because the exceptions Kroger filed were so vague and general they preserved nothing for the court to review.

On July 21, 2006, the Fayette Circuit Court issued an opinion and order upholding the Secretary's decision. The court did not comment upon the non-preservation argument, preferring to rule instead on the merits of the various claims. The circuit court found the hearing officer's findings of fact and conclusions of law were supported by substantial evidence and were not clearly erroneous as a matter of law. The circuit court wrote,

> [t]he evidence and the applicable law clearly supports [sic] the hearing officer's findings that [the Cabinet] was authorized and obligated to conduct the type of compliance buys utilized in this situation and that [Kroger] violated the laws and regulations applicable to the WIC program which supported the findings and the ultimate suspension of [Kroger] from the program. Further, the evidence clearly supports the hearing officer's findings [that the Cabinet] provided appropriate training as required by law and that [Kroger] in fact received such training. Finally, the evidence clearly supports the hearing officers [sic] findings and conclusions that no

> participant would be denied access to the program as a result of the suspension since the evidence showed there were numerous other stores within a reasonable geographic area that are approved and participate in the WIC program and provide the products provided by [Kroger].

This appeal followed.

Before this Court, Kroger alleges the Cabinet: (1) wrongly subjected it to compliance buys; (2) wrongly used an internal policy to classify it as a high-risk vendor; (3) did not use the term "concentrate" uniformly on food instruments and failed to provide adequate cashier training; (4) breached its statutory and contractual duties by providing inadequate vendor monitoring; (5) breached its implied covenant of good faith and fair dealing; and (6) erroneously determined participants would still have adequate access if Kroger were disqualified as a program vendor.

Before we can reach the merits of this appeal, we must first determine the allegations advanced by Kroger have been preserved for our review. "[I]n administrative law cases, a party who disagrees with the hearing officer's recommended order must bring that disagreement to the attention of the agency head or be precluded from raising the issue in court." *Herndon v. Herndon,* 139 S.W.3d 822, 825 (Ky. 2004). The filing of exceptions to an ALJ's recommendation under Kentucky Revised Statutes (KRS) Chapter 13B serves two purposes. First, it preserves and identifies issues for the agency head to review. Second, it preserves issues for subsequent judicial review. *Rapier v. Philpot,* 130 S.W.3d 560, 563 (Ky. 2004); *Eiland v. Ferrell,* 937 S.W.2d 713, 716 (Ky. 1997). In both instances, a clear, concise statement of a party's objection(s) obviates the need for the

agency head or the court, on subsequent judicial review, to decipher the intended argument. Here, Kroger filed exceptions alleging a dozen flaws in the ALJ's findings, conclusions and recommendation. However, they were of such a general nature they were of little benefit to anyone. Kroger reminds us that it filed detailed findings of fact, conclusions of law and a recommended order before the ALJ issued his decision. We have reviewed that document but we simply do not see how a pleading submitted to the ALJ on April 15, 2005, can preserve complaints that did not arise until the ALJ issued his decision a month later on June 15, 2005. If that were the case, filing exceptions to preserve an issue for our review would be required only when a party has not filed proposed findings of fact, conclusions of law and a recommended order. Our research has not revealed that to be the case.

In *Couch v. Natural Resources and Environmental Protection Cabinet,* 986 S.W.2d 158, 161 (Ky. 1999), an exception was filed stating a hearing officer's findings "were contrary to 'the law and to the facts, to KRS Chapter 350, and to the administrative regulations issued pursuant to KRS Chapter 350.'" The Supreme Court of Kentucky held such a general statement was inadequate to preserve an issue for judicial review. Other courts have reached the same conclusion. *Howard v. Secretary of Health and Human Services,* 932 F.2d 505, 509 (6th Cir. 1991) ("A general objection to the entirety of the magistrate's report has the same effects as would a failure to object."); *Lockert v. Faulkner,* 843 F.2d 1015, 1019 (7th Cir. 1988) ("an objection stating only 'I object' preserves no issue for review. . . . A district judge should not have to guess what

arguments an objecting party depends on when reviewing a magistrate's report."). We see no difference in the wording chosen by Kroger in voicing its exceptions and the language held to be inadequate in *Couch.* Thus, we see no reason for a different result. Since the exceptions filed by Kroger are tantamount to having filed no exception at all, the only findings and conclusions available for our review are those "contained in the agency head's final order that *differ* from those contained in the hearing officer's recommended order." *Rapier,* at 564. However, since the Secretary adopted the ALJ's findings, conclusions and recommendation as his own, there is no difference in the ALJ's report and the Secretary's final order. Therefore, nothing is preserved for our review and we must affirm the Secretary's decision. While we deny review for lack of preservation, were we to review the merits of the case, we would agree with the analysis of the Fayette Circuit Court.

For the foregoing reasons, the final opinion and order of the Secretary is affirmed.

ALL CONCUR.

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