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**UNITED STATES OF AMERICA**
**BEFORE THE FEDERAL TRADE COMMISSION**
**OFFICE OF ADMINISTRATIVE LAW JUDGES**

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| **In the Matter of**<br><br>**Altria Group, Inc.**<br>**a corporation;**<br><br>**And**<br><br>**JUUL Labs, Inc.**<br>**a corporation.** | **Docket No. 9393** |

**ANSWER AND DEFENSES**
**OF RESPONDENT ALTRIA GROUP, INC.**

Pursuant to Rule 3.12 of the Federal Trade Commission's ("FTC" or the "Commission") Rules of Practice for Adjudicative Proceedings (the "Rules"), Respondent Altria Group, Inc. ("Altria"), by and through its undersigned counsel, hereby files the following answer to the Commission's Administrative Complaint (the "Complaint") against Altria and JUUL Labs, Inc. ("JLI").

## INTRODUCTION

Through this action, the FTC is seeking to unwind Altria's $12.8 billion minority investment in JLI based on a fundamental misunderstanding of why Altria made that investment, a fundamental misunderstanding of why Altria shut down Nu Mark (its e-vapor subsidiary), and a fundamental misunderstanding of the regulatory framework in which Altria and JLI operate. As will be shown in this proceeding, contrary to the FTC's allegations, Altria did not withdraw its own products to facilitate a JLI deal, and Altria's e-vapor products did not serve as a competitive constraint on JLI — which, after Nu Mark's exit, would go on to lower prices in

response to competition. Altria withdrew its e-vapor products because it concluded that they could not meet FDA's regulatory requirements, because they lacked consumer appeal, and because they had lost money and had no short- or long-term path to profitability. The minority investment that the FTC challenges, which was designed to make JLI a more successful competitor by, among other things, helping it to successfully navigate complex regulatory hurdles and thereby continue selling its products, does not violate the antitrust laws. Altria submits that, on the full record, and in considering the applicable law, the relief sought by the Complaint should be denied.

Altria's subsidiary, Philip Morris USA, has for more than a century been one of the nation's leading manufacturers of conventional, combustible cigarettes. In 2012, Altria established a new subsidiary, Nu Mark, to develop reduced-harm tobacco products, recognizing that adult consumers were becoming interested in e-vapor products because they could potentially provide some or all of the satisfaction of combustible cigarettes without the associated tar and without the stigma associated with smoking. Although Altria set up Nu Mark to compete, it did not have scientists or technical experts who were experienced in developing e-vapor products. After failing in its initial efforts to develop a successful product on its own, Altria undertook an acquisition strategy beginning in 2014. All of this was done at a time when the FDA did not regulate e-vapor products.

Far from being a "threat to JLI's market dominance" as the FTC alleges, Altria's effort was a failure. By late 2017, the original product using a platform that Altria had acquired in 2014, the "cig-a-like" MarkTen, had failed to gather traction with consumers and was ineffective in getting smokers to convert to e-vapor products. Consumer demand was shifting to pod-based products, like JUUL, a product introduced by JLI, a Silicon Valley startup. Still without proven

research and development capability required to internally develop a competitive e-vapor product, Altria again sought to acquire products in the hope of expanding sales.

By this point, FDA regulations imposed a significant constraint on Altria's options. Congress has designated the FDA as the only federal agency that "possesses the scientific expertise needed to implement effectively all provisions of the Family Smoking Prevention and Tobacco Control Act." Pub. L. No. 111–31, § 2(45), 123 Stat. 1776, 1781 (2009). Under that statute, as made applicable to e-vapor products via an FDA regulation known as the "Deeming Rule," all e-vapor products had to obtain FDA authorization before they could be sold to consumers (through a submission known as a Premarket Tobacco Product Application ("PMTA")).

The FDA made clear that e-vapor products would only be authorized to be sold if they were appropriate for the protection of public health because they generated positive health benefits for American consumers of tobacco products. But the FDA exercised its enforcement discretion to allow products that had been for sale in the United States on or before August 8, 2016 to remain for sale, pending PMTA approval, so long as an application was filed by a deadline set by the agency. That enforcement discretion could be revisited, and, regardless, the FDA was clear that any new or changed product without "8/8/16 status" could not be sold to consumers until after receiving PMTA approval, a multi-year process.

Recognizing that its existing cig-a-like products were not competitive, Altria, in late 2017, scrambled to acquire a pod-based product that had 8/8/16 status. Altria held unsuccessful exploratory discussions with JLI and, at the same time, scoured the globe for pod-based products with 8/8/16 status that it could acquire. As talks with JLI were going nowhere, in the fall of 2017, Nu Mark licensed the rights to an e-vapor product owned by a Chinese manufacturer that

had 8/8/16 status. Due to the product's 8/8/16 status, Nu Mark could not make material modifications to the newly acquired e-vapor product without waiting for PMTA approval.

Nu Mark rushed to rebrand the Chinese-made product as MarkTen Elite and to expand its availability to consumers in March 2018. But after initial optimism about its prospects, Altria realized by the summer of 2018 that Elite had many problems and was not converting adult smokers. Elite also was not effectively competing with other e-vapor products, including JUUL, which was successful in large part because of its proprietary nicotine salts formula that provided users with a satisfying, cigarette-like experience. Elite, by contrast, did not provide consumers with an experience similar to that of traditional cigarettes or other e-vapor products, like JUUL.

Despite Altria spending millions and using its distribution expertise to introduce Elite to consumers, at the time it was pulled, Elite had a trivial nationwide share of sales and little consumer appeal. In the four years before the business was wound down, Nu Mark had lost hundreds of millions of dollars — and it was projected to lose hundreds of millions more in the coming years. Altria also concluded that Elite, as well as Nu Mark's preexisting MarkTen products, could not obtain PMTA approval in their current form. Both MarkTen and Elite lacked a key element for obtaining PMTA approval — the ability to convert existing smokers and thereby significantly reduce the overall harm to the health of American tobacco consumers.

As a result of these considerations, in September 2018, at a time when negotiations with JLI had broken off, Altria began the process of shutting down the vast majority of its ongoing e-vapor development work (including work on a PMTA for Elite), having concluded that the existing Elite product could not obtain FDA approval. Instead, Altria would restructure its resources to transition to "growth teams," charged with hitting the reset button on Altria's e-vapor strategy and trying to come up with a competitive e-vapor product from scratch. But

even in a best-case scenario, where Altria would be able to rapidly develop such a product (its poor track record notwithstanding), it would not be able to sell the product for many years and only if authorized by the FDA.

Meanwhile, on September 12, 2018, FDA Commissioner Gottlieb wrote letters to Altria, JLI, and three other e-vapor manufacturers, expressing concern that e-vapor products were contributing to the "epidemic rate of increase in youth use," threatening to revisit its enforcement discretion as set out in the Deeming Rule, and expressly calling for manufacturers to consider stopping the sale of flavored products. Altria recognized the letter as creating new regulatory exposure for e-vapor products. In response, on October 25, 2018, Altria determined to discontinue its Elite product and the flavored MarkTen products (other than the traditional tobacco, menthol, and mint varieties).

Altria also continued its effort to reach a deal with JLI. And, on December 20, 2018, after twenty months of on-again, off-again discussions, Altria made a $12.8 billion investment for a 35% stake in JLI. Recognizing that JLI and Altria had different strengths developed in different markets — JLI with the ability to design satisfying e-vapor products and Altria with mature distribution systems and regulatory know-how — as part of the agreement, the parties designed a pro-competitive structure under which Altria would devote significant resources to help shore up JLI's crucial PMTA efforts. In order to facilitate the provision of those services, Altria also agreed as part of the final transaction that it would not develop or acquire new e-vapor products while holding a significant investment in JLI. Altria's commitment was reasonably ancillary to the pro-competitive benefits provided by the transaction; without it, JLI could not have agreed to allow Altria access to JLI's development plans and gained the full benefits of Altria's regulatory expertise. The transaction thus both made JLI more efficient and

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