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UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
OFFICE OF ADMINISTRATIVE LAW JUDGES

In the Matter of:)
ALTRIA GROUP,)
a corporation,) Docket No.
and) 9393
JUUL LABS, INC.,)
a corporation,)
Respondents.)
-----)

Monday, August 3, 2020

Remote Telephonic Prehearing Conference

Scheduling Conference
Altria Group and Juul Labs

8/3/2020

1 APPEARANCES :

2

3 ON BEHALF OF THE FEDERAL TRADE COMMISSION:

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1 P R O C E E D I N G S

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3 JUDGE CHAPPELL: This is the initial prehearing
4 scheduling conference in Docket Number 9393 in the
5 matter of Altria Group, Inc. and Juul Labs. This
6 prehearing conference is being connected telephonically
7 and is being transcribed by a court reporter who is on
8 the line with us. Will the court reporter state their
9 name for the record.

10 MADAM REPORTER: Sally Jo Quade. Thank you,
11 Your Honor.

12 JUDGE CHAPPELL: I will need everyone to mute
13 your phones when you are not speaking.

14 I need to know, is anyone on this call who is
15 not with one of the parties in this case? Someone from
16 each party needs to let me know. I'll start with the
17 government.

18 MR. VOTE: Your Honor, this is Dominic Vote on
19 behalf of complaint counsel. As far as I'm aware,
20 everybody who has dialed in from our team is from the
21 FTC.

22 JUDGE CHAPPELL: All right, so I'll take that as
23 your appearance, Mr. Vote. Anyone else you want to add
24 to your appearance for the government?

25 MR. VOTE: Yes, Your Honor. With me virtually

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1 is James Abell and Meredith Levert. Thank you, Your
2 Honor.

3 JUDGE CHAPPELL: I'll take appearances from the
4 respondents, please.

5 MR. WOLINSKY: Good afternoon, Your Honor, this
6 is Marc Wolinsky from Wachtell Lipton. I am also joined
7 by Jonathan Moses, one of my partners, and two of the
8 lawyers from Altria in-house legal counsel are also on
9 the line.

10 JUDGE CHAPPELL: Okay. And Juul?

11 MR. GELFAND: Good afternoon, Your Honor. This
12 is David Gelfand on behalf of Juul, or JLI as we refer
13 to it, and I would like to introduce to Your Honor
14 Jeremy Calsyn, and Jessica Hollis, both from my law
15 firm. We also have a couple of in-house lawyers from
16 JLI on the phone as well. And as far as I know, nobody
17 from outside.

18 JUDGE CHAPPELL: I need both respondents to
19 acknowledge like the government's counsel in that you
20 have no one that you have knowledge of that has dialed
21 in that is not part of your trial team?

22 MR. GELFAND: That is correct, Your Honor.

23 MR. WOLINSKY: Your Honor, Marc Wolinsky. The
24 same, no one outside the client and lawyers at my firm,
25 and also, I should have introduced Debbie Feinstein from

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1 Arnold & Porter is on, which I don't anticipate she will
2 have a speaking role today.

3 JUDGE CHAPPELL: All right. And before anyone
4 makes any statements, I will need that person to
5 identify him or herself for the court reporter. Madam
6 Reporter, can you understand me? You'll know when it's
7 my voice?

8 MADAM REPORTER: Yes, sir.

9 JUDGE CHAPPELL: All right.

10 MR. GELFAND: Your Honor, Michael Sibarium from
11 the Pillsbury firm, also representing JLI. He's on the
12 phone as well.

13 JUDGE CHAPPELL: All right.

14 MR. GELFAND: Thank you, Your Honor.

15 JUDGE CHAPPELL: A letter was received from a
16 member of the press regarding access to this phone
17 conference. For reasons which are stated in the order
18 issued on July 28th, 2020, scheduling this phone
19 conference, access to the scheduling conference is
20 limited to the parties.

21 I could not in fairness allow one member of the
22 press to join the phone conference after the public has
23 been on notice by the order that this live phone
24 conference is not accessible by the public. The purpose
25 of this conference is to discuss initial scheduling

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1 order. There is no evidence, there is no testimony
2 presented. In addition, a transcript of this conference
3 will be made available to the public. I've asked that
4 the completion of the final transcript be expedited so
5 that it will be available to the public as soon as
6 possible, and I am told the final transcript will be
7 available some time tomorrow.

8 Moving on. I need everyone to mute their phones
9 when they are not speaking on the conference call. If I
10 said that already, I'm reading my agenda backwards.

11 Let me talk about the scheduling order. The
12 parties provided joint edits to the proposed scheduling
13 order my office sent out. I have looked over the joint
14 proposal and with one exception, the proposed changes
15 are fine. A suggested date fell on a Saturday, March
16 20th, that date will be changed to March 19th. I will
17 issue a scheduling order incorporating the parties'
18 proposed changes shortly.

19 Who wants to provide a status on settlement
20 discussions?

21 MR. VOTE: Your Honor, this is Dominic Vote on
22 behalf of complaint counsel. I can start if you would
23 like.

24 JUDGE CHAPPELL: Go ahead.

25 MR. VOTE: We have a date on the calendar

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1 scheduled for a very preliminary discussion with
2 defendants, and that will be the first discussion we
3 will have had. So too early to tell Your Honor where
4 that will lead, but certainly we plan to keep the Court
5 apprised of any developments on that front.

6 JUDGE CHAPPELL: All right. Anything from the
7 respondents?

8 MR. WOLINSKY: Your Honor, Marc Wolinsky. We're
9 on the same page as Mr. Vote.

10 JUDGE CHAPPELL: JLI?

11 MR. GELFAND: Nothing further from us, Your
12 Honor. Same page.

13 JUDGE CHAPPELL: I am still getting an echo.
14 Everyone on this call who is not speaking, please mute
15 your phones.

16 Each side may present a brief case overview of
17 not more than 10 minutes. If you refer to photos, these
18 will not be exhibits and they will not be part of the
19 record. The transcript of this conference will be made
20 available to the public, so you are instructed not to
21 present any confidential information in your overview.

22 Government, go first, do you wish to give us an
23 overview?

24 MR. VOTE: Yes, Your Honor.

25 JUDGE CHAPPELL: Go ahead. I'm timing it.

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1 MR. VOTE: This case is about the largest
2 tobacco company in the United States, Altria, joining
3 forces and agreeing not to compete with Juul, the
4 dominant e-cigarette company in the U.S. Prior to the
5 agreement at issue in this case, the two companies
6 competed aggressively with one another in the market for
7 closed tank e-cigarettes and consumers benefited
8 significantly from that competition.

9 But in late 2018, that competition was lost when
10 Altria abruptly exited the e-cigarette market and nearly
11 simultaneously announced a \$12.5 billion investment in
12 Juul, along with a six-year noncompete agreement broadly
13 covering the e-cigarette space.

14 I would like to start by telling you a little
15 bit about the e-cigarette products at issue in this case
16 and what we mean by closed tank e-cigarettes. I will
17 then turn briefly to the agreements between the parties,
18 and then provide some color as to why we allege that
19 those agreements have eliminated both current and future
20 competition.

21 E-cigarettes are battery-powered devices that
22 vaporize a liquid solution containing nicotine. There
23 are two very different categories of e-cigarettes,
24 closed tank systems and open tank systems. Closed tank
25 systems, which are the kind of products sold by Juul and

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1 Altria, and the ones at issue in our complaint, often
2 look a lot like a small USB drive, though some products
3 are developed to look like a cigarette.

4 But the key fact is this: They use prefilled
5 cartridges of e-liquids. Consumers cannot refill them
6 with their own liquids.

7 JUDGE CHAPPELL: Are you saying tank or take?

8 MR. VOTE: Tank, Your Honor.

9 JUDGE CHAPPELL: T A N K?

10 MR. VOTE: Exactly.

11 JUDGE CHAPPELL: Go ahead.

12 MR. VOTE: They are typically sold in
13 convenience stores, and they used to be available in a
14 wide variety of flavors, but now are only available in
15 tobacco and menthol flavors. So that's closed tank
16 products I'm talking about now.

17 By contrast, open tank systems are more
18 customizable devices that allow consumers to refill
19 whatever e-liquids they prefer. They are typically sold
20 in vape shops that also market a wide range of flavored
21 liquids that can be used in these devices, among many
22 other tobacco products. If you see one on the street,
23 the open tank systems are the device that cause a very
24 large puff of vapor when you use them.

25 Now, our complaint alleges that because of the

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1 significant differences in these two products, and
2 because they're sold in different channels, the
3 appropriate relevant market in this matter is limited to
4 the sale of closed systems electronic cigarettes in the
5 United States.

6 Now, until the fall of 2018, Altria had been
7 investing heavily and competing vigorously in the closed
8 tank e-cigarette market, for years, through a division
9 called NuMark, that's N U M A R K. It was spending
10 millions of dollars on marketing and research and
11 development, and in July of 2018, told investors that
12 its NuMark products were getting traction with consumers
13 and driving growth. But just a few months later on
14 December 7th, Altria publicly announced that it would
15 wind down its entire e-cigarette business, and less than
16 two weeks after that announced its \$12.5 billion
17 acquisition of a 35 percent share of Juul.

18 Altria's investment in Juul included a six-year
19 noncompete that ended Altria's ability to compete in the
20 closed tank e-cigarette market in any meaningful way, as
21 well as a services agreement that would allow Altria to
22 provide marketing and regulatory support to its new
23 e-cigarette partner. In the simplest of terms, Altria
24 decided if you can't beat them, join them.

25 Now, the fact that Altria exited the market just

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1 two weeks before closing their massive investment in
2 Juul is not just a coincidence. We alleged in our
3 complaint, and the evidence will show, that Juul made
4 clear, and Altria was fully aware, that there was no way
5 this transaction was going to work unless Altria agreed
6 to exit the closed tank e-cigarette market and cease
7 competing with Juul. And exit the market they did.

8 Altria will claim that they shut down the NuMark
9 business because it was not successful enough and it
10 faced challenges. Certainly all e-cigarette firms have
11 faced significant challenges, including regulatory
12 challenges, but this justification is pretextual.
13 Certainly none of the other closed tank e-cigarette
14 suppliers have suggested that they intend to abandon
15 this strategically important market as a result of
16 regulatory challenges. The bottom line is this: Juul
17 communicated and Altria knew that it had to get out of
18 the e-cigarette business in order to complete its
19 investment in Juul.

20 JUDGE CHAPPELL: You have five minutes
21 remaining.

22 MR. VOTE: Thank you, Your Honor.

23 Altria's agreement to invest in Juul and
24 withdraw its NuMark products from the market immediately
25 eliminated significant competition between two of only a

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1 few closed tank e-cigarette suppliers. Altria was
2 already competing with Juul on price, offering
3 aggressive promotions that directly benefited consumers,
4 securing important shelf space at convenience stores and
5 working to improve its existing products.

6 But in addition to eliminating aggressive
7 competition between Juul and NuMark, the six-year
8 noncompete provision agreed to by the parties also
9 eliminated future competition by putting a grinding halt
10 to Altria's significant and ongoing effort to develop
11 next-generation e-cigarette products or to explore
12 partnerships to bring new e-cigarette products to the
13 market.

14 Before this transaction, Altria was fully
15 committed to competing in the closed tank e-cigarette
16 market and had told its investors as much. As any
17 reasonable company would, it developed a plan B to make
18 sure it was prepared to go on competing if the deal
19 negotiations with Juul fell apart. But for its
20 investment in Juul, and the accompanying noncompete
21 agreement, Altria would undoubtedly be competing
22 aggressively in the closed tank e-cigarette market
23 today.

24 Consumers have now lost over two years of
25 head-to-head competition between Altria and Juul and

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1 they have lost over two years that Altria would have
2 spent investing and developing new products. The market
3 for closed tank e-cigarettes was already highly
4 concentrated before Altria's investment in Juul, and
5 whether viewed as a minority acquisition under Section 7
6 of the Clayton Act, or a series of illegal agreements
7 under Section 1 of the Sherman Act, Altria's investment
8 in Juul has eliminated actual and future competition to
9 the detriment of consumers, and that competitive harm
10 cannot be justified or outweighed by any pro-competitive
11 justification offered by defendants.

12 I look forward to answering any questions the
13 Court may have and presenting this case as efficiently
14 as possible. Thank you, Your Honor.

15 JUDGE CHAPPELL: Thank you.

16 Respondent?

17 MR. WOLINSKY: Good afternoon, Marc Wolinsky.

18 Your Honor --

19 JUDGE CHAPPELL: Are you going to do five
20 minutes each or are you doing the whole ten minutes
21 yourself? What's your plan?

22 MR. WOLINSKY: The plan is for me to use eight
23 minutes and Mr. Gelfand to use two minutes.

24 JUDGE CHAPPELL: All right.

25 MR. WOLINSKY: And may I start now?

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1 JUDGE CHAPPELL: Yes, go ahead.

2 MR. WOLINSKY: Okay, thank you.

3 Your Honor, I want to start with an overview of
4 the e-vapor category and then talk about the regulatory
5 scheme. The big difference between e-vapor products and
6 cigarettes is that e-vapor products do not have many of
7 the harmful chemicals generated by burning tobacco and
8 that's why the FDA recognizes that they may be less
9 harmful than cigarettes.

10 You heard about Cigalike products. NuMark sold
11 a Cigalike product and it looks like a cigarette. Juul
12 is a well-known example of a pod-based product, and as
13 you have heard, it looks like a thumb drive. It's
14 modern looking. Other products in this category include
15 Vuse Alto, which is sold by R. J. Reynolds, NJOY, Ace
16 and MyBlu. And those are on the pictures I sent in for
17 your reference.

18 Turning to the regulatory scheme, e-vapor
19 products are highly regulated by the FDA and generally
20 must be authorized before they can be sold. To get
21 authorization, a manufacturer has to submit what is
22 known as a PNTA, or Premarket Tobacco Product
23 Application, which I think we're on accord with the FTC,
24 this is an extremely expensive, burdensome, and
25 years-long process.

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1 Under a regulation called the Deeming Rule, the
2 FDA allows products that were on the market before
3 August 8, 2016, to stay on the market pending the filing
4 of a PMTA by a deadline which is met next month, and any
5 product not on the market as of 8/8/16 can't be sold
6 without authorization. And if a manufacturer wants to
7 make certain modifications to the product, it's deemed
8 to be a new product, and again, you can't materially
9 modify a new -- an existing product without getting PMTA
10 authorization.

11 In order to get approval, the applicant has to
12 show with extensive evidence that it is -- statutory
13 language -- "appropriate for the protection of public
14 health," because, among other things, it converts
15 smokers. If you can't convert smokers, you're not
16 likely to reduce the risk to the population and it's not
17 in the public interest.

18 Your Honor, I wanted to go over some regulatory
19 framework, because it is central to understanding why
20 the FTC's case is so flawed. You heard from opposing
21 counsel that Altria discontinued its e-vapor products in
22 the months and weeks before the JLI deal was signed, and
23 that is true. What is not true is the allegation in the
24 complaint that JLI negotiated to secure Altria's exit in
25 order to "eliminate a threat to JLI's market dominance."

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1 That allegation is not true for two reasons.
2 First, JLI did not secure Altria's exit from e-vapor.
3 Altria withdrew its products for its own independent
4 reasons, including regulatory reasons. And second,
5 Altria's products were not and were never going to be a
6 threat to JLI's market dominance.

7 The decisions to withdraw the products came at
8 two separate times. The final decision to discontinue
9 Elite was made in September 2018 after the FDA sent a
10 letter to the leading manufacturers highlighting the
11 risks of e-vaping and encouraging them to remove their
12 flavored products from the market. Before the FDA sent
13 that letter, and at a time when JLI negotiations had
14 broken off, Altria had already concluded that Elite had
15 no future and had begun the process to stop working on a
16 PMTA.

17 Senior leadership recognized that Elite was a
18 money loser and that it was not effective in getting
19 smokers to stop or reduce their use of cigarettes. The
20 FDA's concerns about e-vaping tipped the scales, and
21 that's highlighted by the fact that something the FTC
22 doesn't recognize, that at the same time Altria
23 discontinued Elite, it also discontinued the flavored
24 versions of its Cigalike products, including one called
25 strawberry brulee. Elite was not a competitive threat

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1 to Juul.

2 In order to convert smokers to vaping, an
3 e-vapor product has to give smokers the nicotine
4 satisfaction that they can get from a cigarette. Juul
5 figured out how to do that with two products that make
6 use of nicotine salts and increased levels of nicotine.
7 Elite did not have nicotine salts, had lower levels of
8 nicotine, and because of that, it could not compete
9 effectively with Juul, and those things could not be
10 changed because of the 8/8/16 rule. That's the story on
11 Elite and MarkTen.

12 Altria did continue to market its remaining
13 Cigalike products after the FDA's September 2018 letter.
14 The decision to discontinue them was made in early
15 December 2018. Even then, the prospect of completing a
16 deal with JLI was uncertain, due diligence was still
17 under way. But just as with Elite and the NuMark
18 flavors, the remaining products were not discontinued to
19 placate JLI.

20 They admitted the existing product was losing
21 popularity, would not have gotten FDA authorization, had
22 lost hundreds of millions of dollars and was projected
23 to lose another \$235 million over the next three years.
24 They were never a competitive threat to JLI, in part,
25 because they looked like cigarettes and had the stigma

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1 associated with e-cigarettes. They also didn't have
2 nicotine salts and the high levels of nicotine.

3 So the FTC is not going to be able to prove that
4 there was an implicit or explicit agreement. There is
5 an express agreement which the FTC is challenging under
6 a rule of reason analysis, as an agreement that as long
7 as Altria held a significant investment in JLI in the
8 future, it would not develop or acquire new e-vapor
9 products.

10 This noncompete does satisfy the rule of reason,
11 and it goes back to the regulatory framework. As part
12 of the agreement, Altria committed to use its expertise
13 to help JLI get FDA authorization, not only for existing
14 products, but for new products. To do that effectively,
15 Altria needed access to JLI's inside information, and
16 the parties both recognized that in order to help JLI be
17 more competitive in the future, it made sense that
18 Altria would not be able to use -- have access to JLI's
19 inside information and use it in developing its
20 competing products.

21 As to those competing products, at the time
22 Altria agreed to stop developing products, it had
23 nothing on the board, and any products that it was going
24 to develop were years and years off into the future,
25 again because of this regulatory framework, because of

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1 the PMTA process.

2 Finally, a word about remedies. The remedy that
3 the FDA is seeking is not going to promote competition.
4 NuMark, the MarkTen Elite, and MarkTen products are not
5 coming back to the market. As for the future products,
6 they are years and years -- if they were to be
7 redeveloped, they are years off into the future, and the
8 market will be evolving significantly over the coming
9 years as PMTA applications are made by other applicants.

10 So in conclusion, the FTC's position boils down
11 to two ideas. One, that Altria should have continued
12 selling products that it concluded could not get FDA
13 authorization because they were not effective in
14 reducing the risks of smoking. Consumers were not
15 benefitting from these consumers. And two, that Altria
16 should have continued selling product that had lost
17 hundreds of millions of dollars, and was projected to
18 lose hundreds more. Again, consumers would not be
19 benefited by this money-losing proposition of a product
20 that would fail.

21 In a case that's governed by a rule of reason
22 standard, those positions are decidedly unreasonable.
23 Your Honor, if you have any other questions, I'd be
24 happy to -- any questions, I would be happy to answer.

25 JUDGE CHAPPELL: Thank you. I have none.

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1 MR. GELFAND: Thank you, Your Honor. This is
2 David Gelfand on behalf of JLI. Just a few additional
3 points.

4 First, by way of introduction of my client, JLI,
5 it was founded by a couple of Stanford students as a
6 startup back in 2007. They were former smokers looking
7 to develop alternatives to cigarettes, but it was not
8 until 2015 that they actually introduced the products
9 that are at issue in this case. So just three years
10 before the transaction at issue.

11 As Mr. Wolinsky explained, that product hit the
12 right cord with adult smokers because it was well
13 designed and used proprietary nicotine salt formulation
14 that satisfied smokers. It's that product design that
15 helped JLI increase its sales.

16 The company is greatly proud in the success of
17 transitioning smokers away from traditional cigarettes
18 and you will hear that's a big part of their mission.

19 I don't want to repeat what Mr. Wolinsky said,
20 I'll just tell you a couple of things from JLI's
21 perspective. First, JLI's witnesses will be adamant,
22 Your Honor, that they had no agreement with Altria that
23 Altria would cease selling its NuMark products. In
24 fact, they didn't see that coming. The FTC's case is
25 based on exchanges of term sheets, none of which became

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1 agreements. There were various terms that were being
2 discussed as possible inclusion in a future transaction
3 document.

4 Second, the evidence will also be clear that JLI
5 viewed the Altria products as competitively irrelevant.
6 My client did not adjust their prices, did not adjust
7 their competitive strategy because of those products,
8 either while they were on the market or as a result of
9 Altria's decision to stop selling them.

10 Third, JLI had good reason to ask for this
11 noncompete that's at the center of some of the complaint
12 counsel's allegations. Altria was going to have access
13 to very sensitive information, and they were going to be
14 providing very important services to JLI to get this
15 product approved by the FDA and distributed. And
16 because of that, they had good reason to not want Altria
17 to be able to dilute its attention, take the
18 confidential information they were going to have access
19 to and turn around in the market and compete against
20 them with new products.

21 Fourth, there is cognizable benefit from the
22 services that Altria provided to JLI, Your Honor.

23 JUDGE CHAPPELL: I don't know if you heard me,
24 you have one minute remaining.

25 MR. GELFAND: Thank you, Your Honor. Cognizable

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1 benefits, including critical assistance on the PMTA
2 application, which was recently filed. That application
3 was more robust as a result of the assistance that
4 Altria provided and more likely to be accepted and
5 consumers will benefit from that.

6 Finally, the market remains dynamic and
7 competitive. Our client sees this every day. As it
8 contains in its mission of transitioning adult smokers
9 away from combustible cigarettes, they have many other
10 products to choose from. The evidence will show that
11 consistent with the FDA's regulations, other competitors
12 have been successful in going after consumers, the
13 market has remained competitive, and other companies
14 continue to win business.

15 For these reasons, and others that we will
16 develop through discovery and in a trial, Your Honor,
17 complaint counsel's claims are without merit. Thank
18 you.

19 JUDGE CHAPPELL: All right. Anything further?

20 MR. VOTE: Not from complaint counsel, Your
21 Honor.

22 MR. WOLINSKY: Your Honor, Marc Wolinsky.
23 Nothing from me.

24 MR. GELFAND: Nor from me. This is David
25 Gelfand, Your Honor. Thank you.

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1 JUDGE CHAPPELL: Thank you. Hearing nothing
2 further, we are adjourned.

3 (Whereupon, at 3:36 p.m., the hearing was
4 adjourned.)

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1 CERTIFICATE OF REPORTER

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3 I, Sally Jo Quade, CERT, do hereby certify that
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