



Insight

A Primer on the Current Status of the Epic v. Apple Case

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Executive Summary

- In the Epic Games v. Apple lawsuit, which recently began court proceedings, Epic Games alleges that Apple is exploiting a monopolistic position through its restrictions on sideloading and payment processing fees—arguments that mirror broader policy debates at both the federal and state levels.
- Apple claims that its commission fees are in line with or below the industry standard and that its sideloading restrictions are the best way possible to protect users from fraudulent and malicious software.
- This case could upend numerous markets beyond Apple and Epic Games and affect the business models of a variety of different digital products while also giving momentum to regulatory proposals in state legislatures and in Congress.

Introduction

Monday, May 3, 2021, marked the start of the court battle between Epic Games and Apple regarding the Apple App Store business model. Epic alleges that Apple is engaging in anti-competitive behavior by [restricting](#) and imposing “prohibitive” payment processing fees, thus demanding legal remedy. This case is one of the most significant legal challenges to the Apple App Store and its iOS ecosystem. It comes at the same time many other tech giants are facing increased antitrust scrutiny and amid [multiple state-level legislative initiatives](#) seeking to regulate app stores. The outcome of this case will have great significance not only for Apple, but for other operating-system developers in the market.

Before considering the potential impact of this suit, this primer outlines what led to this legal challenge and then examines the position of both parties. It concludes the case has the potential to impact a variety of markets that extend beyond the two parties in the case, such as app stores, mobile operating systems, and app development—all key elements of the digital-services economy as a whole.

How the Case Arose

Epic Games is a game development studio that is behind the video game sensation *Fortnite*. As of May 6, 2020, *Fortnite* had a user base of [350 million registered users](#) and over [133 million downloads on iOS](#). Since its release in 2017, *Fortnite* has had a great impact both on the gaming sphere and in pop culture. The game became notorious for its [viral dances](#) and was the first video game to feature live digital concerts with high-profile artists such as [Travis Scott](#) and [Marshmello](#).

The Apple App Store is the exclusive platform to download apps to iOS mobile devices, as Apple restricts the installation of other app stores or third-party distribution platforms. It also restricts the installation of software through the web, a process commonly known as sideloading. In order to distribute apps in the Apple App Store, developers must consent to Apple’s terms of service, and apps will undergo a vetting and review process. Users

can circumvent these restrictions through methods such as “jailbreaking,” but these methods are not officially supported by Apple and carry increased exposure to [malware and spyware](#).

By consenting to these terms of service, distributors are obligated to use Apple’s payment processing service for all their digital goods and service sales, for which Apple will collect a [commission fee](#) in certain cases. The rate charged by Apple will vary according to the service provided and yearly revenue: For subscription services, Apple will charge 30 percent for the first year of subscription, with the rate decreasing to 15 percent the years after. For in-app purchases, Apple will charge 15 percent for companies with yearly revenues under \$1 million, and 30 percent for companies above that threshold. According to estimates, [only 2 percent of developers](#) would cross that threshold. The sale of physical goods and advertisement revenue have no charge.

Even prior to the events that led to the legal case between Epic and Apple, Epic CEO Tom Sweeney was a [vocal advocate](#) for reducing commission fees in digital game stores. He argues current fees are “prohibitive.” As part of this effort to generally reduce commission fees for software distribution, Epic launched the [Epic Games Store in December of 2018](#), with a much lower 12 percent fee, in hopes of disrupting the PC game distribution market.

On August 20, 2020, Epic Games introduced an update to its *Fortnite* mobile app that included a new feature: a direct payment option, which would allow users to bypass Apple’s and Google’s payment processing service, and therefore, its commission. It would offer these services at a discount, under the argument that by bypassing Apple’s and Google’s “tax,” it [could offer better prices to their consumers](#). This direct-to-consumer model constituted a violation of the guidelines of both services, leading to the removal of the game from both the Google and Apple app stores.

Epic immediately responded by filing separate lawsuits against Google and Apple, alleging that the companies have been conducting anti-competitive behavior. This suit marked the start of the ongoing legal conflict between Epic Games and the two companies.

Epic’s Argument: The Current App Store Model Harms Competition

In its lawsuit against Apple, Epic Games accuses Apple of [holding monopoly power](#) on both the “iOS app distribution market” and the “iOS in-app payment processing market.” It supports this claim by pointing out Apple’s App Store is the only distribution service available to iOS users, due to its restrictions. For developers to publish in the App Store, they must use Apple’s payment processing service, per the App Store guidelines. Epic claims that this business model constitutes a monopoly and is anti-competitive, as Apple does not allow the entrance of competing app stores or payment processing services, thus blocking other services Epic, as well as some policymakers and other large app makers, seem to focus more heavily on Apple than other app stores due to its “walled garden” approach, which heavily restricts sideloading. (Google allows sideloading, although it discourages the practice.)

Due to the lack of competition in these markets, Epic alleges Apple is able to charge a 30 percent commission to developers. It argues this fee [negatively impacts small developers and end users](#) with what it assesses as a prohibitive “Apple Tax,” as it forces apps to either increase prices to compensate for the fee or accept reduced revenues; Apple’s own apps are not subject to the fee. It is important to note that at the time the lawsuit was filed, Apple was charging a 30 percent fee for the sale of all digital goods and services, but began offering 15 percent reduction for small developers on November 18th, 2020.

Additionally, Epic argues that while some may claim that Google's Android operating system could be considered a competitor, both consumers and developers face various constraints that keeps them locked-in to Apple's iOS. For consumers, switching to an Android device requires investing in a new phone, as hardware and software are often tied to each other. Epic suggests this is a prohibitive cost that prevents consumers from easily switching between systems. As was pointed out during the recent trial, however, [26 percent of users switch platforms](#) when they buy a new device. For developers, Epic argues, forfeiting the iOS market would imply a serious revenue loss. iOS consumers tend to make double the in-app purchases than users of other operating systems, such as Android, and are often considered a more desirable market. This revenue loss would be especially prohibitive for small developers, according to Epic. Thus, Apple is locking in developers to its iOS distribution service and subjecting them to their "Apple tax."

Apple's Argument: Epic Is Seeking Special Privileges That Would Harm the Broader App and Mobile Operating Systems Markets

Apple responded to Epic Games' lawsuit with a [counter lawsuit](#) for breach of contract, demanding damages for the inclusion of the direct-payment option mentioned above. In its filing, Apple claims that Epic asked for an individual arrangement which would grant it an exclusive, lower commission fee. Additionally, Apple has highlighted how Epic Games has exclusively targeted Apple, despite the 30 percent fee being an [industry standard](#) in comparison with other platforms in the digital marketplace. It also points out how many developers and apps have been able to thrive due to the effectiveness of the app store and its vetting and distribution service, which contradicts Epic's narrative that the fees are "prohibitive."

Regarding the restrictions on sideloading, Apple argues that it puts them in place in order to guarantee user safety against malware and spyware. By restricting the installation of software in its devices to only "Apple-approved" apps, it prevents less tech-savvy individuals from mistakenly installing malicious code into their devices and thereby provides users with a sense of ease because apps have already been vetted. This "walled garden" approach is Apple's method of competing in the smartphone market, as it provides a more guided and hands-on protection, in comparison with other operative systems such as Android.

Current arguments by Apple highlight that Epic's lawsuit is an attempt to specifically gain leverage against Apple, as Epic is not pursuing lawsuits against [consoles, which also present](#) the same "locked-down" approach, with restrictions on sideloading and a 30 percent fee. Epic claims that is not the case, due to the fact that these consoles are often sold at a loss, with commission fees subsidizing this loss over time. In this case, Epic argues, these fees are pro-consumer because it lowers the price of the console, allowing them to pay for the hardware over time as they make use of their digital stores.

Apple has also attempted to discredit Epic's actions by pointing out similarities in how Epic enforces rules in their games' ecosystems. Following along its breach of contract argument, it emphasizes that the removal of *Fortnite* from the app store is due to a breach of contract that would give Epic an unfair advantage. This removal is the same course of action Epic [takes against cheaters](#), as it hopes to achieve a "level playing field" that guarantees users of the service stay on it in the long term. Thus, Apple argues that removing the game is an effort to create a fair environment for developers in the same way Epic attempts to create a fair environment for *Fortnite* players.

The Importance of This Case for the Tech Industry

The outcome of this case will have a significant impact on app stores, developers, and consumers. This case

arises while multiple proposals seeking to regulate app stores are already being debated at the state and federal levels. The court's decision could impact the momentum of bills and more generally could provide a foundation for mandating sideloading or prohibiting app stores from requiring the use of their payment processing system. This kind of regulation could seriously impact Apple's business model, which has centered on competing on a privacy-first methodology—its justification for the “walled garden” approach. The result would be to eliminate a choice for consumers.

A decision against Apple could also pose a serious harm for small developers, who benefit from the consumer trust built in Apple's “walled garden.” Through its vetting system and sideloading restrictions, Apple increases the overall trust in the apps distributed to iOS, thus [lowering the barriers to entry](#) for smaller developers that often lack the trust that established companies possess. End users will be less doubtful to install an app from an unknown, as Apple's approval signals it can be safely installed into their device and will be free of fraudulent charges or spyware.

Additionally, a restriction on the payment processing service requirement might severely impact the viability of ad-based or free apps, as the current monetization scheme allows them to enjoy the benefits of the app store ecosystem without being subject to these commission fees. This shift could lower the supply of valuable apps such as [online banking apps](#), which have played a key role in driving financial inclusion.

As Apple's argument highlights, the impacts of this case extend beyond the two companies involved in it. The payment processing service requirements are one way these services can ensure they are compensated for the maintenance and support of their app store and its services. Prohibiting this requirement will incentivize developers to freeride on these app stores, as they can now introduce their own payment processing service and avoid these fees. This would likely lead to lower revenue for app distribution services, making them a less appealing business and could even lead some platforms to abandon altogether. This would harm the developers who find such platforms' payment processing an easy way to provide the service and distribute their apps, as well as the users who benefit from the efficiencies of one-stop service in such stores.

This potential impact extends beyond large mobile app store operators such as Apple and Google. For example, video game console manufacturers would likely have to reconsider their current business model for app distribution. In some cases, their [hardware may be a loss leader](#) while they bring in revenue through the sales and distribution of apps and games. This business model could be put in jeopardy if the court prohibits app stores from requiring the use of their payment processing systems, as console makers could lose valuable revenue from the fees collected from in-game purchases. The result could be increased hardware costs for consumers, as manufacturers would not be able to rely on their app store fees to subsidize low hardware prices.

Conclusion

The Epic v. Apple case might be decisive for the industry amid calls for sideloading mandates and [antitrust action](#) against Apple and Google. Most of the questions asked in this case are similar to questions and concerns some policymakers at both the state and federal level have raised regarding the current app-store market. The court's decision could provide significant momentum to existing initiatives aiming to regulate sideloading restrictions or digital payment processing services. Its impact would extend beyond smartphones, as a possible sideloading mandate could impact other markets such as video game consoles and streaming devices, which also have restrictions similar to Apple's. The final verdict of the case could imply a paradigm shift for the industry as a whole.