# *LEGAL OPINION:*

# *CRYPTOCURRENCY COMPLIANCE IN GERMANY*

***PREPARED BY:*** BSKP Rechtsanwälte Steuerberater Wirtschaftsprüfer
Dr. Rolf B. Arnade, LL.M. Rechtsanwalt – attorney-at-law
Taubenstr. 20 - 22
10117 Berlin

hereinafter referred to as the "**Law Firm**"

***PREPARED FOR:*** Web Shield Legal Library
spółka z ograniczoną odpowiedzialnością sp.k.
18 Twarda Street, 19th floor
00-105 Warsaw, Poland

hereinafter referred to as the "**Client**"

| Version | Date of preparation | Effective date | Effective/Archived |
|---|---|---|---|
| v. 1.0. | 10.10. 2018 | 10.10.2018 | Effective |
| v. 1.1 | 10.01.2019 | 10.01.2019 | Effective |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |
| | | | |

*Table of contents:*

# EXECUTIVE SUMMARY

The problem with drafting a legal statement on cryptographic currencies is that there is no specific legal regulation for this new field of financial instruments yet. This legal statement therefore has to face the challenge to find answers for questions concerning a digital business world based on legal provisions drafted for an analogue world. So far there are not even court decisions avilable to refer to. The only sources of legal qualification are official statements of European or National public agencies being part of the German executive system.

In short : it is not forbidden to have cryptographic currencies. It is not forbidden to use them in business. However, certain services relating to those cryptographic currencies may be subject to regulation and non-compliance with such requirement may lead to fines or even imprisonment. Whether a permit by a regulative agency is needed, will be decided on a case-by-case basis. This legal statement will point out the principles underlying such decisions for the three fields of practical use of cryptographic currencies: initial coin offering (ICO), cryptographic currency exchange and shopping with cryptographic currency payment.

# I. INTRODUCTION

## 1. The basis for preparing a legal opinion.

### 1.1. Legal acts.

There is no specific legal regulation dealing with cryptographic currencies in Germany. The legal acts to be considered are of general nature and initially designed for other subject matters of the analogue business world.

For the relationship between parties of a deal the main act to refer to is the German Civil Law Code (Bürgerliches Gesetzbuch – BGB).

For the relationship between the protagonists in the business of cryptographic currencies on one side and the state and its agencies on the other side one has to refer to the following **national statutes**:

- Banking Sector Act (Kreditwesengesetz – KWG)
- Securities Exchange Act (Wertpapierhandelsgesetz – WpHG)
- Securities Prospectus Act (Wertpapierprospektgesetz – WpPG)
- Payment Services Supervision Act (Zahlungsdiensteaufsichtsgesetz – ZAG)
- Capital Investment Act (Kapitalanlagegesetzbuch – KAGB)
- Wealth Investment Act (Vermögensanlagegesetz – VermAnlG)

In addition the following EU-legal acts are to be considered:

- Regulation (EU) No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (market abuse regulation – MAR)
- Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (second markets in financial instruments directive – MiFID II)

### 1.2. Other.

Furthermore orders of **National or European regulatory agencies** are relevant. This legal opinion refers to official statements issued by the following agencies or organizations:

- European Central Bank - ECB (Europäische Zentralbank)
- European Banking Authority (EBA) (Europäische Bankenaufsichtsbehörde)
- European Securities and Market Authority - ESMA (Europäische Wertpapier- und Marktaufsichtsbehörde)

and in Germany:

**Federal Supervisory Agency for Financial Services** (Bundesanstalt für Finanzdienstleistungsaufsicht – BaFin)

In the following legal opinion the author will cite the abbreviations for a.m. agencies and statutes or regulations.

## 2. Aim of this legal opinion.

This legal opinion intends to give a detailed insight into the current regulatory framework of cryptocurrencies in the specific areas of Initial Coin Offering (ICO), Cryptocurrency Exchange and Shopping with Cryptocurrency Payment in Germany.

Since Germany has not enacted a specific law regarding cryptocurrencies yet, the regulations dealing with the usage of cryptocurrencies are wide-spread and need to be harmonized. Therefore the Law Firm presents the different approaches in great detail.

# II. CRYPTOCURRENCY – DEFINITION

Cryptocurrencies are **digital assets** functioning as means of exchange in financial transactions. To secure those transactions cryptography controls the creation of additional units and verifies the transfer.[1] The control is decentralized as opposed to centralized digital currency and central banking systems.[2] Technically distributed ledger technology, typically a **blockchain**, is applied serving as a public financial transaction database.[3]

## 1. Civil law characterization of cryptocurrencies

A cryptocurrency unit does not qualify as "Sache" (i.e. thing) in the meaning of § 90 BGB. It lacks to be a corporeal object, which is required by the definition in that provision defining the concept of a thing. Because German property law applies a numerus clausus to property rights there is no chance to extend property rights designed for things in the meaning of § 90 BGB by use of an analogy also to cryptocurrencies.[4] The definition of "Sache" as corporeal object leaves space for the existance of non-corporeal objects, simply objects. That way a cryptocurrency can be defined as non-corporeal object (nicht körperlicher Gegenstand).[5] However, the BGB does not connect any specific rights to such non-corporeal objects.

They also do not qualify as debt, because they do not constitute any claim out of themselves. To constitute a claim an identifiable debtor is needed. However, cryptocurrencies only exist as virtual recording of a transaction inside the blockchain. The recording only shows the relation as transaction to a publicly visible key.[6] But this recording does not have any character beyond the pure description of a fact. Cryptocurrencies do not even represent a claim on the issuer of the cryptocurrency.[7] The transaction for which the currency is used may create a claim, but the cryptocurrency as of itself does not. The value of the cryptocurrency in the virtual wallet depends on recognition by a contractual partner, who accepts the cryptocurrency. But this acceptance is not enforceable.

Legal literature tends to grant cryptocurrencies the qualification as "another right" within the meaning of § 823 (1) 1 BGB.[8] But this may fairly be doubted, because there is no person against whom such a right out of the cryptocurrency itself could be enforced. A right is relative and a cryptocurrency does not establish any relation.

---

[1] Wikipedia „Cryptocurrency"; Schueffel, Patrick: The Concise Fintech Compendium, Fribourg School of Management, Fribourg/Switzerland, 2017

[2] Wikipedia „Cryptocurrency"

[3] Wikipedia „Cryptocurrency"; Schlund, Albert/Pongratz, Hans: Distributed-Ledger-Technologieund Kryptowährungen – eine rechtliche Betrachtung, DStR 2018, 598

[4] LG Konstanz BB Beilage No. 19/1996, 8; Shmatenko, Leonid/Möllenkamp, Stefan: Digitale Zahlungsmittel in einer analog geprägten Rechtsordnung, MMR 2018, 495, 497

[5] Schlund/Pongratz DStR 2018, 598, 600

[6] Shmatenko/Möllenkamp Fn. 4

[7] EBA Opinion on „virtual currencies", 4.7.2014, EBA/op/2014/08, note 30

[8] Shmatenko/Möllenkamp Fn. 4

Thus cryptocurrencies do not constitute any right or legal position enforceable in any way. They depend purely on acceptance by a contractual partner on this partners' sole discretion. This does not hurt the function of cryptocurrencies, because they are merely used in smart-contract-transactions, where transfer of the cryptocurrency-unit does only happen when the blockchain system indicates compliance with the defined synallagmatic action on the side of the contractual partner. Also, while civil law remedies will not apply, criminal law like the provisions about fraud are applicable.

## 2. Public financial law characterization of cryptocurrencies

Cryptocurencies do not qualify as (foreign) **currencies**, because they are not issued by an official central bank. They do not constitute cash money, because they lack corporeality. But they do not qualify as book-money as well, because they do not constitute a claim against a bank or a similar entity storing the currency.[9] Cryptocurrencies are not stored with any third party but simply within a virtual wallet with no person or entity besides the "owner" having knowledge as to the content of that virtual wallet and therefore not developing a will of storing the cryptocurrency on behalf of the "owner". Finally it does not qualify as e-money within the meaning of § 1 (2) 3 ZAG, § 675f (4) 1 BGB, because this would require an obligation to at least some other persons to accept it with a certain value at a certain date. However, participants of cryptocurrency-transactions, including the initial issuer, do not take any obligations to bind themselves in that way.[10]

BaFin qualifies cryptocurrencies as **financial instruments** in form of units of account (Rechnungseinheiten) in the meaning of § 1 (11) 1 No. 7 KWG.[11] This official qualification can be considered binding as long as no court has ruled otherwise. It will constitute the base for further consequences, especially concerning legality and regulation as described infra.

However, with a decision dated 25.09.2018 the higher regional court in Berlin (i.e. Kammergericht, abbr.: KG) ruled in a criminal proceeding that Bitcoin lacks the general acceptance as a currency and therefore cannot be compared with the financial instruments under § 1 (11) 1 No. 7 KWG. The court criticized BaFin for its definition and argued that it cannot be the job of an administrative agency to do what is merely left for legislature.[12] However, this court decision has no direct impact on BaFin´s administrative practice. In the meantime BaFin reacted to this court decision and made clear that she looks at the decision with respect, but does not see a reason to change either her legal position nor her administration practice. The KG-decision is looked at merely as a decision in criminal law and therefore does not have any consequences for the administrative practice of BaFin, which follows rules of administrative law.[13] While it is very understandable for KG in a criminal proceeding to demand a clear legislative definition for what is allowed and what should be fined to meet constitutional standards that there may be no conviction, if not based on a clear and unambiguous law (Art. 103 (2) GG = Grundgesetz i.e. German Constitution: nulla poena sine lege), it has been

[9] Schlund/Pongratz DStR 2018, 598, 599; Spindler, Gerald/Bille, Martin: Rechtsprobleme von Bitcoins als virtuelle Währung WM 2014, 1357, 1360; Keding, Sebastian: Die aufsichtsrechtliche Behandlung von Machine-to-Machine-Zahlungen unter Rückgriff auf Peer-to-Peer-Netzwerke WM 2018, 64, 67; Djazayeri, Alexander: Die virtuelle Währung Bitcoin – Zivilrechtliche Fragestellungen und internationale regulatorische Behandlung jurisPR-BKR 6/2014 Anm. 1

[10] Schlund/Pongratz DStR 2018, 598, 599p.; Kaulartz, Markus: Die Blockchain-Technologie CR 2016, 474, 477

[11] BaFin, Hinweise zu Finanzinstrumenten nach § 1 Abs. 11 Sätze 1 bis 3 KWG, revisited 26.07.2018, 2. b) gg)

[12] KG judgement of 25.09.2018, (4) 161 Ss 28/18 (35/18)=NJW 2018, 3734=ZIP 2018, 2015

[13] Hufeld, interview with Handelsblatt, handelsblatt-online 28.10.2018

recognized that there may be different standards in criminal and administrative law. This is an example for the so-called split interpretation, between administrative agencies and criminal courts. While this split interpretation has been accepted over years in legal literature[14], the German Federal Court (BGH = Bundesgerichtshof) has denied this legal principle.[15] While, however the BGH is the highest authority in criminal and civil matters, it has no authority over administrative proceedings. The Federal Administrative Court (BVerwG = Bundesverwaltungsgericht), which is the highest authority in administrative proceedings has ruled to the opposite and stated that the fact that a clause may be not clear may only lead to the result that a criminal provision sanctioning non-obedience with the administrative guidelines cannot be applied. But this does not keep the administration from following its guidelines in the course of their administrative work.[16] The German Federal Constitutional Court (BVerfG = Bundesverfassungsgericht) kept up this line of BVerwG.[17] It will be interesting to see, where the courts and the legislature will be heading to. Following the FATC recommendations there is a high likelihood that pressure on the legislature will increase to more clearly open the door for regulation of cryptocurrencies. This would then lead to a legal justification of BaFin´s practice.At present BaFin may not invoke any criminal proceeding according to § 54 KWG, but may still issue a binding cease and desist order, which may be enforced as of itself.

# III. INITIAL COIN OFFERING

## 1. Description

Initial Coin Offering (ICO) is a **non-regulated method of collecting funds for crowdfunding based on distributed-ledger-technology (DLT)**. So called “tokens”, initially generated in a blockchain-process (so called “mining”) are issued in a publicly held bidding process to subscribers. The initiator describes the project in a so-called White Paper (technique, relevant market, development of the

[14] Schürnbrand, Wider den Verzicht auf die gespaltene Auslegugn im Kapitalmarktrecht, NZG 2011, 1213, 1215

[15] BGH NZG 2011, 1147

[16] BVerwG BVerwGE 106, 216 = NJW 1998, 2690 (2692) and BVerwGE 122, 29 = NZG 2005, 265 (270)

[17] BverfG NZG 2006, 499 (500) = NJW 2006, 3340

project). Additionally “Terms and Conditions” are issued with the legal frame for the ICO.[18] Subscribers pay their tokens in regular (Fiat) currency or in cryptocurrency according to those terms and conditions.[19]

The **tokens** issued differ with respect to the rights granted with them:

- Currency tokens work as currency and can be used outside of the token community to purchase goods or services from anybody who would accept those tokens as value. Those tokens build a cryptocurrency as of itself besides the established cryptocurrencies.
- Utility tokens do only grant rights inside the token community. They work like a digital voucher or license to be honored by the initiators of the ICO, usually granting rights to certain products (sometimes not even developed) or services, other tokens or rights to vote on functionalities of the product etc..
- Security tokens (aka equity or investment tokens) promise future capital, be it as interest, profit share or the like or stock shares or stock share options. They come close to venture capital investments or classical crowd investments.[20]

To qualify as **security** within the meaning of § 2 (1) WpHG/Art. 4 (1) No. 44 MiFID II a token needs

- Transferability
- Negotiability on financial or capital markets
- Embedded legal rights like shares in companies and other securities equivalent to shares in companies, partnerships or other entities, and depositary receipts in respect of shares; bonds or other forms of securitised debt, including depositary receipts in respect of such securities; or any other securities giving the right to acquire or sell any such transferable securities or giving rise to a cash settlement determined by reference to transferable securities, currencies, interest rates or yields, commodities or other indices or measures;
- Non-qualification as instrument of payment.[21]

The last point takes currency tokens usually out of the qualification as security, because they are designed to function as an instrument of payment.[22] Unlike BaFin in literature some authors demand the additional requirement of standardization, which they read from the term “categories of securities”.[23] However, for the issue of an authorization-requirement in form of a permit the test BaFin applies will be relevant, at least for practical use.

A token may from case to case be considered as share in investment assets within the meaning of § 1 (1) KAGB.[24]

---

[18] Weitnauer, Wolfgang: Initial Coin Offerings (ICOs): Rechtliche Rahmenbedingungen und regulatiorische Grenzen, BKR 2018, 231

[19] Schueffel, Fn. 1; BaFin: Hinweisschreiben (WA) WA 11-QB 4100-2017/0010 v. 20.2.2018, No. 5

[20] Weitnauer BKR 2018, 231, 232; Zickgraf, Peter: Initial Coin Offerings – Ein Fall für das Kapitalmarktrecht AG 2018, 293, 302; Klöhn, Lars/Parhofer, Nicolas/Resas, Daniel: Initial Coin Offerings (ICOs) – Markt, Ökonomik, Regulierung ZBB 2018, 89, 92

[21] BaFin, Hinweisschreiben v. 20.2.2018, 1. a)

[22] Zickgraf AG 2018, 293, 307

[23] Klöhn/Parhofer/Resas ZBB 2018, 89, 100; Zickgraf AG 2018, 293, 299

[24] BaFin, Hinweisschreiben v. 20.2.2018, 1. b)

A token may be considered an investment within the meaning of § 1 (2) VermAnlG, as long as it does not qualify as security (§ 2 (1) WpHG/Art. 4 (1) No. 44 MiFID II), as investment asset (§ 1 (1) KAGB), or as long as its acceptance does not constitute a deposit business (§ 1 (1) 1 No. 1 KWG). Depending on the specific design the token could be a share in a business entity (§ 1 (2) No. 1 VermAnlG), a partial loan (§ 1 (2) No. 3 VermAnlG), a subordinated loan (§ 1 (2) No. 4 VermAnlG), a participatory (§ 1 (2) No. 5 VermAnlG) or another investment (§ 1 (2) No. 7 VermAnlG).[25]

## 2. Legality

An ICO is not out of itself illegal. With an official notice letter BaFin has made clear that it is not the token, which is illegal, but certain services connected with those tokens may be, if rendered without proper permits or under violation of requirements for specific elements of the services rendered. BaFin pointed out that a general statement as to legality of tokens is impossible and that BaFin will consider on a case-by-case basis whether the services rendered constitute a violation of law. BaFin expressly focussed on similarities to securities and mentioned that it is not the labelling of the tokens as utility tokens or security tokens which decide on the required allowances, but rather the real rights granted by those tokens.[26] Relevant is an investigation into the economic substance of the token.[27]

In 2017 BaFin started 36 investigations as to the legality of ICO-services and ordered in four cases that the services rendered were without permit and needed to be stopped. The cases were forwarded to the prosecutors for further criminal action.[28]

## 3. Limitations for particular industries

There is no limitation for any particular industry. Any limitations are such of principle according to the specific service rendered on behalf of the tokens, but irrespective of any field of industry.

## 4. Requirements

### 4.1. Permit.

According to § 32 KWG a permit is required, if bank services are rendered professionally within a course of business (gewerbsmäßig). That means that offering ICOs does not require a permit as long as the initiator and the entity for which the funds are raised are identical. However, because the mining process already requires technical capacity usually not available for average companies they usually need specialised **service providers** to administer the ICO. Those service providers will then need a permit.

[25] BaFin, Hinweisschreiben v. 20.2.2018, 1. c)

[26] BaFin, Hinweisschreiben v. 20.2.2018, 1.a)

[27] Klöhn/Parhofer/Resas ZBB 2018, 89, 102

[28] Krempl, Stefan: ICO Bafin hat 2017 vier Crowdfundings mit Kryptogeld untersagt, Heise online v. 05.03.2018

The same would apply to **professional investment advisors** suggesting investment into tokens, be it a currency token, to be qualified under § 1 (11) 1 no. 7 KWG or a security token according to § 1 (1a) 2 no. 1 and 1a KWG, § 2 (8) 1 no. 4, 10 WpHG.[29]

Offering a **trading platform** for security tokens or currency tokens would qualify as multilateral trading system in the meaning of § 1 (1a) no. 1b KWG, which also requires a permit.[30] Trading with tokens may qualify as banking services in form of principal broking service within the meaning of § 1 (1) 2 No. 4 KWG or underwriting business within the meaning of § 1 (1) 2 No. 10 KWG, but may as well be financial services in form of investment broking within the meaning of § 1 (1a) 2 No. 1 KWG, operating a multilateral trading system within the meaning of § 1 (1a) 2 No. 1b KWG, placement business within the meaning of § 1 (1a) 2 No. 1c KWG, contract broking within the meaning of § 1 (1a) 2 No. 2 KWG, portfolio management within the meaning of § 1 (1a) 2 No. 3 KWG, proprietary trading within the meaning of § 1 (1a) 2 No. 4 KWG or asset management within the meaning of § 1 (1a) 2 No. 11 KWG.[31]

If the service provider combines his services with offering payment services, he will need a permit according to § 10 (1) ZAG as long as none of the exceptions of § 1 (1) no. 2 – 5 ZAG, for instance a CRR bank, applies.[32]

## 4.2. License.

A licensing out of permits is illegal and therefore void. However, ICO-service providers may cooperate with financial institutes, already holding a permit for bank services in that way that they render their services not independently, but rather under the roof of that financial institute.

## 4.3. Registration.

Permits are registered with BaFin according to §§ 32 pp. KWG.

## 4.4. Additional requirements.

Several regulatory limitations apply:

**Security tokens** are usually considered similar to ordinary securities so that the laws on security regulations apply:

- The offering of security tokens requires publication of a prospectus according to § 3 (1) WpPG.[33]
- If the funds are raised for a pool of investments rather than a single investment in the issuer´s own business, § 1 (1) KAGB applies. Such investment would be considered investment into an open

[29] Weitnauer BKR 2018, 231, 234

[30] Weitnauer BKR 2018, 231, 234

[31] BaFin, Hinweisschreiben v. 20.2.2018, 4.

[32] Weitnauer BKR 2018, 231, 234; BaFin, Hinweisschreiben v. 20.2.2018, 4.

[33] Weitnauer BKR 2018, 231, 233

investment pool limiting the offered investments to those types of securities expressly listed in §§ 192 pp., 219 KAGB.[34]

- The rules on insider trading (Art. 14 MAR), ad-hoc-publication (Art. 17 MAR), administering insider listings (Art. 18 MAR) and on director´s dealings (Art. 19 MAR) apply.[35]

Meanwhile BaFin has declared that real **utility tokens** just granting rights to purchase goods or services within the initiator´s own network are free of regulation.

## 5. Supervision

### 5.1. Supervisory authority.

The supervisory authorities for ICO are mainly **BaFin** and according to the specific details of the case also ESMA.

### 5.2. Notification of running business activity.

No specific notification requirements other than those mentioned under 4.4 supra apply arising simply out of the ICO. That will change as soon as the services are rendered in a way requiring a permit (in that case see 5.3).

### 5.3. Reporting.

The ICO itself does not constitute a reason for reporting. However, if the service provider offers services qualifying it as financial institution within the meaning of § 1 (1a) KWG or bank according to § 1 (1) KWG it has to fulfil the reporting requirements of § 24 KWG (for details see IV. 5.3 infra).

### 5.4. Security mechanisms.

So far no specific security mechanisms have been developed.

## 6. Summary

As long as the ICO is not administered by any service provider it is free of regulation, if the funds are raised against issuance of utility tokens.

If currency tokens or security tokens are given out, permits and additional requirements may apply. In those cases it would be recommendable to discuss the planned ICO with BaFin first and design the process according to the result of that consultation.

[34] Weitnauer BKR 2018, 231, 234

[35] Weitnauer BKR 2018, 231, 234

# IV. CRYPTOCURRENCY EXCHANGE

## 1. Description

A cryptocurrency exchange (aka **digital currency exchange** - DCE) allows customers to trade (i.e. buy or sell) cryptocurrencies or digital currencies for other assets, such as conventional fiat currencies or other cryptocurrencies. The business concept differs. Some take the bid-ask spreads as base for their transaction commissions (usual concept). Others charge fixed transaction fees for use of their platform.[36]

A digital currency exchange can be a **brick-and-mortar business** or a **strict online business**. As a brick-and-mortar business, it exchanges traditional payment methods and digital currencies. As an online business, it exchanges electronically transferred money and digital currencies. Exchanges may accept credit card payments, wire transfers or other forms of payment in exchange for digital currencies or cryptocurrencies.[37]

The cryptocurrency bought at the exchange platform can be sent to the user's personal cryptocurrency wallet. An alternative to this concept is converting cryptocurrency balances into anonymous prepaid cards which can be used to withdraw funds from ATMs worldwide. The creators of cryptocurrencies are often independent of the cryptocurrency exchange that trade in the currency. In one type of system, digital currency providers (DCP) are businesses that keep and administer accounts for their customers, but generally do not issue digital currency to those customers directly. Some exchanges are subsidiaries of DCP, but many are legally independent businesses. The denomination of funds kept in DCP accounts may be of a real or fictitious currency.[38]

**Decentralized exchanges** such as Etherdelta, IDEX and HADAX do not store users' funds on the exchange, but instead facilitate peer-to-peer cryptocurrency trading. Decentralized exchanges are resistant to security problems that affect other exchanges, but as of mid 2018 suffer from low trading volumes.[39]

Multilateral trading systems connect seller and buyer automatically, while both parties stay anonymous and cannot choose which partner to contract with. If there is a match between offer and acceptance the transaction closes automatically and the software handles the details.

## 2. Legality

A cryptocurrency exchange is not as of itself illegal. However, the specific concept may be considered illegal. Running a cryptocurrency exchange without the relevant **permit** will be considered illegal and is subject to fines and imprisonment.

[36] Wikipedia „Cryptocurrency Exchange“

[37] Fn 23

[38] Fn 23

[39] Fn 23

The legal consequences for cryptocurrency exchange platforms arise out of the legal qualification of the subject matter traded there. As pointed out before, cryptocurrencies are qualified as financial instruments within the meaning of § 1 (11) 1 No. 7 KWG.

## 3. Limitations for particular industries

There is no limitation for any particular industry. Any limitations are such of principle according to the specific service rendered on behalf of the exchange platform, but irrespective of any field of industry.

## 4. Requirements

### 4.1. Permit.

A permit according to § 32 (1) KWG is required, whenever the entity offers **banking services or financial services**, as long as those services are to be rendered professionally (i.e. "gewerbsmäßig") or to an extent requiring a merchantlike internal business organization (§ 1 (1) 1 KWG for banking or § 1 (1a) 1 KWG for financial services). "Gewerbsmäßig" is defined as being designed for a longer time period thereby expecting profits from such business. Therefore one-time-services will not fall under this provision. However, administering an exchange platform usually is meant to run for a longer time period.[40]

The services rendered need to qualify as banking services as described in § 1 (1) 2 KWG or financial services as described in § 1 (1a) 2 KWG.
If the exchange entity "gewerbsmäßig" buys and sells cryptocurrencies on commission (under its own name but to be accounted to the client), it will be considered **principal broking** (i.e. "Finanzkommissiongeschäft") within the meaning of § 1 (1) 2 no. 4 KWG and thus a banking service requiring a permit.

According to § 1 (1a) 2 KWG the following (among others) qualify as **financial services** requiring a permit:

*"1. the brokering of business involving the purchase and sale of financial instruments (investment broking, i.e. „Anlagevermittlung"),*
*1a. providing customers or their representatives with personal recommendations in respect of transactions relating to certain financial instruments where the recommendation is based on an evaluation of the investor's personal circumstances or is presented as being suitable for the investor and is not provided exclusively via information distribution channels or for the general public (investment advice, i.e. „Anlageberatung"),*
*1b. operating a multilateral facility, which brings together a large number of persons' interests in the purchase and sale of financial instruments within the facility according to set rules in a way that results in a purchase agreement for these financial instruments (operation of a multilateral trading facility),*
*1c. the placing of financial instruments without a firm commitment basis (placement business),*
*2. the purchase and sale of financial instruments on behalf of and for the account of others (contract broking, i.e. „Abschlußvermittlung"),*
*3. the management of individual portfolios of financial instruments for others on a discretionary basis (portfolio management),*

[40] Deutsche Bundesbank, Merkblatt über die Erteilung einer Erlaubnis zum Erbringen von Finanzdienstleistungen gemäß § 32 Absatz 1 KWG (4.11.2016), p. 2

*4. the*
*(a) continuously offering to purchase or sell financial instruments at self-determined prices on an organised market or in a multilateral trading facility,*
*(b) undertaking trading, often for own account, in an organised and systematic manner outside an organised market or a multilateral trading facility by providing a system accessible to third parties in order to transact business with these third parties,*
*(c) the purchase and sale of financial instruments for own account as a service for others or*
*(d) the purchase and sale of financial instruments for own account as a direct or indirect participant in a domestic organised market or multilateral trading facility by means of a high-frequency algorithmic trading strategy characterised by the use of infrastructures that are designed to minimise latency periods through system determination of order initiation, generation, routing or execution without human intervention for individual transactions or orders and by a high volume of intraday reports in the form of orders, quotes or cancellations, also where no service for others is rendered (proprietary trading, i.e. "Eigengeschäft"),"*

Each possible way of organizing a cryptocurrency exchange fits under on or another of the above mentioned provisions.

It does not help to avoid the permit-requirement, if the financial institute simply **resides outside of Germany**. As long as the financial services are rendered inside Germany or cross-border, the financial institute either needs to apply for a German permit or needs to show that it holds a comparable permit in its country of origin.

Additional permits may be necessary according to the special services offered:
If the exchange service provider combines its services with offering payment services, it will need a permit according to § 10 (1) ZAG as long as none of the exceptions of § 1 (1) no. 2 – 5 ZAG, for instance a CRR bank, applies.[41]

Providing accounts for the cryptocurrencies rather than transferring them into the buyer´s virtual wallet may qualify as banking service in form of deposit business according to § 1 (1) 2 no. 1 KWG.

## 4.2. License.

A BaFin permit cannot be licensed out by the holder of the permit. However it is legal to connect with the holder of the permit as a **contracted intermediary** ("vertraglich gebundener Vermittler") according to § 2 (10) 1 KWG that way slipping under the liability roof of the permit holder. Such contracted intermediaries do not need a separate permit for their business, if the permit holder (usually a CRR-bank) notifies BaFin about the agreement. BaFin will then list them in a public registry of contracted intermediaries visible in the internet according to § 2 (10) 6 KWG. Since 3.1.2018 BaFin also lists contracted intermediaries of out-of-state entities holding a comparable permit in their home state and offering their services across border in that registry (§ 53b (2a) 2 KWG).

## 4.3. Registration.

BaFin registers permit holders as well as their contracted intermediaries in a **public registry**.

[41] Weitnauer BKR 2018, 231, 234

### 4.4. Additional requirements.

The rules on insider trading (Art. 14 MAR), ad-hoc-publication (Art. 17 MAR), administering insider listings (Art. 18 MAR) and on director´s dealings (Art. 19 MAR) apply.[42]

## 5. Supervision

### 5.1. Supervisory authority.

The supervisory authority is BaFin.

### 5.2. Notification of running business activity.

(see 5.3)

### 5.3. Reporting.

Once the operator of the exchange qualifies as financial institution he has to obey the **reporting requirements** as set out in § 24 KWG:

*„(1) An institution shall report to BaFin and the Deutsche Bundesbank without delay*
*1. the intention to appoint a senior manager and to authorise a person to represent the institution in all aspects of its business, stating the facts which are germane to assessing his/her trustworthiness, professional qualifications and sufficient availability to exercise his/her respective tasks, as well as the realisation, withdrawal or change of that intention;*
*2. the retirement of a senior manager and the revocation of the authorisation to represent the institution in all aspects of its business;*
*3. changes in the legal form, unless authorisation is already required pursuant to section 32 (1), and changes in the firm name;*
*4. a loss amounting to 25% of eligible capital pursuant to Article 4 (1) number 71 of Regulation (EU) No 575/2013;*
*5. the relocation of the office or domicile;*
*6. the establishment, relocation and closure of a branch in a non-EEA state and the commencement and termination of the provision of cross-border services without establishing a branch;*
*7. the discontinuation of business operations;*
*8. the intention of its governing bodies appointed according to law and its articles of association to bring about a decision on the institution's liquidation;*
*9. a fall in the initial capital below the minimum requirements pursuant to section 33 (1) sentence 1 number 1, and the discontinuation of appropriate insurance cover pursuant to section 33 (1) sentences 2 and 3;*
*10. the acquisition or disposal of a major participating interest in its own institution, the reaching, exceeding or falling below the thresholds for participating interests of 20%, 30% and 50% of the voting rights or capital, and the fact that the institution becomes or ceases to be the subsidiary of another undertaking, as soon as the forthcoming change in these participatory relationships comes to the institution's attention;*
*11. each case in which the counterparty to a securities repurchase agreement, reverse repo, or a lending transaction in securities or commodities did not discharge his/her settlement obligations;*

[42] Weitnauer BKR 2018, 231, 234

*12. the emergence of, change in or termination of a close link with another natural person or another undertaking;*
*13. the emergence of, change in the level or termination of a qualifying participating interest in other undertakings;*
*14. the submission of a draft recommendation pursuant to section 25a (5) sentence 6;*
*14a. the approval of a higher variable remuneration component pursuant to section 25a (5) sentence 5 stating the approved increase of the variable remuneration component in relation to the fixed remuneration component;*
*15. the appointment of a member of the supervisory body, stating the facts which are germane to assessing his/her trustworthiness, professional expertise and sufficient availability to exercise his/her respective tasks;*
*15a. the retirement of a member of the supervisory body;*
*16. a change in the ratio of balance sheet capital to the sum of total assets, off-balancesheet liabilities and the replacement cost for claims arising from off-balance-sheet transactions (modified balance sheet capital ratio) of at least 5% based on the monthly return pursuant to section 25 (1) sentence 1 or the monthly balance sheet statistics pursuant to section 25 (1) sentence 3, in each case at the end of a quarter, in relation to the institution's approved annual accounts; where the institution prepares its accounts according to international accounting standards or is required to prepare interim accounts under the German Securities Trading Act, a corresponding change in the modified balance sheet capital ratio shall also be reported based on the interim accounts in relation to the approved annual accounts according to international accounting standards;*
*17. loans*
*(a) to limited partners, to shareholders in a private or public limited company or in a limited partnership company, or to shareholders in a public institution if they own more than 25% of the capital (nominal capital, total amount of capital shares) of the institution, or if they hold more than 25% of the voting rights, if these have not been granted on market terms or if they are not adequately secured in line with banking practice, and*
*(b) to persons who have granted loans, insofar as these are not loans pursuant to letter (a), pursuant to Article 26 (1) letter (a) and Article 51 letter (a) of Regulation (EU) No 575/2013 as last amended, if these are more than 25% of the Tier 1 capital pursuant to Article 25 of Regulation (EU) No 575/2013 as last amended Section 24 100 without taking account of capital pursuant to Article 26 (1) letter (a) and Article 51 letter (a) of Regulation (EU) No 575/2013 as last amended, if these have not been granted on market terms or if they are not adequately secured in line with banking practice.*

*(1a) An institution shall report to BaFin and the Deutsche Bundesbank annually*
*1. its close links with other natural persons or undertakings,*
*2. its qualifying participating interests in other undertakings,*
*3. the name and address of any holder of a major participating interest in the reporting institution and in the undertakings subordinated to it as described in section 10a that are domiciled abroad, as well as the amounts of these participating interests,*
*4. the number of its domestic branches,*
*5. the modified balance sheet capital ratio based on the approved annual accounts,*
*6. the classification as a major institution pursuant to section 17 of the Remuneration Ordinance for Institutions (Institutsvergütungsverordnung) of 16 December 2013 (Federal Law Gazette I page 4270) as well as a change in this classification,*
*7. if the institution is a CRR institution, the information that is required by the European Banking Authority to compare remuneration trends and practices within the meaning of Article 75 (1) of Directive 2013/36/EU in conjunction with Article 450 (1) letters (g) and (h) of the Regulation (EU) No 575/2013 as last amended, and*
*8. if the institution is a CRR institution, the information pertaining to senior managers and members of staff that earn total annual remuneration of at least €1 million within the meaning of Article 75 (1) of Directive 2013/36/EU in conjunction with Article 450 (1) letter (i) of the Regulation (EU) No 575/2013 as last amended that the European Banking Authority requires for publishing aggregate information.*

*(1b) When reporting a loan pursuant to subsection (1) number 17, the institution must state the collateral provided and the terms of the loan. Such loans which it has reported pursuant to subsection (1) number 17 shall be reported once again to BaFin and the Deutsche Bundesbank without delay if the collateral provided or the terms of the loans are contractually altered, together with the corresponding alterations. BaFin may require institutions to submit to itself and to the Deutsche Bundesbank every five years a summary report of the loans to be reported pursuant to subsection (1) number 17.*

*(2) An institution intending to merge with another institution within the meaning of this Act or with an e-money institution or a payment institution within the meaning of the Payment Services Oversight Act shall report this fact to BaFin and the Deutsche Bundesbank without delay.*

*(2a) A member of a supervisory body of a CRR institution that is of major importance within the meaning of section 25d (3) sentence 7, of a financial holding company or a mixed financial holding company shall inform BaFin and the Deutsche Bundesbank without delay Section 24 101 about the commencement and termination of activities as a senior manager or member of the supervisory board of another undertaking.*

*(3) A senior manager of an institution and the persons who actually manage the business of a financial holding company or a mixed financial holding company shall report to BaFin and the Deutsche Bundesbank without delay*
*1. the commencement and termination of activities as a senior manager or member of the supervisory board of another undertaking, and*
*2. the acquisition and disposal of a direct participating interest in an undertaking, as well as any changes in the amount of such a participating interest.*
*A direct participating interest within the meaning of sentence 1 number 2 shall be deemed to be the holding of at least 25% of the undertaking's capital.*

*(3a) 1 A financial holding company shall report to BaFin and the Deutsche Bundesbank without delay*
*1. the intention to appoint a person who is actually to manage the business of the financial holding company, stating the facts which are germane to assessing his/her trustworthiness, professional qualifications and sufficient availability to exercise his/her respective tasks, as well as the realisation of that intention;*
*2. the retirement of any person who has actually managed the business of the financial holding company;*
*3. changes to the structure of the financial holding group which mean that the group will, in future, be active across sectors;*
*4. the appointment of a member of the supervisory body, stating the facts which are germane to assessing his/her trustworthiness, professional expertise and sufficient availability to exercise his/her respective tasks;*
*5. the retirement of a member of the supervisory body.*
*A financial holding company shall submit to BaFin and the Deutsche Bundesbank annually a summary report of those institutions, German asset management companies, financial undertakings, ancillary service providers and payment institutions within the meaning of the Payment Services Oversight Act, that are subordinated undertakings within the meaning of section 10a. BaFin will transmit a list of these to the competent agencies of the other EEA states, the European Banking Authority and the European Commission pursuant to sentence 1. The establishment, modification or discontinuation of such participating interests or corporate relationships shall be reported to BaFin and the Deutsche Bundesbank without delay. Sentence 1 numbers 1 and 2 in respect of the persons who actually manage the business of this undertaking, sentence 1 numbers 4 and 5 in respect of members of the supervisory body of this undertaking as well as sentences 2 to 4 shall apply mutatis mutandis to mixed financial holding companies.*

*(3b) BaFin and the Deutsche Bundesbank may impose additional notification and reporting requirements on institutions or certain types or categories of institutions, in particular in order to obtain more in-depth insights into developments in the institutions' financial situation, into their principles of proper management or into the abilities of members of the institution's governing bodies where this is necessary to fulfil the tasks of BaFin and the Deutsche Bundesbank.*

*(4) The Federal Ministry of Finance, acting in consultation with the Deutsche Bundesbank, may issue by way of a statutory order more detailed provisions on the nature, scope, timing and form of the reports and on the submission of the documentation provided for in this Act, as well as on the permissible data carriers, transmission channels and data formats, and may supplement the existing reporting requirements by the obligation to submit summary reports and summary lists, insofar as this is necessary for the performance of BaFin's tasks and especially to enable it to obtain consistent records for assessing the banking business conducted and financial services provided by institutions. It may delegate this authority by way of a statutory order to BaFin, provided that statutory orders of BaFin are issued in agreement with the Deutsche Bundesbank. The central associations of the institutions shall be consulted before the statutory order is issued."*

### 5.4. Security mechanisms.

No specific security mechanisms have been developed with respect to cryptocurrency exchanges. The usual security mechanisms developed for banks and financial institutions apply.

## 6. Summary

Operators of cryptocurrency exchanges principally need a permit due to the intention to gain profits and third party relatedness of the business.[43] Such requirement may be avoided by slipping under the roof of a bank or financial institution already holding a permit by qualifying as contracted intermediary. However, even in that case a notification to BaFin is required.

[43] Spindler, Gerald/Bille, Martin: Rechtsprobleme von Bitcoins als virtuelle Währung, WM 2014, 1357, 1365

# V. SHOPPING WITH CRYPTOCURRENCY PAYMENT

## 1. Description

Cryptocurrencies are used as payment by use of **smart contracts**. Those contracts administered based on DLT-software connect transfer of the cryptocurrency payment to defined prerequisites, which could be proof of shipment of a good or rendering of services or vice versa could define transfer of the cryptocurrency as prerequisite of the shipment of goods or rendering of services.

Shopping against cryptocurrencies here shall be understood as an exchange of goods (or services or works) against cryptocurrencies. It is a contract inter partes. However, a platform for smart contracts run by a service provider could be used as well.

The legal characterization of the cryptocurrency transaction is not so easy. Usually "shopping" would be understood as a purchase agreement within the meaning of § 433 BGB: A seller offers a good for payment by the buyer. § 433 (2) BGB requires the buyer to pay the purchase price agreed upon. A purchase price, however, is understood as a certain amount of money. Money can only be a fiat currency, regardless of the specific currency, but not a virtual cryptocurrency not issued by any central bank. For cryptocurrencies lack the character of money, a transfer of cryptocurrency does not qualify as payment of a purchase price.[44] The contrary opinion, which defines cryptocurrency as debt over a certain value, which shall be sufficient to fulfil the requirement of "purchase price",[45] is not convincing. A debt needs a debtor, which is not in sight in case of cryptocurrencies.

While purchasing cryptocurrency against fiat money would qualify as purchase of rights within the meaning of § 453 (1) BGB in the variation of purchasing "other objects",[46] an initial agreement between the parties to exchange goods against cryptocurrency has to be characterized as exchange within the meaning of § 480 BGB, which, however, applies the rules of a purchase accordingly to the exchange.[47]

If the parties initially agreed on a purchase, i.e. goods against money, and later the buyer offers cryptocurrency instead, the initial contract is a purchase within the meaning of § 433 BGB and the later transaction of cryptocurrency has to face the problem of extinction of the obligation. Transfer of the cryptocurrency does not constitute an extinction by performance within the meaning of § 362 (1) BGB, because the obligee of the purchase did not render the "performance owed", which was money. Instead acceptance of the cryptocurrency by the seller constitutes an acceptance in lieu of performance according to § 364 (1) BGB.[48]

[44] Schlund/Pongratz DStR 2018, 598, 600; Shmatenko/Möllenkamp MMR 2018, 495, 500; Djayazeri jurisPR-BKR 6/2014 Anm. 1

[45] Ammann, Thorsten: Bitcoin als Zahlungsmittel im Internet, CR 2018, 379, 380

[46] Schlund/Pongratz DStR 2018, 598, 600

[47] Schlund/Pongratz DStR 2018, 598, 600; Shmatenko/Möllenkamp MMR 2018, 495, 500

[48] Shmatenko/Möllenkamp MMR 2018, 495, 500

This being the obligatory side of the transaction, it is even more difficult to legally explain the transfer side. §§ 929 pp. BGB do not apply, because of the numerus clausus of the rights of things, those provisions necessarily requiring a thing within the meaning of § 90 BGB, which does not apply to cryptocurrencies. Here it has been suggested that § 413 BGB can be used as omnibus clause, so that the transfer will be arranged according to §§ 413, 398 BGB by simple agreement to transfer the cryptocurrency.[49] However, this solution faces two problems. On one hand this requires acknowledgement of a right resting in the cryptocurrency. And on the other hand a simple agreement would not be sufficient, because the cryptocurrency also has to move from the virtual wallet of the buyer to that of the seller (or any other destination the seller has defined). It is a principle of a cryptocurrency transaction that said transaction necessarily will also include a transfer of the cryptocurrency in form of a new accountable assignment from the seller to the buyer.[50] A convincing solution to this problem remains missing.

If the contract, however, is one on the rendering of services in form of a service contract within the meaning of § 611 BGB or in form of a contract to produce a work within the meaning of § 631 BGB promising cryptocurrency for the service or work does not hurt, because both provisions do not require a price, i.e. money, but the agreed remuneration. Such remuneration does not have to be fiat money, but could be anything the parties agree upon as fair countervalue for the service or work, including cryptocurrency.[51]

## 2. Legality

Shopping contracts as defined supra are not out of themselves illegal. Illegality may arise out of the subject matter of the services to be rendered, unfair conditions or a severe misrelation between the values exchanged. However, here illegality does not arise out of the use of cryptocurrencies, but would apply to the same extent, if fiat currency were promised rather than cryptocurrency. The discussed solution to apply an analogy to §§ 873, 925 BGB[52] violates the numerus clauses of the rights of things and is thus not convincing. Therefore these cases will not be discussed further.

Illegality could apply, if a third party service provider without permit renders services with respect to the cryptocurrency, that would require a permit, e.g. certain payment processing services. However, again the illegality would not arise out of the shopping contract itself.

## 3. Limitations for particular industries

There is no limitation for any particular industry. Any limitations are such of principle according to the specific service rendered, but irrespective of any field of industry.

[49] Spindler/Bille WM 2014, 1357, 1362; Schlund/Pongratz DStR 2018, 598, 600; Zickgraf AG 2018, 293, 299

[50] Ammann CR 2018, 379, 382

[51] Shmatenko/Möllenkamp MMR 2018, 495, 500

[52] Fn 41

## 4. Requirements

### 4.1. Permit.

The parties of the shopping agreement do not need a permit.[53] Use of cryptocurrencies as described, namely simply for handling an exchange of goods, services or works against remuneration, does neither require a merchantlike internal business organization, nor is the use of cryptocurrencies motivated by the intention to gain profits.[54] Furthermore the decision to use cryptocurrencies arises out of an **inter partes agreement** and does not affect any public interests.

This may only be different, if the cryptocurrency itself becomes the subject matter of the sale.[55] Because cryptocurrencies are characterized as financial instruments within the meaning of § 1 (11) 1 No 7 KWG trading with them could constitute broking or security exchange or another financial service requiring a permit.[56] However, those cases have been described in chapters III. (ICO) and IV. (cryptocurrency exchange) and will not be repeated here, because they are not typical for the shopping contracts as defined under 1. supra.

### 4.2. License.

Consequently there is no room for any license.

### 4.3. Registration.

Cryptocurrency use in shopping contracts does not require any type of registration.

### 4.4. Additional requirements.

There are no specific additional requirements for those contracts arising out of the use of cryptocurrencies. Requirements could lie on service providers offering platforms for such contracts or who professionally sell cryptocurrencies. (see here the description in chapter III. ICO supra)

## 5. Supervision

### 5.1. Supervisory authority.

There is no relevant supervisory authority. BaFin will not look into such shopping contracts, but rather be interested in the details of any service contracts around the use of cryptocurrency.

[53] BaFin: Virtuelle Währungen/Virtual Currency (VC), 28.4.2016

[54] Spindler/Bille WM 2014, 1357, 1363

[55] Fn 42

[56] Schlund/Pongratz DStR 2018, 598, 601

### 5.2. Notification of running business activity.

No notifications are required.

### 5.3. Reporting.

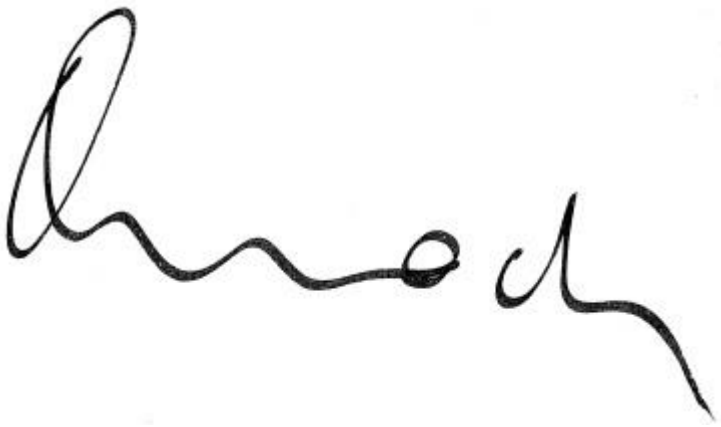
Without any supervision there is also no reporting duty according to those contracts.

### 5.4. Security mechanisms.

No security mechanisms apply.

## 6. Summary

The general legal principle of private autonomy allows contracts on shopping of goods, services or works against cryptocurrencies.[57] No regulation, permit or other limitation does apply to those contracts besides those limitations applying to any of such contracts, if the goods, services or works were offered against fiat currency.



Dr. Arnade

Rechtsanwalt

[57] Schlund/Pongratz DStR 2018, 598, 601; Spindler/Bille WM 2014, 1357, 1362