

The legality of online penny auctions in Germany

Online auction games (often called penny auctions) have become very popular in Germany and are offered in a plethora of types (variations of eBay, unique bid auctions, reverse auctions etc.). In a recent decision, the Administrative Court of Appeal of Baden-Wuerttemberg held that auction games may be regarded as illegal gambling and could therefore be prohibited by the competent authority. In older decisions, civil courts already had decided that contracts between a penny auction operator and a customer might be null and void. Martin Arendts, of Arendts Anwälte, explains the relevant case law and its consequences.

In the Baden-Wuerttemberg case, the plaintiff, a UK-based company, organised a website where electronic products in demand (like iPhones and tablets) were 'auctioned' on a countdown basis (a clock was counting the remaining time until the auction was supposed to end). In order to be able to place a bid for a product, the participant/customer had to purchase 'bidding points' (a virtual right to bid), and depending on the purchased amount, pay an auction fee of EUR 0.60 up to EUR 0.75 for a bidding point (*Gebotspunkt*). So, the operator generates most of its turnover not directly from the auction price (in practice, markedly below the street price, so participants are eager to recover 'sunk costs' and stake even more bidding points), but from auction fees, selling bidding points. In auction games, participants are usually not reimbursed for used bidding points (or other forms of auction fees).

If a participant uses a bidding point, the current bid price of the offered product increases by EUR 0.01 (a 'penny,' correctly a cent). The use also extends the duration of the auction for up to 20 seconds or longer. The participant who places the last bid wins the auction and can acquire the product.

In a letter dated 31 August 2011, the Regional Authority in Karlsruhe (*Regierungspräsidium Karlsruhe*), the central gambling authority for the State of Baden-Wuerttemberg, informed the operator that this activity constituted illegal gambling. The operator objected and argued that the auction was not a game of chance, but a competition, suggesting that the outcome depended on the skill of the participants. A participant can influence the competitors for a product by the election of his user name, the choice of auctions, the

date of his bids, the number of his bids or the pattern of bidding.

Nevertheless, the Regional Authority insisted that the auctions offered were illegal gambling within the meaning of section 3 of the Interstate Treaty on Gambling and issued a prohibition order, dated 14 November 2011. The operator filed an action against this prohibition order and requested its cancellation. The plaintiff argued that bidding for a product does not depend on chance, as each bidder had the opportunity to influence the course of the bid and outcome of the auction through their own actions. So it should be regarded as a kind of strategy game. The charges for the bidding points were merely a participation fee.

The Administrative Court of Karlsruhe dismissed these arguments and held that the online auctions were indeed illegal gambling¹. Although the cost of bidding was only EUR 0.60 to EUR 0.75, there was no *de minimis* threshold². As the whole system was aimed at inducing multiple bids, the sum of several bids was relevant. The bidding points were also not a participation fee, but a consideration for gambling. Only by staking a bidding point is the customer able to participate in the auction and to acquire a chance to win the auction. The winner of the auction is decided by hazard. Even if an above-average sophisticated bidder (under German gaming law, only the average participant is relevant) might use his bidding points in a successful manner, the outcome of the auction still depends on uncertain future events (whether another participant stakes a further bid). The unpredictable behaviour of other participants is random. This randomness cannot be distinguished from the general risk of living³.

According to the Administrative

Court of Karlsruhe, the auction also has to be characterised as a game (of no genuinely moral or economic purpose). A bidder in a classic auction was not risking any costs, if his bids were not successful. In penny auctions, a serious formation of prices was not visible. According to the court, the auctions of the plaintiff were offering playful attractions and amusement value and were therefore regarded as games⁴.

The operator appealed this first instance decision, which was heavily criticised in the legal literature as having looked only at the isolated case (possible further bids by a competitor), ignoring the overall view (the final successful bid)⁵. The auction fee for the bidding point could also not be regarded as a consideration for gambling.

The operator won the appeal. The Administrative Court of Appeal of Baden-Wuerttemberg cancelled the prohibition order with effect for the future⁶. The court of appeal argued that the Regional Authority abused its discretion as there was no consistent administrative practice.

Although the state had to pay the costs of the legal procedure, the decision might prove to be a pyrrhic victory for penny auction operators. With regard to the material legal points of the case, the court of appeal clearly followed the line of arguments of the first instance decision. So, new prohibition orders against penny auction operators might be upheld by the courts.

The court of appeal reaffirmed in its decision that the online auctions, offered by the plaintiff, were indeed a game of chance. The outcome predominantly depends on chance and not on the skill of the participants⁷. Even in an overall view the participants were staking the risks of a loss, typical for a

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game. A genuinely moral or economic purpose was lacking. The court of appeal also points to the fact that a successful bidder was in practice winning at the expense of the other participants. As a product can be won well below the normal price (theoretically with only one bidding point), the purpose of seriously buying a product stays on the sideline. According to the court of appeal, the decision whether a game is a game of chance has to be seen from an economic point of view. A success in the auction is predominantly determined by chance. It is typical for a game of chance that the winnings (valuable assets) are higher than the stake. Finally, the court of appeal held that under the current gambling law (Amended Interstate Treaty on Gambling, effective 1 July 2012) penny auctions were not approvable. The court points to the high frequency and the fact that customers were incited to stake further bids (and the risks associated with 'robots,' bidding software).

How auction fees, paid for bidding rights, are assessed by civil law is also highly disputed by German courts. The District Court of Kiel held that a contract for betting rights was perfectly legal and dismissed an action of an unsuccessful bidder, asking for a refund⁸. On the other hand, the District Court of Bochum argued that such a contract was indeterminate and in any case *contra bonos mores* (section 138 par. 1 German Civil Code)⁹. The court pointed to the fact that the contractual system was not transparent. Most participants would lose money without receiving a fair equivalent. In my point of view, it is quite likely that the civil court will follow the new administrative court decisions.

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1. Verwaltungsgericht Karlsruhe, decision of 15 November 2012, file no. 3 K 331/11, ZfWG 2013, 57.
2. Against Rotsch/Heissler, Internet- 'Auktionen' als strafbares Glücksspiel gem. § 284 StGB?, ZIS 2010, 403 et seq., 211, which argued in favour of a *de minimis* threshold of EUR 20.
3. Against Rotsch/Heissler, ZIS 2010, 403 et seq., 214.
4. Quoting Fritsche/Frahm, Zahlen schon fürs Bieten - Internetauktionen mit kostenpflichtigen Gebotsrechten, WRP 2008, 22 et seq., 33.
5. Diesbach/Mayer, Was ist zufällig an einer Auktion?, ZfWG 2013, 67 et seq.
6. Verwaltungsgerichtshof Baden-Württemberg, decision of 23 May 2013, file no. 6 S 88/13.
7. Quoting van der Hoff/Hoffmann, Der Einsatz von kostenpflichtigen Geboten bei Countdown-Auktionen - Kauf, Spiel, Glück?, ZGS 2011, 67 et seq.
8. Amtsgericht Kiel, decision of 16 December 2011, file no. 113 C 151/11, ZfWG 2013, 70.
9. Amtsgericht Bochum, decision of 8 May 2008, file no. 44 C 13/08.