FIN LAW

Copy Trading and Algorithmic Trading Software—What Are the Risks?

(11th of November 2026)

FIN LAW

Introduction to Copy Trading and Algorithmic Trading Software

Significance in modern finance

Both copy trading mechanisms and algorithmic trading software have evolved into widely used tools across international capital markets.

Mechanism of copy trading

In copy trading arrangements, retail investors systematically mirror the individual transactions and portfolio choices of selected third-party traders.

Functionality of trading bots

Algorithmic trading software connects directly to a user's brokerage account to independently analyze live market data and trigger transactions based on pre-programmed logic.

Substantial risk of financial loss

Because of high market volatility and leverage, automated and mirrored strategies frequently expose users to severe capital depreciation.

Legal uncertainty in loss scenarios

When significant trading losses occur, determining which participating entity carries primary legal liability remains a complex and contested issue.

Potentially Liable Parties in the Trading Ecosystem

Accountability of signal providers

Lead traders and signal creators can face civil liability if they disseminate deceptive performance statistics or make misleading promises regarding projected returns.

Responsibilities of trading platforms

Intermediary copy trading platforms become vulnerable to claims if they violate statutory consumer protection rules or fail to provide mandatory risk disclosures.

Liability risks for software developers

Providers of automated software are primarily exposed to claims arising from technical programming bugs, transmission failures, or inadequate operational warnings.

Execution duties of brokerages

Brokers executing automated orders bear legal responsibility whenever orders are routed erroneously or executed in breach of established execution standards.

Role of investor contributory negligence

The individual investor's own choices, including their risk appetite settings and strategy selection, play a decisive role when assessing potential damages.

Statutory Prerequisites for Damage Claims Under German Law



Strict compliance with legal elements

Under the German civil law framework, recovering capital requires fulfilling precise statutory conditions rather than merely demonstrating poor investment performance.



Requirement of a valid legal relationship

A claimant must establish the existence of a legally recognized relationship with the provider, which is typically grounded in a service or software contract.



Demonstration of a concrete breach

The investor bears the burden of proving that the counterparty committed a distinct and culpable breach of its contractual or statutory duties.



Establishment of causality and fault

Financial recovery is only possible if the breach of duty was committed with legal fault and directly caused the sustained monetary damages.



Insufficiency of trading losses alone

Experiencing market losses is an inherent risk of financial trading and does not, by itself, constitute sufficient grounds to establish legal liability.

Regulatory Classification and Licensing Obligations



Priority of economic substance over formal branding

Regulatory authorities evaluate business models based strictly on their actual operational functions rather than promotional terminology or marketing labels.



Licensing triggers for investment advice

A regulatory license becomes mandatory whenever a provider offers personalized, product-specific investment recommendations directly to individual clients.



Classification as financial portfolio management

Operating an automated system that independently makes and executes investment decisions within discretionary parameters generally triggers strict portfolio management licensing rules.



Distinction between software and financial services

Providing purely technical infrastructure must be clearly separated from activities that involve autonomous order routing or active investment brokerage.



Compliance with the German Securities Trading Act (WpHG)

Disseminating strategy signals or operating algorithmic trading software can impose formal notification requirements and strict governance duties under the WpHG.

Strategic Risk Mitigation and Contractual Design

01

Early-stage regulatory assessment

Developers and fintech providers should thoroughly audit their operational architecture and decision-making logic early to identify licensing obligations before going to market.

02

Viable operation without licensing

Through meticulous structural, contractual, and technical design, many trading software tools can be lawfully operated without obtaining a banking license.

03

Precise allocation of contractual relationships

The multilateral legal relationships connecting investors, software vendors, signal providers, and brokers must be clearly defined in separate agreements.

04

Comprehensive operational transparency

Providing exhaustive documentation regarding the functionality of algorithms and the realistic risks of total loss substantially limits civil liability exposure.

05

Implementation of technical safeguards and tailored terms

Deploying automated safeguards against order transmission anomalies, alongside carefully customized terms and conditions, forms an essential protective framework for providers.

Contacts

Dr. Lutz Auffenberg LL.M. (London)

German Attorney at Law,
Partner at FIN LAW,
Specialist Attorney in Banking
and Capital Markets Law



FIN LAW

Rechtsanwaltsgesellschaft
mbH

Senckenberganlage 19
60325 Frankfurt am Main

E. info@fin-law.de

I. https://fin-law.de

T. +49 69 87 000 1320