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THE IMPACT OF VIRTUAL ASSET REGULATION ON THE BALANCE OF DOMESTIC AND FOREIGN POLICY: THE DIMENSION OF NATIONAL SECURITY IN THE EUROPEAN SPACE

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Abstract

The article highlights the timeliness of researching the institutionalization of the virtual assets (VA) market, particularly cryptocurrencies, and its transformation from a niche technological innovation into a significant factor in international relations and public policy. It emphasizes that virtual assets challenge the state's traditional monopoly on money issuance and control over financial flows, creating new threats to national security. In response, governments are compelled to develop comprehensive public policies that lie at the intersection of competing interests. The study argues that this conflict of interests is especially acute in the European space, where the European Union, through the Regulation on Markets in Crypto-Assets (MiCA), seeks to establish uniform rules that will have global implications.

The purpose of the article is to determine how virtual assets influence the balance between domestic and foreign policy priorities of states and their role in ensuring national security within the European space. According to this purpose, the research sets the following objectives: to demonstrate that public policy on cryptocurrency regulation represents a point of convergence between internal and external political interests; to show that domestic policy in this area aims to protect consumers and combat crime; and to argue that in the sphere of foreign policy, this direction serves as a tool of geopolitical influence and protection of sovereignty for European states, thereby strengthening collective national security.

Thus, the political science conceptualization of cryptocurrency regulation is examined not as a technical or economic matter but as a strategic security task, in which the state must balance the competing imperatives of domestic innovation and external security. Regulation of virtual assets is no longer optional but has become a critical component of state policy. A successful balance between domestic (economic development) and external (security and sanctions) priorities will determine the resilience of the state in the new digital reality.

Keywords: state, EU, national security, regulatory policy, cryptocurrency, virtual assets, European space, domestic policy, foreign policy, MiCA, FATF.

Introduction. The study of the institutionalization of the virtual assets (VA) market, particularly cryptocurrencies, and its transformation from a niche technological innovation into an important factor in international relations and public policy, is both relevant and timely for modern political science in its theoretical and practical dimensions. Virtual assets challenge the state's traditional monopoly on money issuance and control over financial flows, creating new threats to national security. Unregulated VA circulation is used for money laundering, financing terrorism, circumventing international sanctions, and conducting cyberattacks.

In response, states are compelled to develop comprehensive public policies that emerge at the intersection of competing interests. On the one hand, domestic policy seeks to stimulate innovation, protect consumer rights, and collect tax revenues. On the other hand, foreign policy and national security demand strict control to prevent illegal cross-border activities and preserve financial stability. This conflict of interests is especially acute in the European space, where the European Union, through the Regulation on Markets in Crypto-Assets (MiCA), attempts to establish a single set of rules that will have global implications.

The purpose of the article is to determine how virtual assets influence the balance between the domestic and foreign policy priorities of states and their role in ensuring national security within the European space. To achieve this purpose, the study sets the following research objectives: to demonstrate that public policy on cryptocurrency regulation represents a point of convergence between domestic and foreign political interests; to note that domestic policy in this area aims to protect consumers and combat crime; and to substantiate that in the sphere of foreign policy, this area becomes a tool of geopolitical influence and protection of the sovereignty of European states, thereby strengthening collective national security.

The research methodology is based on political science analysis employing several approaches. The comparative method is used to examine regulatory models; the neo-institutionalist approach helps to analyze the role of new rules such as MiCA and FATF standards; and elements of the risk-analysis approach are applied to identify threats to national security.

The source base includes EU normative acts (MiCA, TFR), FATF reports, analytical papers (WEF, Chainalysis), and academic publications from 2021-2025.

Results. The European space, through the Regulation on Markets in Crypto-Assets (MiCA), demonstrates an attempt to create a "gold standard" of regulation, using the "Brussels effect" to extend its norms globally. This approach strengthens the collective national security of the EU member states but at the same time creates challenges for maintaining a balance with innovation policy. A key global actor that forces states to integrate domestic and foreign policy in this area is the Financial Action Task Force (FATF), particularly through the implementation of the "travel rule."

The scientific novelty of the article lies in the political science conceptualization of cryptocurrency regulation not as a technical or economic issue but as a strategic security task, in which the state must balance the contradictory imperatives of domestic innovation and external security.

The phenomenon of virtual assets (VA), led by cryptocurrencies, has undergone a rapid evolution – from a niche interest of narrow technical communities to a powerful factor in global politics. In 2024-2025, the stage of the "Wild West" is ending, giving way to the systemic institutionalization of this market. This process has a fundamental political dimension, as it directly affects the foundations of state sovereignty: the monopoly on money issuance and control over financial flows (ResearchGate, 2025).

The decentralized and cross-border nature of cryptocurrencies creates a unique set of threats to national security. They are actively used for money laundering, financing terrorism, and paying cybercriminals (for example, ransomware developers). Most notably, in the current geopolitical context, they serve as tools for bypassing international economic sanctions (TRM Labs, 2024). Reports from international analytical companies such as Chainalysis indicate that, although illegal operations account for a relatively small share of total volume, their absolute value is critical for the activities of criminal and hostile state actors [Chainalysis, 2025].

In response, states face a complex political choice in shaping independent public policies for regulating these aspects. Such policy becomes a point of intersection—and often conflict – between two core domains: domestic and foreign policy. Domestic policy focuses on supporting innovation, protecting consumer rights, and generating budget revenues through taxation (Zavada, 2022). In contrast, foreign policy and the security sector emphasize strict control, transparency, and compliance with international standards, particularly those of the Financial Action Task Force (FATF) (2025).

The most systematic response to this challenge is emerging within the European space. The adoption of the Regulation on Markets in Crypto-Assets (MiCA) in 2023 and its entry into force in 2024, along with the related Regulation on Transfers of Funds (TFR), which implements FATF standards, represents an unprecedented attempt to create a unified and comprehensive regulatory framework (European Parliament, 2024; FATF, 2024). Analyzing how MiCA balances domestic and foreign priorities is crucial for understanding the future of global financial governance and security policy.

The scientific discourse on virtual assets between 2021 and 2025 has shifted from primarily economic and technical analysis toward political science and security studies. Broadly, recent research can be divided into three groups.

The first group focuses on virtual assets as instruments of geopolitics and threats to national security. Scholars analyze the use of cryptocurrencies to bypass sanctions by state actors (such as Russia and North Korea) and to finance non-state groups, including terrorist organizations (TRM Labs, 2024; U.S. Department of the Treasury, 2025). In this context, the war in Ukraine has become a catalyst, demonstrating the dual role of cryptocurrencies: as a tool for providing rapid financial assistance to the victim of aggression, and as a potential means for the aggressor to evade restrictions (Joshi, N. 2025).

The second group of studies addresses regulatory responses, particularly in the European context. The main focus is on the MiCA Regulation, which analysts view as the EU's attempt to expand its regulatory influence globally (the "Brussels effect") by setting a "gold standard" for the industry (European Parliament, 2024). Meanwhile, Ukrainian authors actively examine the incorporation of MiCA provisions into national legislation, such as Draft Law No. 10225, which forms part of Ukraine's commitments on its path toward EU membership (Staryk, 2025).

The third group of works focuses on the role of international institutions, primarily the FATF. The organization's updated standards – especially Recommendation 15 and its "travel rule," which requires virtual asset service providers to exchange information about senders and recipients – have become a global driver of regulatory policy (FATF, 2025). Studies show that despite slow implementation, these standards are steadily compelling states to tighten control over the sector (FATF, 2024) and to seek a balance between domestic and foreign policy objectives.

Forming state policy on virtual assets requires balancing competing imperatives. On the domestic policy level, governments must address three core tasks: stimulating innovation, ensuring fiscal interests, and protecting consumers and financial stability. Excessively strict regulation risks stifling the industry or pushing it to other jurisdictions. Therefore, public policy should create incentives for the development of the fintech sector. Moreover, states seek new revenue streams through the taxation of VA transactions. In Ukraine, this issue remains highly debated and is reflected in recent legislative initiatives (Staryk, 2025; Zavada, 2022). Domestic policy also aims to protect citizens from fraud and excessive market speculation, which can have systemic consequences (Myronov, 2024). These goals generally call for legalizing and integrating virtual assets into the legal field while establishing clear rules of conduct.

In terms of foreign policy and national security, control and sanctions are key tools that define state sovereignty. Priorities in this domain differ fundamentally and focus mainly on oversight and restriction. A central element is combating illegal activity (AML/CFT) as a core national security requirement. The state must implement international standards, particularly those of the FATF, to prevent money laundering and terrorist financing (FATF, 2025). Another aspect concerns the international sanctions regime, as cryptocurrencies have become proven instruments for sanction evasion. For instance, the U.S. Department of the Treasury has repeatedly imposed sanctions on crypto mixers and exchanges associated with Russia and North Korea (TRM Labs, 2024; U.S. Department of the Treasury, 2025]. Consequently, controlling virtual assets has become an instrument of foreign policy used to exert pressure on hostile regimes.

Recent academic literature also draws increasing attention to monetary sovereignty, particularly in connection with the emergence of global private stablecoins and central bank digital currencies (CBDCs) of other states (for example, the digital yuan), which are viewed as direct threats to national sovereignty and thus require state-provided protective mechanisms (ResearchGate, 2025).

Within this context, the European space under MiCA serves as a model of balance. The MiCA Regulation represents a unique attempt to reconcile these two dimensions (European Parliament, 2024). On the domestic side, MiCA creates a single market through "passporting," allowing licensed companies to operate across the EU, which stimulates innovation. It also introduces strict consumer protection requirements and rules for stablecoin issuers (Pingen, 2023). On the external side, MiCA is closely linked with the Regulation on Transfers of Funds (TFR), which directly implements the FATF "travel rule." This enhances transaction transparency and significantly restricts the anonymous use of virtual assets for illicit purposes, strengthening the EU's collective security (FATF, 2024).

Thus, through MiCA, the European space addresses the problem of balance by setting a high regulatory standard. It functions not merely as an internal directive but as a foreign policy instrument that, through the "Brussels effect," compels companies and countries outside the EU (including Ukraine) to adopt these standards to gain access to one of the world's largest markets (European Parliament, 2024).

Therefore, state policy on the regulation of virtual assets has evolved from a narrowly specialized financial issue into one of the central components of national security strategy and political governance. The analysis demonstrates that effective public policy in this field requires a careful balance between domestic priorities (innovation, taxation, and consumer protection) and external priorities (anti-money laundering, sanctions enforcement, and protection of monetary sovereignty).

The European experience with MiCA and TFR implementation illustrates this balance model, where high standards of transparency and security (required by FATF) are integrated into a unified market mechanism. For Ukraine, which seeks EU integration, harmonizing national legislation with MiCA (Staryk, 2025). is not only a technical obligation but also a strategic step toward strengthening its own financial security and resilience amid hybrid aggression. Regulation of cryptocurrencies has ultimately become an integral part of the modern political process. A successful balance between domestic (economic development) and external (security and sanctions) priorities will determine a state's resilience in the new digital reality.

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