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RECALIBRATING GLOBAL MONETARY POWER: CBDC AS A STRATEGIC RESPONSE TO FINANCIAL WEAPONISATION

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I. ABSTRACT

This paper undertakes a doctrinal legal analysis of the weaponisation of finance and explores the potential of Central Bank Digital Currencies (CBDCs) and other digital monies as tools to mitigate such financial coercion. The weaponisation of finance refers to the strategic use of financial sanctions, currency restrictions, and control over international payment systems by states to achieve geopolitical aims. This phenomenon disrupts global financial stability, raising profound legal and normative questions about sovereignty, economic freedom, and human rights. Employing a doctrinal methodology, the paper critically examines the current legal frameworks governing sanctions law, monetary controls, and international financial regulations, analysing key statutes, treaties, regulatory policies, and case law. Special emphasis is placed on the advent of CBDCs, government-issued digital currencies with programmable capabilities that provide enhanced transparency, traceability, and regulatory oversight. The analysis highlights how CBDCs may serve as legal instruments to curb the Weaponisation of finance by enabling stricter compliance enforcement, enhancing monetary sovereignty, and offering alternatives to dominant global currencies subjected to unilateral sanctions. Concurrently, the paper assesses the risks related to privacy intrusions, potential governmental abuse, and fragmentation in the international monetary system due to competing CBDCs. The study concludes by emphasising the necessity for robust legal safeguards, multilateral regulatory cooperation, and clear central banking mandates to balance the benefits of CBDCs in countering financial weaponisation with protections for privacy and financial freedom. This research contributes to the intersection of international finance law and emerging digital monetary technologies, providing insights crucial for policymakers, legal scholars, and regulators navigating the complexities of finance, sovereignty, and technology in a rapidly evolving global order.

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II. KEYWORDS

Weaponisation of finance, Central Bank Digital Currencies, financial sovereignty, sanctions law, digital money.

III. INTRODUCTION

The increasing use of finance as a tool for power and political goals represents a major change in how countries exert influence and achieve their geopolitical aims. Instead of mainly using conventional military forces, modern states are increasingly turning to the financial system such as currencies, payment systems, capital markets, and regulatory frameworks as instruments of diplomatic pressure. In this new approach, access to global financial systems is seen as a valuable resource; while deliberately cutting off this access can cause economic damage without resorting to direct military conflict.

This development challenges traditional views that financial systems are neutral and raises important legal and ethical concerns related to sovereignty, economic freedom, and human rights. Within this broader trend, economic sanctions are a key example of financial coercion. There are generally two types of sanctions. Trade sanctions involve limiting the movement of goods and services through measures like trade bans, export controls, tariffs, and restrictions on certain industries such as energy or technology. Financial sanctions, on the other hand, directly affect monetary and financial systems.

They can include freezing a country's foreign reserves, blocking access to banking and payment networks, restricting access to financial markets, or preventing certain individuals or entities from interacting with regulated financial institutions. While both types of sanctions are often used together, financial sanctions have become more prominent because they can quickly and widely disrupt a target's economy while keeping military options available. The use of finance as a tool of foreign policy is not a random outcome of current systems but a planned strategy by states. It turns the financial system into a platform for political influence, where rewards and

punishments are carefully designed to shape the actions of other governments and non-state entities.

On one side, having access to strong and liquid financial markets, leading reserve currencies, and key payment systems can serve as strong incentives: countries that support the interests of a major financial power may find it easier to participate in the global financial system and gain favorable terms. On the other side, being cut off from these systems through sanctions, reducing exposure, or regulatory actions acts as a real threat of punishment meant to push for changes in policies. As stated by former U.S. Treasury Secretary Jacob J. Lew, commonly known as Jack Lew, the modern range of financial tools enables governments to "cripple a country financially without firing a shot,"² a statement that highlights the shift from physical force to financial means and needs to be examined carefully from a legal perspective.

This shift in using finance as a tool for coercive diplomacy has been made possible by the close connection between countries in the global economy and the fact that major financial control points are managed or influenced by a few states. The use of certain reserve currencies in trade and financial reserves, the role of specific financial centers in handling transactions, and the dependence on a small number of systems for international payments all create unequal power structures.

Countries that control or strongly influence these systems can use them to achieve their own or group foreign policy aims, sometimes pushing beyond current international laws related to sanctions, non-interference, and foreign jurisdiction. For countries affected by these actions and for many others watching from the side the situation raises worries about the loss of control over their own financial systems and the increasing political use of global financial resources. In this context, the emergence of Central Bank Digital Currencies (CBDCs) and other digital money systems has garnered increasing interest as a way to address these imbalances in power.

Digital currencies issued by governments, operated under public law, offer new levels of transparency, traceability, and control in monetary processes. Supporters suggest

² Jacob J. Lew, Remarks of Secretary Lew at CSIS (June 2, 2014), U.S. Dep't of the Treasury, <https://home.treasury.gov/news/press-releases/jl2414>. Accessed on 24th Oct, 2025

that these tools could strengthen a nation's monetary independence by decreasing dependence on foreign payment networks, by creating more direct and reliable ways for central banks to settle transactions, and by allowing for more accurate enforcement of sanctions and regulations. However, using CBDCs to counter the misuse of financial systems also introduces new legal challenges: increased monitoring capabilities, the risk of being excluded from digital financial systems without justification, and the possibility of greater division as different CBDC systems develop within separate geopolitical groups.

This paper explores how financial tools are used as instruments of power within the framework of sanctions law, monetary controls, and international financial regulations. It examines whether central bank digital currencies (CBDCs) and other forms of digital money can be used lawfully and ethically to counteract financial coercion. The paper begins with an analysis of legal texts, treaties, regulatory rules, and court decisions to define the legal aspects of trade and financial sanctions as tools of coercive diplomacy. It assesses how these tools align with principles such as national sovereignty, non-interference, and human rights.

The paper then investigates the legal structure of CBDCs, focusing on how these programmable and transparent digital currencies may enhance financial autonomy or, on the other hand, create new forms of control and exposure. The key argument is that digital monetary technologies have the potential to shift the power dynamics in the global financial system. However, without strong legal protections, clear guidelines from central banks, and effective international collaboration, attempts to regain sovereignty through digital currencies could end up reinforcing the very mechanisms of financial control they aim to challenge.

A. Statement Of Problem

The use of financial tools, such as economic sanctions, currency controls, and limitations on international payment systems, has become a major method of coercive diplomacy in modern geopolitics. Although these financial strategies allow powerful nations to exert influence without engaging in actual military conflict, they also cause

instability in the global financial system, challenge the independence of affected countries, and raise important questions about economic freedom and human rights. Current legal systems that regulate sanctions and monetary controls often fail to balance the needs of national security, state sovereignty, and the protection of human rights, particularly in a global economy where financial systems are largely controlled by a small number of influential nations. At the same time, the rise of Central Bank Digital Currencies (CBDCs) and other digital forms of money may change these dynamics by providing new ways to bypass or reduce the impact of coercive financial policies. However, the legal and regulatory effects of using digital currencies to restore sovereignty and resist financial weaponisation are not yet fully understood. This research aims to address these issues by thoroughly analyzing the legal principles of sanctions, monetary sovereignty, and the development of new digital currency systems.

B. Research Objectives

1. To Investigate the idea and application of using finance as a tool for coercive diplomacy, specifically through economic and financial sanctions.
2. To Review the current legal systems that regulate sanctions, monetary controls, and international financial rules to understand their shortcomings and conflicts in terms of norms and principles.
3. To Explore the possibility of using central bank digital currencies (CBDCs) and other government-backed digital forms of money as ways to protect monetary sovereignty and reduce the impact of financial weaponization.
4. To Evaluate the risks and legal issues that come with introducing CBDCs, including concerns about privacy, potential misuse by governments, and the risk of fragmentation in the global monetary system.
5. To Suggest legal protections, regulatory guidelines, and international cooperation structures needed to manage the advantages and challenges of CBDCs within the context of global financial influence.

C. Research Questions

1. How does the use of finance as a tool in foreign policy function, and what legal structures are in place to regulate its application?
2. What are the key differences and legal consequences of trade sanctions compared to financial sanctions in this context?
3. Can central bank digital currencies (CBDCs) and other digital monetary technologies improve a country's monetary independence and act as effective legal tools to resist financial weaponization?
4. What privacy concerns, human rights issues, and systemic risks are associated with using CBDCs as means to counter financial pressure?
5. What legal protections and international regulatory measures are needed to ensure that CBDCs support national sovereignty without increasing weaknesses?

D. Research Methodology

This research employs a doctrinal legal approach that involves a thorough examination of primary and secondary sources. It includes:

1. A detailed look at laws, international agreements, regulatory policies, and court decisions related to sanctions, financial controls, and the responsibilities of central banks in various legal systems.
2. An in-depth analysis of policy papers and official communications, particularly from central banks and international bodies, to better understand how legal rules are interpreted and how regulations are changing over time.
3. A focused study of legal concepts that address the relationship between national sovereignty, international financial law, and new forms of money, especially central bank digital currencies.
4. An assessment of the legal possibilities and consequences of using CBDCs as a response to financial weaponization, drawing on comparisons between different legal systems and incorporating insights from international politics and economics. This comprehensive doctrinal method seeks to create a detailed and principled understanding of how legal structures need

to adapt to the challenges presented by the misuse of financial tools in the digital age.

E. Review of Literature

1. **J. Caytas, "Weaponizing Finance: U.S. and European Options, Tools and Policies," *Columbia Journal of European Law* (2017):** Caytas looks into how financial sanctions have become a key tool for geopolitical influence, especially by the U.S. and EU after 9/11. The paper explains the important role that the U.S. dollar's global dominance and control over Western financial systems play in allowing these exclusionary measures. The analysis also points out potential dangers to fair legal procedures and worldwide financial stability if these tools are used without limits.³
2. **L. Quaglia & A. Verdun, "Weaponisation of Finance: The Role of European Central Banks and Financial Sanctions against Russia," *West European Politics*, Vol. 46, No. 5 (2023):** Quaglia examines how the European Central Bank and other Eurosystem central banks have been used to implement financial sanctions against Russia, describing this action as "monetary and financial warfare." The paper looks into the conflict between the independence of central banks and the political goals involved in enforcing these sanctions.⁴
3. **Center for Strategic & International Studies (CSIS), "The Weaponization of Global Financial Public Goods and Its Formation Mechanism," *CSIS Translation* (2023):** This study explains how the responsibility of nations for global financial systems creates situations that allow for the use of financial tools as a form of influence or coercion, with Western countries playing a

³ Caytas, Joanna, *Weaponizing Finance: U.S. and European Options, Tools, and Policies* (March 13, 2017). *Columbia Journal of European Law*, Vol. 23, No. 2, 2017, 441-475, Available at SSRN: <https://ssrn.com/abstract=2988373>. Accessed on 14th Oct 2025

⁴ Lucia Quaglia & Amy Verdun (2023) *Weaponisation of finance: the role of European central banks and financial sanctions against Russia*, *West European Politics*, 46:5, 872-895, DOI:10.1080/01402382.2022.2155906. Available at <https://doi.org/10.1080/01402382.2022.2155906>. Accessed on 14th Oct 2025

major role. It highlights globalization as both a factor that makes such actions possible and a domain where these tactics are actively employed.⁵

4. **International Affairs Institute (IAI), "The 'Weaponisation' of Money: Risks of Global Financial Fragmentation," Policy Paper (2025):** This paper examines how the freezing of Russia's central bank reserves and restrictions on Russian access to financial infrastructure have intensified concerns about the political use of money. It argues that such measures may encourage states to diversify reserves, increase reliance on gold, expand renminbi-based payments, and explore fintech or CBDC platforms, thereby contributing to long-term risks of global financial fragmentation.⁶
5. **Atlas Institute, "Weaponised Finance: Sanctions, SWIFT and Geopolitical Risk," Policy Brief (2025):** This brief analyses how control over SWIFT, dollar-clearing networks, and related financial infrastructure allows sanctions to operate as instruments of geopolitical pressure. It emphasizes that financial sanctions can influence state behaviour without military force, while also increasing political risk by pushing targeted states to seek alternative payment systems and reduce dependence on Western-controlled financial channels.⁷

F. Research Gap

While many studies have closely examined how financial sanctions are used as tools of political pressure and how certain countries hold major influence over global financial systems, there is still much to learn about the legal aspects of new Central Bank Digital Currencies (CBDCs) in relation to sanctions. There is not enough research looking at how laws related to sanctions, national monetary control, and digital

⁵ The Weaponization of Global Financial Public Goods and Its Formation Mechanism, CSIS Interpret: China (May 2023), <https://interpret.csis.org/translations/the-weaponization-of-global-financial-public-goods-and-its-formation-mechanism>. Accessed on Oct. 17, 2025.

⁶ International Affairs Institute (IAI), "The 'Weaponisation' of Money: Risks of Global Financial Fragmentation," Policy Paper (2025), 2024, Rome, IAI, June 2024, 16 p. (IAI Papers; 24 | 20), ISBN 978-88-9368-337-1, Available

⁷ Goktug Keskin, Atlas Institute, "Weaponised Finance: Sanctions, SWIFT and Geopolitical Risk," Policy Brief (2025), Available at <https://atlasinstitute.org/weaponized-finance-sanctions-swift-and-the-future-of-global-political-risk/>. Accessed on 28th Oct 2025

money interact, and whether they reduce or increase the use of financial tools as a form of coercion.

Also, few studies look closely at the conflict between the ability of digital currencies to enforce rules more effectively and the need to protect personal privacy, human rights, and the stability of the world financial system. As countries develop their own digital forms of money, there is a pressing need for legal research that connects these developments to current international laws and central banking rules, to understand both the benefits and risks of using digital money to regain control over financial systems without causing division or allowing authoritarian behavior.

This study seeks to address this gap by taking a comprehensive and multi-faceted legal approach. It aims to explain how CBDCs could change the international financial landscape in relation to sanctions and claims of national sovereignty, with special focus on legal protections and the need for cooperation between nations.

IV. RESULTS AND DISCUSSIONS

A. Structural Causes of Power Imbalance in the Global Financial System

Existing research⁸ clearly identifies three main factors that explain the long-standing imbalance of power in the global financial system. Based on Charles Kindleberger's important theory called Hegemonic Stability Theory, previous studies show that providing important financial resources that benefit the whole world such as stable currencies, payment systems, and financial safety nets relies on powerful countries that are willing and able to take on greater responsibilities to address shared challenges. Kindleberger's study of the period between the two world wars showed that without strong leadership from a dominant country, economic problems can worsen, as seen during the Great Depression.

The concept known as the "Kindleberger Trap" highlights the difficulties that arise during a shift in global leadership. It points out the risks when a major power loses its

⁸ The Weaponization of Global Financial Public Goods and Its Formation Mechanism, CSIS Interpret: China (May 2023), <https://interpret.csis.org/translations/the-weaponization-of-global-financial-public-goods-and-its-formation-mechanism> Accessed on Oct. 17, 2025.

ability or desire to lead, while other rising powers are not yet ready to take on those leadership roles, which can threaten the stability of the global financial system. The 2007 U.S. subprime mortgage crisis is an example of this. U.S. policies, including efforts to weaken the dollar for domestic economic growth, unintentionally reduced the dollar's role as a global reserve currency.

This led to a diversification of global currency reserves, with the Euro, British pound, Japanese yen, and more recently the Renminbi gaining more prominence. However, the U.S. dollar continues to hold the largest share of allocated global foreign exchange reserves, although its share has gradually declined. IMF COFER data shows that the dollar accounted for approximately 57.8% of allocated reserves at end-2024, declined to around 57.7% in Q1 2025, and stood at approximately 56.92% in Q3 2025. This downward movement supports the argument that, while dollar dominance remains substantial, reserve managers are slowly diversifying away from exclusive reliance on the U.S. dollar⁹. Furthermore, deep financial integration across the globe is often seen as increasing the vulnerability of states to coercive sanctions.

This is because powerful countries influence others by controlling major payment and settlement systems. As a result, this integration strengthens imbalances in power within international economic relationships. In addition, the continued use of the U.S. dollar as the main reserve currency provides considerable geopolitical influence, allowing for the ability to impose economic pressure and sanctions unilaterally.

B. Doctrinal Case-Law Framework on Economic Coercion and Financial Controls

A doctrinal analysis of financial weaponisation must also consider judicial treatment of economic coercion, sanctions, and financial controls. In *Military and Paramilitary Activities in and against Nicaragua* (*Nicaragua v. United States*), the International Court of Justice recognised the principle of non-intervention as part of customary international law and held that coercion becomes legally significant where it bears upon matters in which a state is permitted to decide freely.

⁹ Ibid

Although the Court did not treat every form of economic pressure as an unlawful use of force, it found that the United States' trade embargo violated obligations under the 1956 Treaty of Friendship, Commerce and Navigation. This demonstrates that economic measures may fall outside the law on armed force yet still attract legal consequences under treaty law, non-intervention principles, or other applicable rules of international law.

Sanctions-related financial controls have also been assessed in domestic and regional courts. In *Dames & Moore v. Regan*, the United States Supreme Court upheld executive measures connected with the Iranian asset's settlement, illustrating the broad but legally structured authority of the executive in emergency financial-control measures when supported by congressional acquiescence. By contrast, in *Kadi v. Council and Commission*, the Court of Justice of the European Union required EU implementation of UN asset-freezing measures to comply with fundamental rights guarantees, including judicial review and due process. WTO jurisprudence further confirms that security-based trade restrictions are not wholly immune from legal scrutiny.

In *Russia – Measures Concerning Traffic in Transit*, the WTO Panel held that invocation of the GATT Article XXI security exception is reviewable, even while recognising substantial deference to states in genuine emergencies. Collectively, these decisions show that financial weaponisation operates within legal limits: courts may defer to national security and foreign-policy discretion, but they also preserve review for treaty compliance, procedural fairness, proportionality, and good-faith invocation of security exceptions.

V. ALTERNATIVES TO THE CURRENT GLOBAL FINANCIAL ORDER AND THEIR LIMITATIONS

Some research points to various options aimed at addressing the geopolitical influence that exists within the existing international financial framework. These options involve converting gold into digital units that function as a standard form of gold, developing alternative currencies for trade invoicing, and building separate international payment networks. Although these approaches could, in theory, offer

ways to reduce reliance on dominant financial structures and lessen the impact of sanctions, real-world obstacles greatly limit their success. These challenges often lead to the continued division of the global financial system.

A. Gold Tokenization

Tokenized gold refers to digital tokens that are directly backed by physical gold reserves, offering a clear and intuitive "safe haven" asset with inherent value. However, several limitations reduce its effectiveness in supporting global trade.

First, the amount of physical gold available worldwide is not enough to support tokenization at the level needed for widespread international use.

Second, there are complex logistical and legal challenges related to the storage and management of gold. Gold stored within a country may have limited liquidity because it is difficult to move, while gold kept in foreign vaults puts holders at risk due to geopolitical tensions, as these foreign holdings can be more easily frozen or seized during conflicts or sanctions.¹⁰

Third, the lack of a unified global regulatory framework concerning ownership, custody, and cross-border transfer mechanisms hinders the smooth international use of gold tokens.

Lastly, market liquidity and adoption are hindered by inconsistent regulatory support and the early stage of this asset class, which limits tokenized gold's ability to fully replace sovereign reserve currencies or major invoicing systems.¹¹

B. Alternative Trade Invoicing Currencies and Payment Systems

China has been expanding its network of bilateral currency swap agreements¹², which are part of broader efforts to promote alternative trade invoicing currencies and payment systems. This initiative aims to lessen reliance on the U.S. dollar and the

¹⁰ Xavier Lavayssière, "Legal Structures of Tokenised Assets," *European Journal of Risk Regulation* (Cambridge University Press, 2025), DOI: 10.1017/err.2024.88 Accessed on 29th Oct 2025

¹¹ Financial Stability Board, *The Financial Stability Implications of Tokenisation* (22 October 2024), available on the FSB official website. Accessed on 12th Nov, 2025

¹² People's Bank of China, Report on Bilateral Currency Swap Agreements 4-12 (2024), <https://www.pbc.gov.cn/en/publications/reports> Accessed on 12th Nov 2025

financial infrastructure controlled by Western countries. These swap agreements allow China and its trade partners to settle international transactions directly using their local currencies, particularly the Renminbi (RMB), bypassing the dollar and avoiding the risks associated with currency exchange. Studies show that these bilateral currency swaps have significantly boosted trade between China and its partners by lowering transaction costs and helping manage exchange rate fluctuations. They also provide a financial safety net during global economic disturbances and offer a more affordable option compared to dollar-based trade invoicing and settlement.

The People's Bank of China has been steadily increasing the number of countries involved in this swap network, which now includes over 40 nations. This allows traders to conduct business using the RMB or local currencies under formal agreements.

In addition to swap lines, China has also developed the Cross-Border Interbank Payment System (CIPS), which facilitates the clearing and settlement of RMB-based international payments.¹³ This system serves as an alternative to SWIFT, the widely used global financial messaging network. While CIPS currently handles a smaller volume of transactions compared to U.S.-dominated systems, its usage has grown significantly since 2022 due to sanctions and geopolitical developments.

Despite these advancements, the alternative currency and payment frameworks face several challenges. Their scope is limited geographically and politically, as adoption is typically limited to bilateral or regional agreements rather than a global standard. There are also difficulties in making different systems work together smoothly. Trust issues, particularly regarding regulatory transparency and the rule of law in non-Western regions, further hinder the widespread acceptance of these systems. As a result, rather than creating a unified global financial system, these developments are contributing to monetary fragmentation, with regional currency blocs vying for

¹³ People's Bank of China, Cross-Border Interbank Payment System (CIPS): System Overview 3-20 (2024), <https://www.cips.com.cn/en/>. Accessed on 15th Nov, 2025

influence¹⁴. This makes it harder to build a fully integrated, multipolar global financial system.

C. Role of CBDC

Central Bank Digital Currencies (CBDCs) mark a new development in the way money is structured, introducing state-supported digital money that could change how monetary and financial systems operate worldwide.¹⁵ Different from cryptocurrencies or private stablecoins, CBDCs are created by central banks and are fully backed by the legal authority of national monetary institutions. This ensures that holders have a direct claim on the central bank, reflecting a level of trust equivalent to the government itself.

1. Transformative Potential and Functional Advantages

CBDCs have the potential to strengthen the core role of central bank money in the digital economy by making domestic and cross-border payments faster, more secure, and more efficient.

They help maintain the stability of national currencies even as the use of physical cash decreases, while also offering features like programmability and transparency, which improve how regulators monitor and enforce financial rules. This digital form of money can promote financial inclusion by providing secure digital payment options to people who do not have access to traditional banking services, through central bank-issued digital wallets, without relying on conventional banking systems.

Importantly, CBDCs can improve how monetary policies are carried out by allowing central banks to track money movements in real time and carry out precise interventions effectively, including measures to manage the flow of capital. Their ability to be programmed also aids in preventing illegal activities like money

¹⁴ International Monetary Fund, *Geo-Economic Fragmentation and the Future of Multilateralism*, Staff Discussion Note No. 2023/001 (15 January 2023); see also IMF Blog, "The High Cost of Global Economic Fragmentation" (28 August 2023). Accessed on 15th Nov, 2025.

¹⁵ Int'l Monetary Fund, *CBDCs and the Future of Payment and Monetary Systems 10-23* (2022), <https://www.imf.org/en/Publications/WP/Issues>. Accessed on 10th Nov, 2025

laundering and financing of terrorism, thanks to built-in systems that ensure compliance with legal standards.

2. CBDCs as Tools to Counteract Financial Weaponization

Financial weaponization usually occurs through sanctions that exclude certain countries or groups, enforced through major payment systems controlled by dominant global powers, primarily using the U.S. dollar and networks like SWIFT. CBDCs provide affected states and groups with a sovereign tool to create alternative payment systems and currency frameworks that are less dependent on the infrastructure of dominant powers. Their programmability may allow real-time monitoring, settlement finality, and compliance controls without relying entirely on correspondent banks or externally controlled messaging networks.

Project mBridge provides the most significant practical example of this possibility. Developed from 2021 by the BIS Innovation Hub with the Hong Kong Monetary Authority, the Bank of Thailand, the Central Bank of the United Arab Emirates, and the Digital Currency Institute of the People's Bank of China, mBridge is a multi-CBDC platform designed to support instant cross-border payments and settlement through a shared distributed-ledger infrastructure. In June 2024, the project reached the minimum viable product stage, and the Saudi Central Bank joined as a full participant, making the platform directly relevant to debates on non-dollar settlement and alternative payment infrastructure.

Legally, mBridge illustrates both the promise and risk of multi-CBDC systems. On one hand, it demonstrates how participating central banks may create sovereign digital settlement channels that reduce dependence on SWIFT-linked correspondent banking and dollar-clearing networks. On the other hand, such platforms require clear rules on jurisdiction, settlement finality, central-bank liability, data governance, AML/CFT compliance, sanctions screening, and dispute resolution. Without transparent governance and internationally accepted compliance standards, multi-CBDC systems could be criticised as mechanisms for sanctions avoidance or bloc-based monetary fragmentation. Accordingly, mBridge strengthens the paper's central claim that CBDCs may counter financial weaponisation, but it also shows that such systems must

be embedded within robust legal safeguards to avoid simply relocating financial coercion into new digital infrastructures.

3. Legal and Regulatory Frameworks

The framework governing Central Bank Digital Currencies (CBDCs) is changing quickly around the world, with different countries adopting varied strategies based on their legal systems, focus on monetary policy, and international political factors.

- **United States:** The United States currently adopts a restrictive approach toward central bank digital currencies (CBDCs). Executive Order 14178, titled *Strengthening American Leadership in Digital Financial Technology* and issued on January 23, 2025, prohibits federal agencies from taking action to establish, issue, circulate, or promote a CBDC within the United States. This position reflects concerns relating to financial privacy, monetary sovereignty, financial stability, and the risk of excessive governmental control over digital money. Separately, the *Anti-CBDC Surveillance State Act* seeks to convert this policy position into statutory law by restricting the Federal Reserve from developing or issuing a CBDC without express congressional authorization. This proposed legislation should therefore be distinguished from the Executive Order, which itself operates as an executive prohibition rather than a conditional approval mechanism. At the same time, U.S. digital-asset policy continues to support regulated private-sector payment innovation, including stablecoin regulation, while rejecting the introduction of a federally issued CBDC.
- **China:** China has been actively developing its digital yuan (e-CNY), supported by well-defined laws that give the People's Bank of China the authority to issue it, making it a legally recognized form of currency. The legal structure includes comprehensive regulations focused on protecting privacy and ensuring strict compliance with anti-money laundering (AML) and counter-terrorism financing (CTF) rules, as well as the enforcement of sanctions. The integration of the digital yuan into

regional cross-border payment systems like CIPS is made possible through coordinated legislative and regulatory efforts. China's legal approach to its digital currency reflects a model centered on national sovereignty, aiming to drive financial innovation and inclusion within the country while also strengthening its geopolitical financial independence and ability to resist external financial pressures.

- **European Union:** The European Central Bank (ECB) is working on a digital euro initiative that is supported by regulatory guidelines focused on safeguarding consumers, maintaining data privacy in line with the General Data Protection Regulation (GDPR), and ensuring financial stability. The ECB is involved in wide-ranging discussions to develop rules that ensure the digital euro meets anti-fraud, anti-money laundering (AML), and sanctions requirements, while also preserving user anonymity as allowed by law.

EU regulations are designed to ensure smooth operation across all member countries through unified oversight structures, reducing the chances of inconsistencies within the single market and supporting seamless cross-border digital transactions.

VI. INTERNATIONAL COORDINATION AND STANDARDS

International organizations like the Bank for International Settlements (BIS), International Monetary Fund (IMF), and Financial Action Task Force (FATF) are key in setting global standards and best practices for regulating central bank digital currencies (CBDCs).

The BIS Innovation Hub works on multi-CBDC pilot programs to improve compatibility and alignment of regulations across countries. The FATF provides clear guidance that anti-money laundering (AML) and counter-terrorist financing (CTF) rules, as well as sanctions compliance, must be updated to fit digital currency systems. This approach focuses on regulating based on risk level

A. CBDC Legal Framework Components and Their Role Against Financial Weaponization

A well-functioning CBDC regulatory framework generally includes the following elements:

1. **Issuance and Legal Tender Status:** The central bank must have clear legal authority to issue and distribute digital currency as official money, backed by the state to ensure its validity and acceptance.
2. **Privacy and Data Governance:** Laws should set clear boundaries on how data is collected and shared, ensuring that individual privacy is protected while still allowing for the necessary level of transparency required for regulatory purposes.
3. **AML/CTF and Sanctions Compliance:** Regulations must include built-in tools for monitoring transactions and enforcing rules, which allow for accurate implementation of sanctions and help in preventing the use of CBDCs for illegal financial activities.
4. **Interoperability and Cross-border Regulation:** Legal structures should support collaboration between different countries to prevent regulatory gaps and ensure smooth and secure international transactions.
5. **Governance and Oversight:** There should be clearly defined roles and responsibilities for the central bank, including managing operational risks and maintaining public accountability, to prevent misuse and ensure the system remains stable and trustworthy.

VII. SUGGESTIONS

1. **Clear statutory authority for CBDC issuance:** States should enact specific legislation defining the legal status, issuance authority, operational limits, and accountability mechanisms for CBDCs.
2. **Privacy and data-protection safeguards:** CBDC frameworks should incorporate strong data-governance rules to prevent disproportionate surveillance and misuse of personal financial information.
3. **Due-process protections against arbitrary exclusion:** Any freezing, blocking, or restriction of CBDC accounts should be subject to legal standards, notice requirements, review mechanisms, and remedies.

4. **International interoperability standards:** Multilateral institutions such as the BIS, IMF, FATF, and central banks should develop interoperable standards for cross-border CBDC use, settlement finality, AML/CFT compliance, and sanctions screening.
5. **Prevention of financial fragmentation:** CBDC systems should be designed as cooperative and interoperable public infrastructures rather than closed geopolitical blocs that may deepen monetary fragmentation.
6. **Regulation of programmable features:** The programmable functions of CBDCs should be legally restricted to legitimate regulatory purposes and should not be used for arbitrary political control or economic coercion.

VIII. SCOPE FOR FURTHER RESEARCH

The ongoing development of central bank digital currency (CBDC) offers many opportunities for further academic investigation:

1. **Empirical Studies on CBDC Adoption and Usage Patterns:** In-depth examination of how users interact with CBDCs during pilot programs, such as China's e-CNY, can clarify factors that influence public acceptance and identify possible side effects, including the reduced role of commercial banks.
2. **Comparative Legal Analysis of National Frameworks:** There is a need for research that explores how different legal systems and governance structures affect the design of CBDCs, the level of privacy protection they offer, and the effectiveness of international cooperation.
3. **Impact on Geopolitical Power Dynamics:** Academic studies that combine various fields of knowledge can help understand how CBDCs affect global financial structures and economic relationships, offering insight into their influence on international politics.
4. **Technological Innovation and Privacy-Enhancing Mechanisms:** Investigating advanced technologies like cryptographic techniques such as zero-knowledge proofs and secure multi-party computation can lead to improvements that enhance user privacy while still allowing for effective regulation.

- 5. Risks of Financial Fragmentation and Systemic Stability:** Future research should examine possible outcomes of widespread CBDC implementation, including the risks of financial fragmentation, the strength of existing safety measures, and the need for coordinated monetary policies among different countries.

IX. CONCLUSION

CBDCs represent a significant legal and technological development in the evolution of sovereign money. Their potential lies not merely in improving payment efficiency, but in reshaping the relationship between monetary sovereignty, sanctions compliance, financial autonomy, and global payment infrastructure. The analysis shows that CBDCs may provide states with alternative mechanisms to reduce dependence on dominant financial networks and mitigate the risks of financial weaponisation. However, this potential is conditional upon the existence of clear statutory mandates, privacy safeguards, transparent governance structures, and internationally coordinated standards.

At the same time, CBDCs may also create new risks, including excessive state surveillance, arbitrary exclusion from digital payment systems, cybersecurity vulnerabilities, and fragmentation of the international monetary order. Therefore, CBDCs should not be understood as a complete solution to financial weaponisation, but as legally sensitive instruments whose legitimacy depends on careful regulatory design. The doctrinal analysis demonstrates that any CBDC framework must balance monetary sovereignty with due process, human rights, proportionality, and accountability.

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