Rate of Change Consensus

To achieve sustainability, Aave must combine value creation

under favorable market conditions with protection

of itself and its users when conditions become unfavorable [1].

Aave must be able to lower the liquidation threshold of collateral assets to reduce the risk it and its users face under those adverse conditions

. While loan-to-value and liquidation bonus are also useful means of reducing the risk of insolvency, they are not effective substitutes.

Over the last several weeks, Gauntlet has collaborated with BGD Labs, Llama, Governance House, and other community stakeholders to align on how to most effectively serve the protocol regarding the tradeoffs between value creation and protection.

Liquidation threshold reductions can impact users in a number of ways. In particular, if a user's account health is low, this type of parameter change can render the account eligible for liquidation.

If a user rebalances their position ahead of a liquidation threshold reduction, they will avoid liquidation. For this reason, Gauntlet will provide notice to the community via communication channels that may include the forums and Twitter, among others.

That said, there is always some chance that a user will not monitor their health factor or fail to supply collateral in time, resulting in "risk-off liquidations".

BGD, Llama, Governance House, and other community members have emphasized that these liquidations impinge on the borrower user experience. It is therefore important that the community explicitly aligns on a desired maximum reduction to liquidation thresholds per AIP.

Community input is also valuable because limits on LT reduction impose an important trade-off:

1. A lower max LT reduction will minimize the impact to borrowers but at the cost of reducing the rate at which risk can be taken off. This, in turn, limits the extent to which leverage can be increased during favorable conditions, making Aave less capital efficient and coming at the cost of borrow volume.

2. A higher max LT reduction will strengthen Aave's ability to maximize capital efficiency under favorable market conditions but increase the potential for risk-off liquidations.

A Snapshot vote will be published with the options being the following: Per AIP, each collateral asset's liquidation threshold may be reduced by an absolute percentage of up to:

- 3% (see point (2) above)

- 2%

- 1% (see point (1) above)

Note:

- This limit would not

apply under severe conditions, such as a contract vulnerability.

- It would

apply to all collateral assets Gauntlet supports, including WETH, WBTC, DAI, &c. [2].

Next Steps:

Gauntlet will create a Snapshot vote immediately. Voting ends on Wednesday, July 27.

[1] Please find a detailed explanation of Gauntlet's Risk Management methodologyhere.

[2] A complete list of currently supported assets can be foundhere.