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Subsidy Fund Proposal from the Arbitrum DAO Procurement Committee

Executive Summary

As voted on in the ADPC proposal [here](#), one of the key tasks of the ADPC was to conceptualize and structure a subsidy fund for the Arbitrum DAO. This proposal intends to set up this subsidy fund, seeking \$10 million worth of ARB to be administered and selected by the Arbitrum DAO Procurement Committee (hereinafter referred to as the 'ADPC') to facilitate the selection of projects that will benefit from the whitelisted security audit service providers selected via the ADPC's procurement framework. The ultimate decision will be made by the ADPC based on the Means Test and the [Application Process Terms](#).

Proposal Request

We propose the creation of a procurement subsidy fund allocating \$10 million worth of ARB to provide financial assistance to both new and existing projects within the Arbitrum ecosystem.

These subsidies will be exclusive to a pre-approved whitelisted set of security audit service providers, selected by the ADPC, who will publicly display their fees. This approach eliminates the need for the ADPC to assess the reasonableness of funds requests.

The aim of the subsidy fund is to incentivise participation and growth among smaller projects helping them to overcome barriers to entry, such as challenges to acquire funding to pay for the cost of robust security audits.

The figure of \$10 million worth of ARB has been determined via a benchmarking exercise conducted with various security audit service providers. This [form](#) was shared with these service providers and based on the responses of 10 service providers (including the likes of Spearbit, Halborn, Nethermind, Three Sigma, Guardian, Zellic, etc.) on their scope of services and fees associated, we have estimated that each project will require a 2-month security audit at an average cost of \$200K. This will enable the ADPC to potentially fund up to 50 projects; however, it should be noted that the average of \$200K is an estimate and fees are usually specific to each project, each project requires a scoping exercise, and audit costs will vary based on the size of the codebase, complexity, etc.

Any feedback on this proposal is encouraged via a public discussion on the community forum.

Subsidy Fund Design & Approach

Exec View

- \$10 million worth of ARB allocated across ~50 projects to spend on whitelisted security audit service providers, with an average amount of \$200K worth of ARB allocated per project and a max cap of \$500K per project.
- ADPC responsible for selection and oversight.
- Our aim is to distribute the Subsidy Fund in an 8-month period, in 4 cohorts of 8 weeks each.

Key Pillars

(A) Subsidy Fund Principles and Criteria

Core Principles Underlying the ADPC Subsidy Fund

Before considering a subsidy application, applicants should carefully evaluate the need for support. The purpose of these guidelines is to clarify the subsidy program and make the process as straightforward as possible.

All applicants should keep in mind the following key principles:

1. Transparency & integrity
2. Applicants must disclose any potential conflicts of interest and receipt of any prior funding.

3. Encouragement of investment
4. Subsidies should incentivise investment that would not otherwise occur without the subsidy. They should not cover costs that the beneficiary would have funded independently in the absence of any subsidy.
5. Proportionate and necessary
6. Subsidies should be proportionate to their intended objective and limited to what is necessary to achieve it.
7. Economic neutrality
8. The requested subsidy amount should not confer an economic advantage. It should be provided on fair terms, comparable to what could reasonably be obtained on the market.
9. Consideration of funding options
10. Applicants are expected to explore all available funding options and responsibly choose the option that best suits their needs.
11. Enhancement of beneficiary security
12. Subsidies should bring about changes that enhance the security of the beneficiary's protocol.
13. Positive impact on the Arbitrum ecosystem
14. Subsidies should have a beneficial effect on the Arbitrum ecosystem, contributing to its growth and sustainability.
15. Value for Money
16. The evaluation method should ensure decisions maximize both financial and non-financial value to Arbitrum.
17. Probity
18. Subsidies should be issued in an environment that ensures fairness, impartiality, and compliance with established guidelines and rules. There will be an emphasis on transparency, accountability, and integrity throughout the procurement process, evidenced by the development of this publicly documented Means Test methodology. This focus on Probity will mitigate procurement risks and safeguard the integrity of the procurement process.
19. Risk Management
20. Risk management policies will be implemented to identify and mitigate procurement risks.
21. Engagement with SMEs
22. We have invited a wide range of organisations to participate, all of whom will be subject to the eligibility criteria.
23. Cyclical Whitelist events
24. We will have clear rules for cyclical whitelist reviews to open a pathway for future applicants and new market entrants.

Means Test: Criteria for Evaluation

The reason for this approach over a purely quantitative approach is that most projects, especially the smaller ones being targeted within this subsidy program do not possess obvious immediately measurable metrics.

The development of this Means Test aims to provide a structured approach for the ADPC to evaluate applications for financial assistance. This tool is designed to identify applicants who would benefit most from support, ensuring equitable access to subsidies within the Arbitrum Ecosystem, particularly for smaller entities with valuable contributions.

The intent is to allocate subsidies to those most in need, avoiding exploitation by larger players looking for a 'free lunch/handout'. Such an event could give recipients an unfair advantage over their competitors or be an inefficient use of the DAO's funds if they do not bring about a net positive change.

The means test will include a scoring system ranging from 1 to 5, reflecting the merit of each application.

- Rating 1: Unsatisfactory
- Rating 2: Below expectations
- Rating 3: Meets expectations
- Rating 4: Above expectations

- Rating 5: Exceptional

Each of the sub-criteria in the means test have varying levels of importance, and they will each have a weighting attached. A weighting of 1 indicates low importance, 2 indicates neutral importance, and 3 indicates high importance.

Each application will be scored by ADPC members, followed by a collective decision on the most deserving grant recipients, taking into account the rating against the eligibility criteria, a value-for-money evaluation and the funds available. The ADPC may make other decisions in relation to the operation of the fund and selection of applicants as further detailed in the Application Process Terms.

After the applications have been reviewed and decisions taken as to the grant beneficiaries, the average score assigned to each project will be shared publicly, ensuring that transparency is maintained throughout the process. In the event that an applicant receives a high score but is not chosen as a grant recipient, explanatory feedback will be provided either on an individual or collective basis to the cohort.

Evaluation Criteria

Criteria

Sub-Criteria

Description

Weight

Arbitrum Ecosystem Contribution

How aligned is the project with the Arbitrum ecosystem and how easy will it be to track the applicant's use of the subsidy funds?

Ecosystem Contribution

How does the applicant's project contribute towards the growth of the Arbitrum ecosystem?

3

Transparency Practices

To what extent does the applicant demonstrate transparency in its operations?

2

Community Engagement

How does the applicant engage with the DAO community and solicit feedback/input on its project, incorporating this into its decision-making?

1

Accountability Measures

What mechanisms does the project have in place to ensure accountability and responsible stewardship of subsidy funds, including governance structures in place?

3

Business Model & Need for the Subsidy

How effectively does the applicant's business model align with their need for the subsidy?

Clarity of Business Model

How well-defined and understandable is the applicant's business model?

2

Team Experience

What is the track record of the team on their ability to execute their plan?

2

Funding Gap Rationale

Is there a clear explanation of the funding gap the applicant is facing, along with the rationale for why additional subsidy funding is necessary to achieve its objectives?

3

Reasonableness of Subsidy Amount Requested

Does the requested subsidy amount make sense within the context of the project's needs and potential impact?

3

Scalability Potential

What is the scalability potential of the applicant's business model following the support of the subsidy?

1

Financial Analysis

How realistic and stress tested is the applicant's financial status and projections and is their plan for the use of the subsidy funds clearly outlined?

Accuracy of Projections

How realistic and well-supported are the financial projections provided by the applicant, inclusive of revenue forecasts and cost analysis?

1

Sensitivity to Scenarios

To what extent does the applicant's financial analysis consider different scenarios, such as base, target and stress scenarios to assess the projects' resilience and adaptability to changing market conditions?

1

KPIs

Are there clearly defined KPIs that will be used to track the project's performance and measure progress towards achieving its goals?

3

Preferred Funding Distribution

Does the applicant have a preferred distribution plan for the subsidy funds, and is there a rationale provided for this distribution approach, such as front-loading funds for critical start-up costs or phased funding based on project milestones?

2

Risk Analysis

Is the applicant aware of risks with their project and what is their plan for mitigating these risks?

Risk Identification

How effectively does the applicant identify and assess potential risks and vulnerabilities that the project may have?

2

Security Requirements

Does the applicant have a clear understanding of its security requirements and the measures needed to protect against security breaches, such as through the conducting of a security audit?

3

Mitigation Strategies

What strategies does the applicant have in place or intend to implement to safeguard against the aforementioned risks?

2

Regarding the 'Ecosystem Contribution' metric above, we have conducted an initial assessment of the types of projects that

are currently building in the Arbitrum ecosystem and identified a few verticals that the ecosystem would benefit from funding. These are set out below, along with the rationales for choosing them. We will provide more weight to these areas and welcome input from the community on our selection.

RWAs & Tokenization

- Commands a small proportion of Arbitrum attention and building however is a focus of big institutions & banks deploying large amounts of capital into tokenization.
- Arbitrum as the home of DeFi is currently trailing in this burgeoning key category (e.g. [Mantle](#) passed a \$60 million support program for tokenized RWAs on their chain and Polygon and Avalanche have been very active in the space).
- Tokenized treasuries and private credit have [passed \\$1.3 billion in terms of value tokenized](#) and are only projected to grow in importance in the near future, highlighted by the recent launch of [BlackRock's](#) tokenized fund.
- Forum discussions talking about RWA's being used as a tool for diversifying the Arbitrum DAO treasury. See [here](#).

Gaming

- Becoming an increasingly relevant Web3 vertical with major games finally launching this year, and will catch some more tailwinds (eg. Shrapnel, Star Atlas, etc.).
- Arbitrum significantly lags behind other major ecosystems (especially Polygon) both in terms of games and in terms of support & incentives for development on their network
- Discussion on ramping up incentives and acknowledging Arbitrum's position in gaming. See [here](#).
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- Attracting gamers in the right demographic (18-34 tech savvy) to support onboarding to Arbitrum's broader DeFi and blockchain ecosystem.
- Aligns with the 'Catalyze Gaming Ecosystem Growth on Arbitrum' proposal [here](#).

Collab Tech

- Definition: Tooling for governance, operations, community, and contributors.
- Arbitrum governance is currently sprawling, exacerbated by the introduction of Orbit, which will result in an ecosystem of decentralized governance organisations making collaboration even more challenging.
- Focusing on and incentivizing new Collab Tech represents an opportunity to clean up governance practices for Arbitrum DAO and beyond.
- This sector is underfunded since it is less understood by VCs, thus, focus and resources will have to come from within.
- The majority of Arbitrum's sequencer fees come from this category (e.g., Quest Protocol).
- Discussion on spinning up a Collab Tech business cluster. See [here](#).

You can find more detailed information on the rubrics informing the Means Test [here](#).

(B) Application Process

Application & Review Windows

The Subsidy Fund will run in 4 cohorts of 8 weeks each. Each cohort will consist of an initial submission period of 2 weeks, followed by a 6-week review period. Moreover, a maximum cap of 25% of the total Subsidy Fund amount can be disbursed per cohort to ensure that the fund is structured to allow the door to be opened to new entrants over time. Each cohort will operate on a first-come-first-served basis for application reviews, and if the maximum capital has been allocated for the cohort, the remaining applicants will be rolled over to the next cohort.

Initial Screening

To efficiently handle the anticipated surge in applications and to ensure that the highest quality and most relevant applicants are selected, the below 5 sub-criteria (with the highest weights as mentioned above in the Means Test) will first be applied to all applicants, with the top-scoring applicants moving forward in the evaluation process and being assessed in greater depth:

1. Funding Gap Rationale
2. Reasonableness of Subsidy Amount Requested

3. KPIs
4. Ecosystem Contribution
5. Accountability Measures

The ADPC reserves the right to introduce Mandatory Requirements over time that operate as threshold tests and will publish those requirements if introduced.

In-Depth Review & Feedback

Projects that pass the initial screening will undergo a review due diligence (DD) by the ADPC, including interviews and constructive feedback (either individually or on a collective basis).

Award & Monitoring

Once approved, projects receive subsidies, with periodic check-ins and a concluding evaluation to measure impact and success.

(C) Selection Process & Reporting

Transparency and continuous dialogue form the backbone of our selection and reporting process, ensuring that each funded project remains aligned with program expectations.

Bi-Monthly Reports

We will provide bi-monthly updates on our selections and updates on funded projects (i.e., in line with each Cohort). These updates will include general project trajectory and progress toward milestones. To create the reports we will set regular monthly check-in dates where projects fill a template/slide in order to give the key info about the project's status, such as:

- Summary of Achievements for the Month
- Funds Utilized
- Milestones Reached
- Challenges Faced & Plan of Action
- Feedback Integration, i.e., how projects have incorporated feedback provided.
- Next Steps & Priorities

Output Metrics

With the initial priorities in mind, some effective measures for meaningful output will look as follows:

- Number of Projects Funded:

Number of projects funded during each cohort.

- Total Funds Allocated:

Cumulative sum of funds distributed in each cohort, showcasing the program's financial impact.

- Percentage of projects funded in target verticals:

As outlined in the Means Test, the three key verticals we have identified are RWAs & Tokenization, Gaming, and Collab Tech.

Outcome Metrics

Depending on the final portfolio of funded projects, we will gauge the success rate of awarded projects through specific outcome metrics. While these metrics can be influenced by a wide range of external factors, such as market conditions and individual decisions on a project level, we are committed to supporting and funding the most promising projects to the best of our ability. Metrics include:

- Percentage of funded projects successfully deployed on Arbitrum
- Percentage of KPIs outlined in the application achieved by funded projects
- Percentage of projects successfully deployed as Orbit chains: One of the key aims of the Arbitrum DAO is to build and expand the Orbit ecosystem. Funding projects that grow the Orbit ecosystem is a net positive to the DAO.

(D) Project Allocation

Our approach to subsidy fund allocation focuses on achieving high impact while ensuring that a de minimus number of projects obtain funding.

To ensure that the subsidy is spread across a large number of projects rather than concentrated in several larger projects, the maximum subsidy to be granted will comprise 5% of the subsidy fund available. Therefore, given that the subsidy fund comprises \$10 million, the maximum subsidy that a project can receive will comprise no more than \$500K worth of ARB. This will ensure that the fund is designed to subsidize at least 20 projects, at a minimum.

(E) Team Setup

The administration and selection process of these subsidies will be managed by the ADPC. Even though the ultimate decision will lie with the judgment of the ADPC, their assessment will be strongly guided by a means test that evaluates key metrics to determine deserving projects.

The activation of the ADPC to manage the Subsidy Fund will hinge on extending the current 6-month mandate once the Subsidy Fund becomes operational. Should the DAO or the ADPC opt against a continuation of the ADPC, a Subsidy Fund Management Committee will need to be elected. The ADPC will allocate ample time for this process to ensure the Subsidy Fund operation is not reliant on the ADPC's mandate extension.

(G) Governance

The Subsidy Fund governance aims for transparency, efficiency, and broad community involvement. It outlines mechanisms to ensure fair and balanced decision-making for all stakeholders.

Multi-Sig

All providers must undergo and successfully complete the standard Know-Your-Business (hereinafter referred to as the 'KYB') verification processes with the Arbitrum Foundation prior to receiving the service-subsidy.

Subsequently, the designated Multi-sig members, established at the inception of the ADPC and voted in favour of by the ArbitrumDAO, will take charge of disbursing funds to the selected beneficiaries, whereby the transactions will be streamed using Hedgey.

In recognition of the additional responsibilities undertaken, each of the five multi-sig wallets is proposed to receive a supplementary compensation ranging from 500 ARB - 1,000 ARB monthly.

It is also important to note, as per the ratified proposal which led to the formation of the ADPC, that the multi-sig committee grants the ArbitrumDAO the authority to claw back funds from the ADPC's multi-sig wallet using the [Zodiac Governor Module](#), if necessary.

Checks & Balances

Kindly note that the subsidy fund will be subject to the same checks and balances found within the [procurement committee proposal](#), regulated by an agreement entered into by all elected ADPC Members, with the Arbitrum Foundation serving as a counterparty to the agreement. These checks and balances include:

Conflict of Interest Provision:

ADPC Members will be bound to act in absolute good faith, utmost honesty, refraining from deriving unauthorized profits from their position & disclose conflicts of interest. ADPC members should always disclose any potential or actual conflicts of interests to other ADPC members who will then proceed to mitigate the respective ADPC Members' involvement in the task in relation to which such ADPC Member is conflicted.

To sum up, all ADPC Members must declare the nature and extent of any interest, direct or indirect, which the ADPC Member is aware that she, he or it has in a proposed task at hand.

Record-keeping and Reporting:

Comprehensive and precise record-keeping is imperative. ADPC Members will be required to maintain detailed accounts and documentation of the ADPC's internal operational workflow together with meeting minutes. Furthermore, periodic reporting is essential so as to keep the ArbitrumDAO updated re. Task-specific progress & internal ADPC Administration.

Duty of Impartiality:

ADPC Members will have an obligation to act in an impartial manner in relation to their tasks & workflow, ensuring that the ADPC is not compromised by personal interests or external influences.

Obligation of Recusal:

ADPC Members with a conflict of interest involving a project and/or service provider being reviewed by the ADPC should recuse themselves from participating in the evaluation, facilitation & administration of the applicable procurement process.

Prohibition of Self-Dealing:

Participants should refrain from voting on sending funds to themselves or organizations where any portion of those funds is expected to flow to them, their other projects, or anyone they have a close personal or economic relationship with.

Ethical Trading:

Members are required to follow ethical trading standards concerning ARB and any other relevant digital assets.

Grant Application Terms and Conditions can be found

[here](#).

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