

Title: [TEMP CHECK] AAVEnomics update

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Simple Summary

This proposal seeks governance feedback and consensus on leveraging the Safety Module Umbrella update to create a clear path and roadmap related to the protocol “fee switch”, defined as updated “AAVENomics”.

Motivation

Before we start

This proposal leverages the [BGD. Aave Safety Module - Umbrella](#) proposal, it is strongly advised to read it before diving into the current proposal.

The current proposal has been peer-reviewed by Aave service providers and active Aave DAO community representatives & delegates.

Introduction

The Aave protocol is the clear market leader in the liquidity vertical and is focused on expanding in both the stablecoin and bridging verticals. The protocol's TVL and net profit growth have largely outpaced market conditions thanks to the coordinated efforts of service providers appointed by DAO governance.

The Aave protocol is also the clear leader on every network Aave has deployed to, and when given a choice, DeFi users leverage Aave over alternatives.

This has allowed the Aave DAO not only to “cover its own bills” but also has built [a large treasury of ETH and stablecoins](#).

Additionally, during the past couple of quarters, the DAO explored revenue sharing with the Merit program, which is essentially a redistribution of the protocol's net stablecoin excess revenue to the GHO minters and stakers to support aligned behaviors and the growth of GHO. Alongside Merit, the Ahab program, which is funded by protocol net ETH & ETH-correlated assets, is mobilized to attract strategic liquidity in Aave markets, supporting protocol growth in the main & new markets.

With the ACI, we consider the DAO now ready to explore a further step in the protocol's maturity and would like to submit for governance consideration a clear path for protocol net excess revenue redistribution to the key actors of the Aave ecosystem, creating new positive dynamics and novel synergies within the industry.

This journey is designed in several incremental steps. This proposal seeks feedback on the journey as a whole as a “TEMP CHECK” and approval to begin the first step via a potential “ARFC”.

To ensure the DAO's long-term sustainability, new steps will be escalated when the protocol reaches specific growth and net excess revenue milestones.

Umbrella: A Proposed Safety Module Paradigm Shift

The Safety Module is a crucial line of defense for the Aave protocol. In case of a shortfall event, and if liquidators do not complete their tasks, the Safety Module is designed to assume the excess debt on behalf of users to avoid or at least mitigate bad debt events.

Fortunately, the Safety Module has never been needed for the Aave protocol. The few excess debt events in Aave protocol history have been addressed by governance through the mobilization of “cash” DAO treasury funds.

However, the current model is inefficient as it relies on secondary liquidity to liquidate Safety Module assets to obtain excess debt assets and clear debt.

With both GHO and StkAAVE, the primary issue with the Safety Module is that the current \$424M hosted in the Safety Module cannot effectively clear \$424M of excess debt. This is because:

1. The value of AAVE would be negatively impacted due to slippage.
2. The GHO peg is unlikely to withstand the mobilization of almost two-thirds of its current supply.

While it is highly improbable to encounter an excess debt event of this magnitude (precedent was less than 1% of this amount), the entire model has room for optimization.

Therefore, Umbrella proposes:

1. Segregation of coverage
2. Elimination of reliance on secondary liquidity

From now on, the Safety Module activation should focus on slippage-free debt burn coverage.

Umbrella allows the deployment of aTokens Safety Modules that are more cost efficient and provides better protection to Aave users; This proposal seeks approval on a multi-step journey toward Umbrella Activation and redefines the Role & benefits of the AAVE assets & tokenomics in the Aave ecosystem.

Umbrella Coverage Adoption Journey

As an initial and immediate step:

We propose segregating StkGHO and StkAAVE Safety Module coverages to distinguish protections and improve StkGHO Safety Module efficiency, which would protect the GHO stablecoin.

With this upgrade, the StkGHO Safety Module is meant to only protect users from GHO debt and is mobilized to clear GHO excess debt only.

GHO is a young stablecoin with limited secondary liquidity. In the current stage of GHO maturity, mobilizing GHO to protect other assets' debt will mean the death of the GHO peg and trust in GHO for limited resources gained.

However, in the context of GHO debt protection only, StkGHO is a perfect tool. In case of a shortfall event, GHO can be seized in the Safety Module and used to clear excess debt by burning GHO. This action is absolutely slippage-free and will not impact the GHO peg.

Safety Module users will suffer a below 1 StkGHO <> GHO exchange rate, but it's a risk they willingly accepted by staking.

Example: If there's 100M GHO in the Safety Module and the protocol suffers a \$3M excess debt GHO shortfall event, via an AIP, 3M GHO will be seized from the Safety Module to clear the debt. As a result, the StkGHO/GHO exchange rate will drop to 0.97, leading to a socialized net haircut of 3% for all Safety Module stakers (around 6 weeks of the current reward rate).

This paradigm shift will make GHO the safest and most trustworthy stablecoin in the ecosystem with currently both an average overcollateralization ratio of 2.5 and ~65% of the supply that can be mobilized to clear any form of excess debt without impacting the GHO peg.

This will de facto make Ethereum StkGHO the first Safety Module adopting the Umbrella standard.

These changes come at the cost of temporarily reduced overall V3 protection, but as discussed earlier, GHO is not mature enough to be a suitable asset to protect other debts than GHO at this moment. The reduced protection will be covered by the introduction of new Safety Modules in further steps.

We propose adopting the following:

Umbrella coverage adoption Journey doctrine:

1. The Legacy Safety Module coverage is set to all live networks Aave V3 debt until replaced.
2. The Legacy StkGHO SM protects GHO debt exclusively. This safety module becomes the prime candidate for becoming the first Umbrella safety module instance via upgrade.
3. The Umbrella Ethereum Safety Modules will not automatically cover Aave V3 deployments; coverage must be opt-in by governance vote.
4. Mid-term: segregate risk further by deploying network-specific Umbrella Safety Modules financed by protocol "local" net excess revenue.

StkGHO Migration and upgrade Journey

GHO is growing and is meant to be a profitable product of the Aave protocol. At ~150/175M GHO, GHO is expected to be net profitable for the protocol, with revenue outpacing system subsidies.

Currently, GHO has a dual reward system with rewards in AAVE sourced from the ecosystem reserve and Merit airdrops sourced from protocol net profits.

We propose, in resonance with previous governance decisions, to slowly cut rewards of the StkGHO safety module in favor of a potential Umbrella StkGHO safety module.

The Merit programs yielded great results in terms of growth, peg preservation, and user behavior optimization. We propose to maintain the Merit program in its current form.

This will keep a dual reward system for StkGHO: a “base yield” paid continuously in GHO to stakers and an “Airdrop” yield via Merit that can be optimized to reward more users with net positive behavior for the protocol, maintaining “boosts” of most wanted behavior but ensuring a sustainable “base yield” for this part of the Safety Module. Both of these rewards are financed by Aave protocol net revenue.

In practical terms, The Legacy GHO safety module has whitelisted AAVE emissions until Oct 2024 and benefit from Merit, we propose to slowly incentivize user migration to the Umbrella stkGHO by letting the AAVE distribution slowly expire and changing the Merit reward focus on Umbrella on the next Merit round post-publication.

This will slightly increase cost and efficiency by having a few weeks off incentives on both StkGHO safety module but gains on users experience allowing them to migrate at their own pace justifies it.

A new role for Aave beyond the Legacy Safety module, AAVENomics update.

AAVE is the center of gravity of the Aave protocol. It is the governance asset of the DAO, allowing true control and ownership of the Aave protocol to a degree not achieved in any other protocol in our industry. But as a Safety Module asset, it's simply not efficient enough. AAVE is not a debt token in the Aave protocol and is not as liquid as ETH and major stablecoins.

End the “Seize and Sell” Doctrine

The “seize and sell” doctrine is dangerous as it's inefficient due to slippage, creates the need to subsidize strong secondary liquidity (StkBPT Safety Module), and causes great price pressure on the asset in case of mobilizing the Safety Module. This reduces the cost of acquiring a large amount of AAVE and taking effective control and ownership of the protocol. With historically 15-30% of the Aave supply in the Safety Module and considering the average governance participation, this risk must be seriously considered.

Additionally, the relatively low maximum slashing of 30% of the AAVE Safety Module means the protocol is allocating funds that are mostly not even mobilizable to protect the protocol.

Lastly, the AAVE Safety Module is not sustainable as it is subsidized by the ecosystem reserve that will eventually run out of funds.

We propose the AAVE Safety Module to not be included in the Umbrella update, StkAAVE will evolve into a staking role acting as a liquidity sink and a way to collect rewards generated from the protocol revenue and other protocol benefits.

StkBPT Redefinition

The Aave DAO has spent large amounts of resources incentivizing AAVE's secondary liquidity to maintain the current Safety Module paradigm.

While the secondary liquidity of AAVE is important, it should not be a focus of the Safety Module.

The DAO earned experience with secondary liquidity management with the Aave Liquidity Committee (ALC) program, yielding great results on GHO peg and growth.

We propose not including StkBPT from the Umbrella Safety Modules and appoint the ALC to manage AAVE secondary liquidity. We also propose the introduction of a “Buy & Distribute” program funded by the protocol's excess revenue, With a budget defined by Aave Finance service providers and management by the ALC.

The ALC and Aave Finance service providers will continue their journey of decentralization and automatization of these processes, contributing to a future with the human element as removed as possible from these actions.

This will increase the Safety Module's budget efficiency, make the subsidy of secondary liquidity sustainable, and allow more granular liquidity management. It is expected to optimize the funds needed to maintain the expected outcome.

In this new system, Liquidity will still be incentivized, but we expect a large optimization in the cost and management of this secondary liquidity.

Introduction of Anti-GHO

Creating a GHO borrow rate discount was a good idea to align AAVE holders and GHO minters, but the discount mechanism is not efficient in terms of protocol accounting and can be optimized.

We propose, based on discussions with several service providers, particularly Bgd Labs, the removal of the GHO borrow rate discount and the introduction of a new “anti-GHO” token generated by StkAAVE holders minting GHO.

The users linearly accumulate anti-GHO, which is claimable at the user’s will. Anti-GHO generation is proportionate to the interest accumulated by all GHO borrowers.

Anti-GHO is a non-transferable ERC-20 linked to a couple of special-purpose GHO facilitators that can be used in two ways:

1. Burn Anti-gho to mint GHO used to repay their own GHO debt “for free.”
2. Mint GHO to be deposited on the user’s behalf in the GHO Safety Module and distribute StkGHO to the user.

Both special-purpose facilitators’ “debt” will be regularly “cleared” by mobilizing GHO from the Aave Collector via Aave treasury regular AIPs to repay, ensuring no long-term unbacked GHO in the protocol.

This new system is more efficient, increases the alignment of AAVE stakers with GHO borrowers, and officially introduces revenue sharing of part of the Aave protocol revenue to some AAVE stakers, acting as the initial step of a more ambitious excess revenue-sharing strategy.

Closing the LEND chapter

Nearly 4 Years ago, After the launch of Aave V1, the Aave protocol proposed the initial AAVeconomics migrating the legacy asset LEND into the current AAVE token.

After a significant amount of time passed and witnessing the lack of activity of the legacy asset, we take this proposal as an opportunity to close the LEND chapter.

We consider that 4 years and the amount of time that will pass for these proposals, publications, approvals, implementations, and execution to offer ample and fair notice to legacy users to migrate to AAVE, we propose to deactivate the legacy migrator contract and transfer the remaining balance to the Ecosystem reserve to be mobilized for Aave Stakers and protocol growth.

Activate Umbrella Atokens Safety Module, initiate “Buy and Distribute” AAVeconomics

The Aave protocol is seen as the industry standard in terms of resilience and safety, making Safety Modules of Aave a popular option for protecting protocol users despite the risks.

Additionally, ~80% of the Aave protocol users deposit in the protocol but do not have Aave debt. Their use case of the protocol is to seek yield on liquidity provided. These users consider the Aave protocol safe enough to keep their assets inside the protocol contracts for the long term.

The paradigm shift to “seize and burn” instead of the current “seize and sell” increases the Safety Module efficiency significantly. The natural progression of this strategy is to mobilize users who consider the Aave protocol safe enough to hold their assets and do not seek to create debt to consider renouncing their Safety Module protection, their borrowing power and short-term aToken liquidity (cooldown period) in exchange for extra yield.

This is done by adding a AToken category to the Umbrella Safety Module. In case of a shortfall event, these tokens are seized and used to burn debt, just as the StkGHO Umbrella Safety Module will function.

Most of the Aave protocol debt is in wETH and stablecoins.

Therefore, we are gathering feedback on the initiation of Umbrella AToken Safety Modules with awETH and aUSDC.

This allows for covering most of the debt in the protocol if these assets need to be mobilized.

Because debt can be repaid in aTokens in Aave V3, the available secondary liquidity of these aTokens is not relevant in excess debt clearing.

To cover debt labeled in other assets, USDC and ETH are the most liquid assets in the ecosystem, making slippage considerations a low issue, especially with a focused scope of Safety Module coverage introduced earlier.

aTokens Safety Modules are proposed to be primarily rewarded in their respective aTokens, financed by their respective Reserve Factor collection on their assets and correlated assets.

Umbrella multi-reward support allows for more mid-term synergies for “Re-Staking”, which will be explored further in this TEMP CHECK.

Details and budgets of these Umbrella Atokens Safety modules should be discussed at the ARFC stage with feedback from both Risk & Finance teams.

We're confident this will allow a factually superior coverage of the Aave V3 protocol at a fraction of the current costs.

Activate a “Buy & Distribute” Program

With the new efficient Umbrella safety modules, it is expected that the protocol revenue surplus will increase. With sustainability reached milestones, this net excess revenue should be mobilized and redirected to token stakers currently funded via the ecosystem rewards contract.

In terms of rewards, the ecosystem rewards will eventually run out of funds. That being said, we propose that StkAAVE remains compensated in AAVE tokens as stakers are already aligned with the asset. To achieve this, a “Buy & Distribute” program is introduced to acquire AAVE assets on secondary markets from protocol revenue and distribute them to the ecosystem reserve. This upgrades the current AAVE safety module in a new “Staking Module”, not part of Umbrella.

There's little to no difference in user experience from the current situation, but in terms of protocol sustainability, it's a paradigm shift. This new system also introduces a constant demand side for the AAVE asset on secondary markets.

It is proposed that this program be funded with the net excess revenue of the protocol.

Rewards rates will be defined according to protocol net excess revenue and will reflect the actual financial results of the protocols, with periods of higher rewards to potential periods with zero yield.

We propose that the Aave Finance service providers manage the “Buy & Distribute” program via treasury AIPs to increase efficiency in the short term. We believe this process also needs to be part of the Journey of decentralization, and we expect the Aave Finance service providers to contribute to a future with the human element as removed as possible from this program

For an easier understanding of the new AAVEnomics vision, please consider the following visual representation:

“Re-Staking” Umbrella Beyond Aave

Aave's Safety track record speaks for itself; while Aave had several excess debt events, the DAO never had to mobilize the legacy Safety module. With the Umbrella upgrade, we expect the efficient coverage to increase significantly compared to the current situation, from a theoretical \$100m to likely billions of mid-terms.

The Aave DAO can mobilize and monetize this coverage beyond the Aave protocol. The Aave DAO service providers are risk experts who can give valuable coverage recommendations to the Aave governance.

The Umbrella multi-token incentives controller allows for rewards in several tokens, and we believe this cost-efficient coverage of already existing significant liquidity will be of high interest for third-party protocols and networks, as shown by the high interest of the “Restaking” DeFi vertical.

While the journey to maturity on this vertical is still long, the ACI wanted to share this mid-term vision to the community of a potential new journey for protocol revenue and Umbrella Stakers Yield.

Specification

Milestones and Trigger Conditions

While the Aave protocol's net excess revenues are at an all-time high, it would be reckless to implement significant new budget spending without considering the protocol's long-term sustainability.

From a user experience perspective, a too-ambitious distribution schedule being forced to halt due to more adverse revenue collection conditions will lead to massive and unwanted frustration.

The Aave DAO has always been a conservative actor and has always prioritized long-term sustainability over short-term yield.

We suggest considering the following elements as key data points to execute changes in Safety Modules in steps:

- Aave Collector net holdings
- Service providers' recurring budget
- Merit and ALC program recurring budgets
- GHO supply
- GHO 30-day average revenue
- Protocol 30-day average revenue

The ACI Proposes this vision to be implemented in 3 different ARFCs to be sequentially proposed alongside reaching set milestones, we welcome governance feedback on this implementation Journey.

Initial ARFC Doctrine Adoption and Deployment of First Umbrella Safety Module: StkGHO

Adoption of the Following Doctrine:

1. The Current StkAAVE and StkBPT Safety modules becomes the “Legacy Safety Module”
2. The Legacy Safety Module is set to cover all live networks Aave V3 debt with a market size exceeding \$100M and older than one year until replaced.
3. The StkGHO Safety modules protect GHO debt.
4. The Safety Modules do not automatically cover Aave V3 deployments; coverage must be opt-in by governance vote.
5. Pre-authorization of introducing “network-specific” Umbrella Safety Module instances financed by “local” revenue.
6. An Umbrella StkGHO Safety Module is deployed and becomes the first Umbrella Safety module with a reward set exclusively in GHO and financed by Aave protocol excess revenue. The feedback of Aave Finance & Risk service providers is expected to define a Safety Target for this Umbrella Safety Module.
7. The legacy StkGHO safety module cooldown is set to zero; AAVE rewards will not be renewed at distribution expiry.
8. The Merit Program continues as it exists today It will reward the Umbrella StkGHO in the following round its deployment to incentivize user migration

This doctrine would be adopted at the ARFC snapshot Stage.

Trigger milestone:

- Already Achieved

Execution:

- BGD Labs give the greenlight for the Umbrella upgrade, initiate the StkGHO Legacy to Umbrella Migration via AIP.

Important note:

As the Umbrella design is still being discussed, details of implementation are subject to change and should be discussed at the ARFC stage of this proposal.

Part II: Initial ARFC Doctrine Adoption and Deployment of First Umbrella Safety Module: StkGHO

Adoption of the Following Doctrine:

1. The Current StkAAVE and StkBPT Safety modules becomes the “Legacy Safety Module”
2. The Legacy Safety Module is set to cover all live networks Aave V3 debt with a market size exceeding \$100M and older than one year until replaced.
3. The StkGHO Safety modules protect GHO debt.
4. The Safety Modules do not automatically cover Aave V3 deployments; coverage must be opt-in by governance vote.
5. Pre-authorization of introducing “network-specific” Umbrella Safety Module instances financed by “local” revenue.
6. An Umbrella StkGHO Safety Module is deployed and becomes the first Umbrella Safety module with a reward set exclusively in GHO and financed by Aave protocol excess revenue. The feedback of Aave Finance & Risk service providers is expected to define a Safety Target for this Umbrella Safety Module.
7. The legacy StkGHO safety module cooldown is set to zero; AAVE rewards will not be renewed at distribution expiry.
8. The Merit Program continues as it exists today It will reward the Umbrella StkGHO in the following round its deployment to incentivize user migration

This doctrine would be adopted at the ARFC snapshot Stage.

Trigger milestone:

- Already Achieved

Execution:

- BGD Labs give the greenlight for the Umbrella upgrade, initiate the StkGHO Legacy to Umbrella Migration via AIP.

Important note:

As the Umbrella design is still being discussed, details of implementation are subject to change and should be discussed at the ARFC stage of this proposal.

A new role for Aave beyond the Legacy Safety module, AAVEnomics update.

The next proposed step is the end of the StkAAVE GHO discount, introduce the anti-GHO system, and close the LEND chapter .

Trigger milestones:

- 175M GHO supply
- Secondary liquidity allowing a 10M swap size at 1% price impact

Execution:

- Set borrow rate discount for Aave V3 GHO facilitator to 0%.
- Create new GHO facilitators linked to the GHO credit system.
- Terminate LEND migration contract.

Part III: “Fee Switch” Activate Umbrella Atokens Safety Module, initiate “Buy and Distribute” AAVENomics

Trigger Milestones:

- Aave Collector net holdings are at *2 yearly service providers’ recurring costs for the past 30 days.
- Aave protocol 90-day annualized revenue is at 150% of all protocol expenses YTD, including the AAVE acquisition budget and aWETH & aUSDC Umbrella budgets.
- Budget is defined, financed, and readjusted quarterly by Aave Finance service providers.

Execution:

- Financing of secondary liquidity for AAVE with Aave Finance AIPs managed by Aave Finance service providers.
- End of Legacy Safety Module:
- StkBPT cooldown is set to 0.
- End of StkBPT rewards. Replaced by liquidity incentives from ALC
- StkAAVE slashing is set to 0%. StkAAVE becomes the asset of the AAVE Staking module
- StkBPT cooldown is set to 0.
- End of StkBPT rewards. Replaced by liquidity incentives from ALC
- StkAAVE slashing is set to 0%. StkAAVE becomes the asset of the AAVE Staking module
- Creation of aUSDC and aWETH Umbrella Safety Modules with aUSDC and aWETH as reward tokens. (If validated by governance feedback)
- Financing of AAVE buy and distribute program by Aave Finance service providers; bought AAVE is distributed to the ecosystem reserve. The distribution pace of AAVE is adjusted to the quarterly budget to avoid running out of funds for stakers. This process is handled by the Aave Finance service providers until fully automated.

Important note:

As the Umbrella design is still being discussed, details of implementation are subject to change and should be discussed at the ARFC stage of this proposal. this TEMP CHECK is meant to query community sentiment and ARFC stage is meant to define actual implementation leveraging service providers and community feedback.

Acknowledgments

The ACI extends its sincere gratitude to all Aave service providers, delegates, and community members who contributed to this proposal's peer review. Your expertise and insights have been invaluable in refining and strengthening this TEMP CHECK. Special thanks to Bgd Labs for their crucial inputs on this proposal and the conception of the Umbrella Safety module. This proposal reflects the collaborative spirit and dedication of the Aave DAO.

Next Steps

1. Gather community feedback on this TEMP CHECK.
2. If consensus is achieved, move this proposal to the TEMP CHECK snapshot stage

Disclosure

The Aave Chan Initiative is independent and has not received any compensation from related parties for drafting this proposal.

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