Funded Protocol: A Decentralized Capital Infrastructure for Proprietary Trading

The Capital Layer for Proprietary Trading

Litepaper
Version 0.1
July 2026

ABSTRACT. Proprietary trading has become a multi-billion dollar industry, yet nearly all of its economic value remains captured by a small number of private companies and their shareholders.

While millions of traders pay evaluation fees every year, external capital has no efficient way to participate in the industry's cash flows. Growth remains constrained by the balance sheets of individual firms.

Funded Protocol introduces the capital layer for proprietary trading.

Liquidity providers supply capital through shared on-chain pools, while operators focus on acquiring and evaluating traders. The protocol manages capital allocation, risk controls and yield distribution.

The first application built on Funded Protocol is a prediction market prop firm, demonstrating the infrastructure before opening it to third-party operators.

1. INTRODUCTION

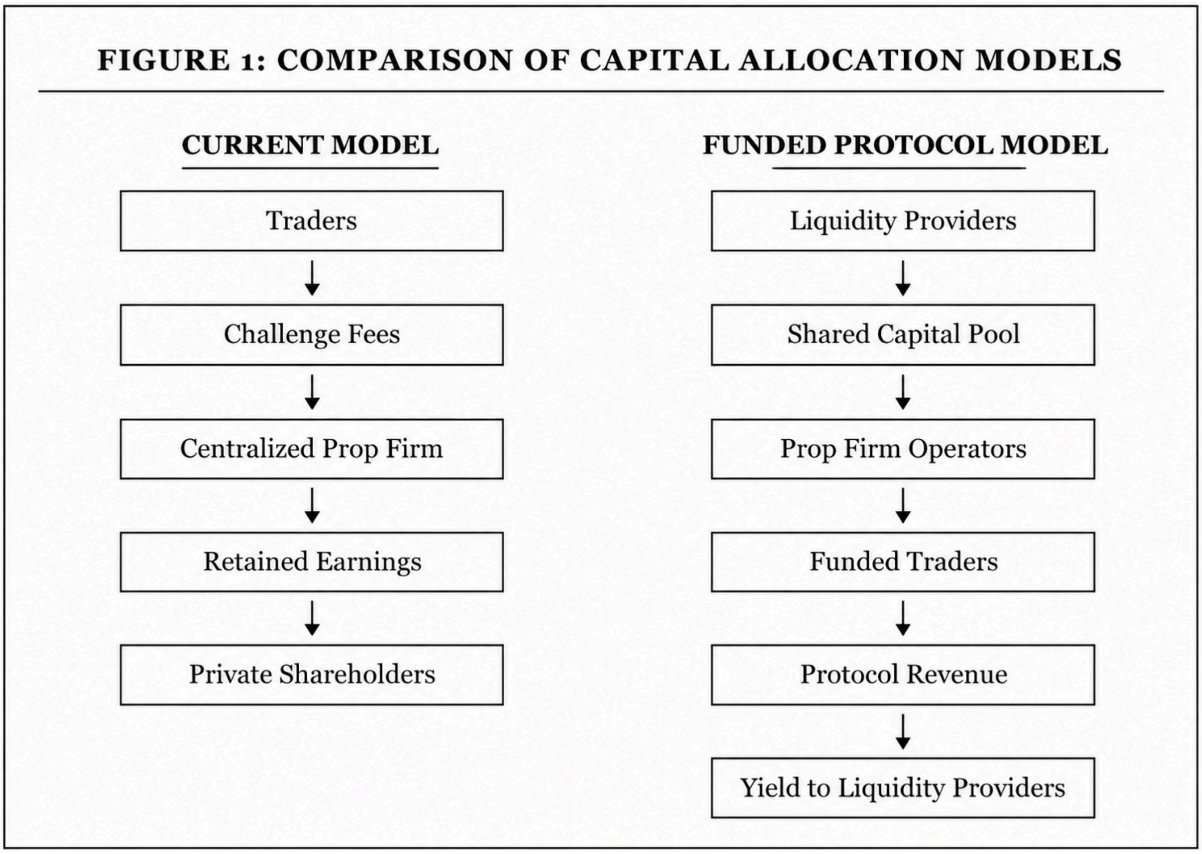
Three independent markets are reaching maturity at the same time.

First, proprietary trading firms have grown into a multi-billion dollar industry with strong demand from retail traders, yet participation in their economics remains limited to private shareholders.

Second, stablecoins have evolved into one of the largest sources of programmable capital. As on-chain yield products continue to attract billions of dollars, investors are increasingly seeking sustainable, real-world cash flows rather than purely inflationary token incentives.

Third, prediction markets are experiencing rapid adoption, creating transparent, liquid and programmable trading venues that are particularly well suited for automated execution and risk management.

Funded Protocol sits at the intersection of these trends, connecting on-chain capital with the economics of proprietary trading through a shared capital layer.



2. THE PROBLEM

Today's proprietary trading firms are vertically integrated businesses.

Each operator is responsible for raising capital, managing treasury operations, acquiring traders, designing evaluations, controlling risk and settling profits.

While this model has enabled the industry to scale rapidly, it creates a fundamental inefficiency: every new funded trader requires additional balance-sheet capital.

As a result, growth is determined not only by a firm's ability to identify profitable traders, but also by its ability to continuously finance larger capital reserves.

At the same time, the economic value generated by the industry, including challenge fees, treasury income and funded trader performance, remains confined within individual companies. External investors cannot directly participate in these cash flows, despite providing capital being the primary constraint to growth.

The industry therefore suffers from two structural limitations:

- Capital is fragmented across isolated company balance sheets.
- Economic value is captured almost exclusively by private shareholders.

Funded Protocol addresses both problems by separating capital ownership from prop firm operations.

3. Funded Protocol

Funded Protocol introduces a shared capital layer for proprietary trading.

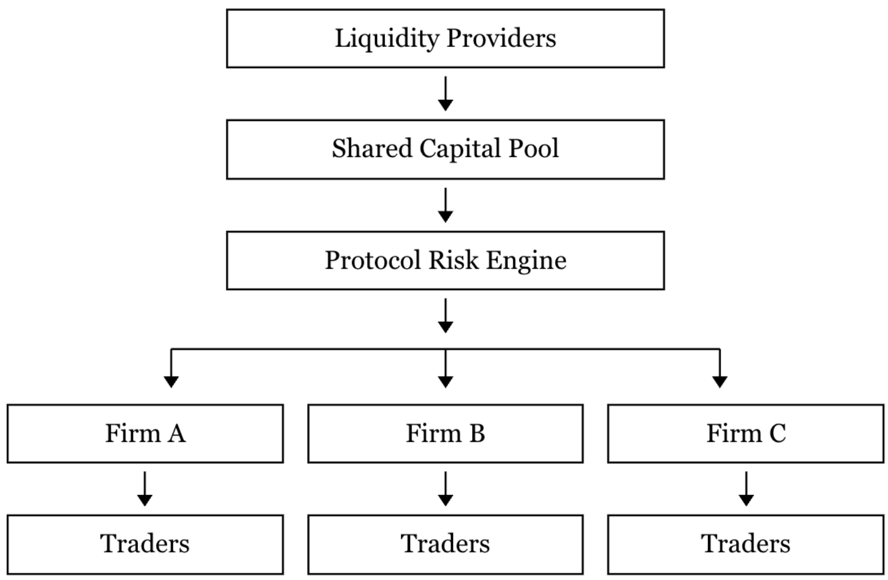
Liquidity providers deposit USDT or other approved stablecoins into a shared Capital Pool.

Prop firm operators configure and operate their own products on top of the protocol. Each operator may define challenge rules, evaluation criteria, challenge pricing, maximum drawdown, daily loss limits, funding sizes, profit splits and supported markets.

The underlying capital remains controlled by the protocol.

Once a trader passes an evaluation, the operator may request a funded allocation. The protocol accepts or rejects the allocation according to current liquidity, utilization and risk limits.

FIGURE 2: PROTOCOL ARCHITECTURE & POOL DISTRIBUTION



Capital becomes shared infrastructure rather than a private balance-sheet asset.

4. CAPITAL EFFICIENCY

Traditional prop firms reserve capital internally before funding traders.

However, the advertised account size is rarely equivalent to the protocol's maximum economic exposure. For example, a $100,000 funded account with a 10% maximum drawdown represents a maximum loss of $10,000 rather than $100,000.

Funded Protocol allocates liquidity based on actual risk exposure instead of nominal account size. The Risk Engine continuously evaluates available liquidity, protocol utilization, trader concentration, operator concentration and portfolio risk before approving new allocations.

This allows capital to be deployed more efficiently while maintaining predefined risk limits.

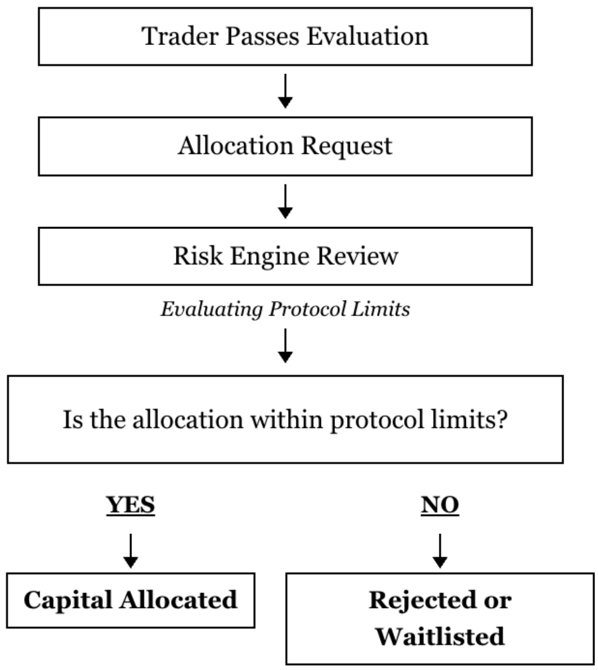
5. RISK ENGINE

The Risk Engine governs the amount of capital that may be allocated at any time. It continuously evaluates the state of the protocol and each proposed funded account.

Relevant parameters include maximum drawdown, daily loss limit, current trader profit and loss, aggregate open exposure, trader concentration, operator concentration, market concentration, strategy correlation, available liquidity, capital utilization, venue liquidity and historical operator performance.

The Risk Engine may reduce allocations, reject new funded accounts or place traders on a waiting list when protocol utilization becomes too high. No prop firm operator may independently exceed protocol-level limits.

FIGURE 3: RISK ENGINE ALLOCATION DECISION PROCESS



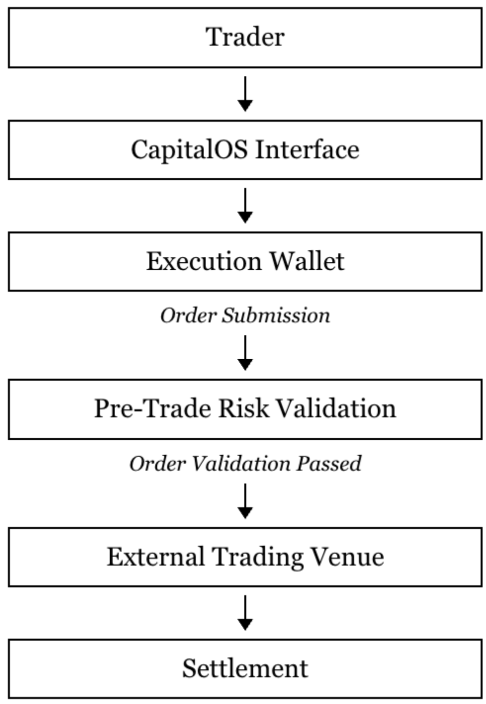
The initial version of the system may use transparent rule-based risk parameters. More advanced statistical models may be introduced only after sufficient operational data has been collected.

6. FUNDED TRADER EXECUTION

Funded traders receive trading permissions, not custody of protocol capital. Each funded trader is assigned a controlled execution environment or dedicated trading wallet.

The trader submits an order through the Funded Protocol interface. Before execution, the protocol verifies that the order complies with the trader's individual limits and with protocol-level risk constraints. If valid, the order is routed to an external venue such as Polymarket.

FIGURE 4: NON-CUSTODIAL ORDER EXECUTION PIPELINE



The trader cannot withdraw underlying funds, transfer protocol capital, or bypass drawdown rules. The protocol can suspend execution when limits are reached. This structure separates trading authority from ownership of capital while creating a transparent execution record for audits.

7. HOW VALUE FLOWS

Funded Protocol generates value for its stakeholders from three primary sources of economic activity.

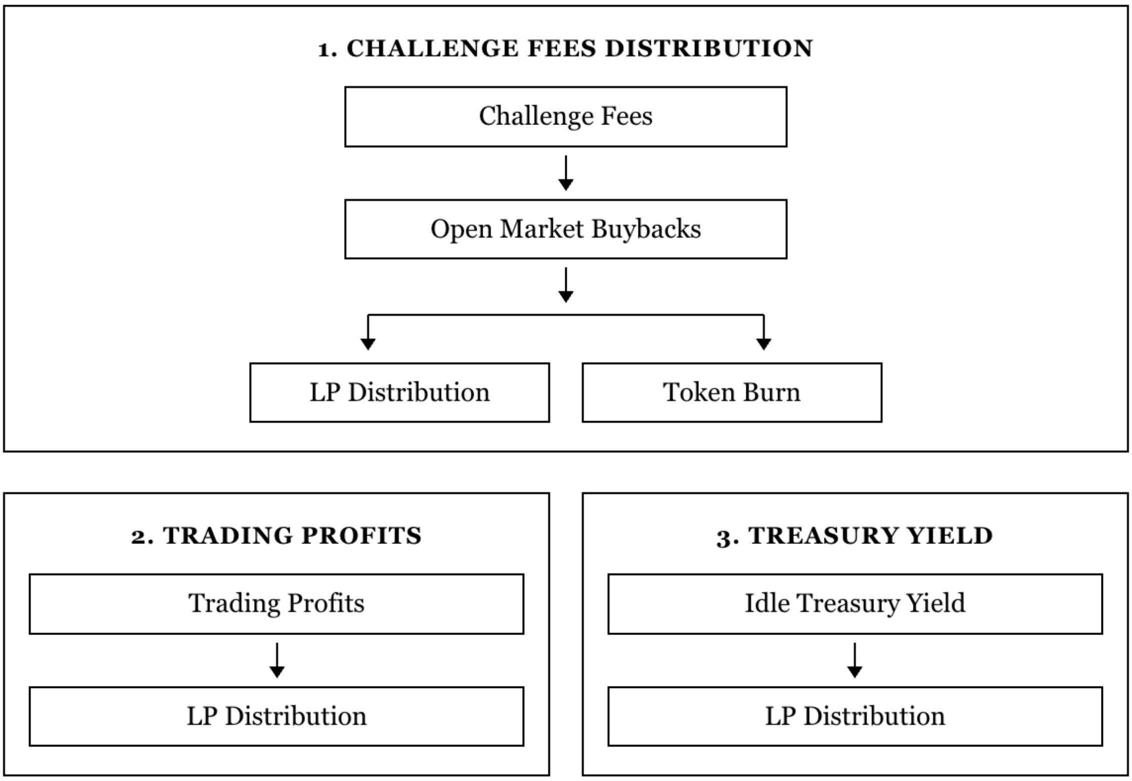
Challenge fees are generated whenever traders participate in evaluations. Rather than remaining entirely within the operating company, these fees are used to repurchase FUNDED tokens on the open market. Repurchased tokens are then split between liquidity provider rewards and permanent token burns.

Funded trading profits generated by the protocol are distributed directly to liquidity providers, rewarding the capital that enables funded accounts.

Finally, while capital remains unallocated, idle stablecoins may be deployed into approved low-risk yield strategies. The resulting treasury yield is also distributed to liquidity providers.

By separating these cash flows, Funded Protocol aligns every source of value with a specific protocol objective: token appreciation, liquidity incentives and long-term capital efficiency.

FIGURE 5: CAPITAL ALLOCATION & REVENUE DISTRIBUTION CHANNELS



8. FIRST APPLICATION

The first application built on Funded Protocol will be TheNews, a prediction market proprietary trading firm. Prediction markets provide transparent pricing, deterministic settlement and programmable execution, making them an ideal environment to validate Funded Protocol in production.

TheNews will serve as the protocol's proving ground, allowing Funded Protocol to validate its capital allocation engine, risk framework and execution infrastructure while generating real economic activity.

Once validated, the underlying infrastructure will progressively be opened to third-party operators, enabling anyone to launch a proprietary trading business on top of Funded Protocol without maintaining their own balance sheet.

PHASE I

Launch the first CapitalOS-powered prediction market prop firm.
Test challenge rules, controlled execution and settlement.
Collect trader and risk data.

PHASE II

Launch the first Capital Pool for approved participants.
Introduce automated allocation limits and transparent performance reporting.

PHASE III

Open the infrastructure to selected third-party prop firm operators.
Add operator-specific pools, limits and revenue-sharing structures.

PHASE IV

Support additional execution venues and trading markets.
Allow the creation of independent capital-backed trading businesses on shared infrastructure.