Carol Sanford - Charly Kleissner Interview

Carol: Hi Charly, welcome, would you please introduce yourself a bit to folks who are listening? Tell them a bit about how you describe the work you do in the world.

Charly: Hi Carol, I'm really pleased to be with you today and look forward to our conversation. I'm Charly Kleissner; you might detect a little accent in my voice. I'm Austrian and I immigrated to Silicon Valley in 1986. I have a PHD in Computer Science, and I have a really, really great career in Silicon Valley; as usually the CTO, the Chief Technology Officer, or the Senior Technology guy on the team in three successful startups. The first startup was a company called Next. Next was the company that Steve Jobs created after he was fired from Apple. I was in charge of the operating system [inaudible] was called Open Step. When Steve sold Next to Apple, he made this the main operating system of Apple; it's called System Ten now. Arguably, it's the products I ever [inaudible]. The second startup I participated in, was a company called Data Mine.

Data Mine was obviously in the data mining business. We sold that company for about four hundred million to Epiphany in the late nineties as well. The third company that I participated in as the CTO and Senior Vice President of Engineering was a company called Ariba. Ariba was a commerce company that was recently bought out by SAP just about nine months ago for about four and a half billion dollars. We bought this company to the market with an IPO in 1999 very, very successfully. That created enough wealth not only for our shareholders, but also for us. When I say us I mean, my wife Lisa and I. In the early two thousands, we suddenly have to ask. It was very clear to us that the only real meaning of wealth in capital is to make a positive contribution to humanity and the planet.

That was the beginning of what is now called impact investing since we challenged our advisors and the status quo about aligning the wealth that we had created in the markets in Silicon Valley and to align that with our values of reaching sustainability for us and the planet. Now we are considered impact investors and that's what we do.

Carol: That's great. There are many different ways of defining impact investing and differentiating it, from traditional investing. You gave just a hint there. Could you highlight two or three things that when you say impact investing, you know this is what you mean and how it moved from how you would have thought about investing before that?

Charly: Great, yes. Impact investing is actually an investment approach. Meaning it's an investment strategy across asset classes. It's not the separate asset class, what that means is that it can do impact investments in cash, in [inaudible] only, in common equity, in private equity, in long short and in real assets. In the year 2003, 2004 we actually articulated an impact investing strategy to go all in, to invest all of our investible assets towards positive social and or environmental impact. That brings up the definition of how we view that the public industry is using it really and that's impact investments not only need to provide a financial return but they also need to provide an explicit ecological and or social return and you have to measure that.

The core principal behind impact investing is the intentionality behind it, so impact investors intentionally make these investments. They don't consider these investments an intellectual exercise of making more money, or an opportunity impact; they see impact investments as an extension of who they really are. We for instance, Lisa and I, we want to make a positive contribution to the sustainability of the planet, therefore; we have to align our investments with sustainability. We cannot say that that's outside of what we care about.

Carol: Wonderful, you're talking about being all in, reminds me of a conversation I had with John Fullerton a couple of days ago. I was blessed enough to get the keynote. His capital institute event last year and we have become quite good colleagues since then. He was speaking about your idea of the one hundred percent club I think he called it. Is that right and what is that?

Charly: Yes that's right, so John Fullerton is also a good friend of mine and a fellow traveler on the way of changing the system. We believe just like he believes that we are at the beginning

of a major transformation where humanity will learn how to live within the caring constraints of the finite planet of finite resources. We like him believe that the financial system is one of the biggest leverage points to actually move in that direction and accomplish that transition. We believe that impact investing within the financial system is one of the major leverage points to do that. What we started out doing is creating, what we created is two big global networks, impact investors.

The first one is called Toniic and we can talk about that a little bit more if you wish, which is really a global network of active impact investors who syndicate their capital to deploy and invest in usually start up to early stage, early growth companies. The second network that we created is the 100% IMPACT Network, which is a global network of asset owners that intentionally committed one hundred percent of their investable assets to positive impact.

Carol: That's great. I would love to hear about the second group a little more, because I haven't heard about it and how it's working and how you reach out to people. Could you say just a bit about that?

Charly: Absolutely, when we started out about twelve months ago, I thought that we would have at most half a dozen, maybe a dozen of fellow travelers who would commit a hundred percent of their business assets to positive impact. We now have thirty six efforts actually participating in that. These thirty six efforts represent mostly family offices but also have individuals, and some small to midsize foundations. Accumulatively about 3.5 billion dollars committed to impact and safe reported about eight to nine hundred million are already into impact. This network expands the globe, so we have participants from Australia, from Hong Kong, from Switzerland, Germany, UK, Netherlands, and the US. It's really for asset owners all the way from one million dollars in a management to six hundred fifty million dollars, in a management.

We position this network for asset owners of one million to one billion. Funny enough, when the giving pledge folks actually met four or five weeks ago in Santa Barbara, one or two of them found out about the 100% IMPACT Network and called me and said, "hey I

don't want to just give out money like the giving pledge does but I actually want to invest like you do." We are gaining visibility also to billionaires and billionaire family offices that are interested in not just aligning their philanthropy with what they care about but also their investment strategies and family of businesses.

Carol: Speaking of investing and you said this earlier. You have to be able to find a way to measure it. It isn't all about counting, it is often about or at least thorough due diligence on when we make an investment. We have done that for years on the financial side and most people know how to do the financial side. What they don't know so well is how to do the social side. That's why I just wrote my new book to try and of give people a sense of what (and it comes out Monday by the way) which is how to really asses whether or not a social or a venture will actually produce the kind of impact that we hope it will produce and create the level of change which is possible. I know you have been thinking about that for a very long time.

Can you describe what you hold in your mind to measure whether the social and ecological return is going to really happen and come at the level you want it to? How do you check the progress as it moves along?

Charly: First of all congratulations on your book. That is great that it is going to come out and I look forward reading it and great work, so thank you for that contribution. With respect to due diligence on the impact side; it is a very, very important principle. We talked about the intentionality of making impact, the second principle of impact investing in particularly for the hundred percenter's [ph] in paying attention to the impact. From intention to attention, and intention and attention are like strategy and vision. A vision without a strategy is as bad as a strategy without a vision. You can have great intentions but if you don't put attention to actually accomplishing the impact, you will fail, you will predictably fail. The impact has to be centered and is centered all the investment activities that we do. From the due diligence all the way to developing and negotiating term sheets.

Ideally, we want to bake into our term sheets the impact metrics that we use to measure the impact. Then of course in executing the transaction, monitoring the impact and potentially exiting the investment. Even so impact investors don't like to talk that much about exiting impact, because impact should be long term as opposed to a short term maximization of short term impact. We actually like to change term sheets to a more dollar term relationship with investees as opposed to [inaudible]. To give you a sense and a concrete example of what we look at in the context of let's say an investment in the wind farm. Wind farms usually are very good in the ecological return because they are renewed energy and we can argue that they replace part of the old [inaudible] economy.

From that perspective, they usually come fairly high on the environmental return. Sometimes when wind farms however go and build their wind parks, they have to replace people who live on the land that they actually have their wind farms on. We recently did a due diligence on an international wind farm provider and we found out that they did not compensate the indigenous population in this instance in middle America, correctly, therefore the social impact is very, very negative for us. Therefore, we could not invest in that particular wind farm, because even so, the environmental impact was quite good, the social benefit was awful. You can see, how us, impact investors, if we find out that this is happening; we need to actually have both.

People sometimes say, what about the negative impact? We know that almost all, I would say every investment has a negative impact as well. What impact investors try to do, is maximize the positive impact and minimize the negative impact. Therefore, having transparency on both sides is so crucial for us and that is why the 100% IMPACT Network and the Toniic network, we use to compare notes on that and make no mistake, if I were to find a more impactful environment, more impact for the investment in any asset class in the investments that I have; and equitity, I would swap them out. Just like a conventionally investor would swap out a better performing financial investment for a worse forming financial investment. We think the same except we replace the financial with impact.

Carol: That's great. Do you have an example of one that you feel really is starting to represent what you want to be doing? You gave us one when [inaudible] because your due diligent should, had the too bigger short fall on the social side.

Charly: Absolutely, yes.

Carol: Tell me what really works?

Charly: Let me start out by starting with cash investments. Everybody has cash and most people bank with one of the big banks. The big banks are really not transparent with the impact that they have. They are actually not transparent with what they do with our cash and therefore, we don't bank with the big banks, but we bank with community development banks. Community development banks are very, very transparent with respect to what they do with your money. They usually support the local economy; they might support the local entrepreneurs, work with the entrepreneurs; etc. We for instance do a lot of banking with a new resource bank in San Francisco or Southern Bank Corp in the southern US. It's not more recipe to do a banking business with them than with commercial banks because they are all FDIC insured.

You can see, actually anybody who has money, just cash like we all do, should actually bank with banks that line up with the values that they believe in. Now with respect to early stage investments, a recent investment that we did called Biolite. Biolite produces cooking stoves for two big markets. One is the recreation market in Northern America, and the other one is really the cooking stove market all over the developing world. They have been very, very successful on both sides. The impact that we look for is actually the penetration of cooking stoves that are less polluting [inaudible] into the developing world which is going really, really, really well. They are already profitable and distribute some of the profits back to the investors.

That will be a great example of a very successful company that's only two years old, that already has a huge impact as well as is on the path of providing great financial recurring as

well. One more example just to give you a sense of all of the different asset classes that we invest in. In real assets, we cannot possibly invest in the old extracted technologies and industries; because not only do they pollute the planet by leaving chemicals in the earth, a lot of times they often don't treat their workers right. The many instances the environmental return is as valuable as the social return. However, we do invest in the modern resources; be that carbon offsets, renewable timber, water and things of that nature.

Land use management, and one investment that we've done is in a mixed land use fund, so that gives you a sense that we invest in. I just told you about cash, I told you about an early stage direct investment, now I tell you and your listeners about a fund. [Inaudible] with capital and [inaudible] with capital one and also with [inaudible] with capital two and they are on track and raising the next funds which is one of our success criteria's. In [inaudible] capital just like we've been using this land use meaning putting conservation easements on the majority of the land that they actually purchase and then they put part of the land to conservation easement which means that nobody who purchases that land later can actually develop it. They also use some limited opportunities for development for ranchers or for recreational facilities in a more sustainable way such that the combined the combination

I've found sustainable development and conservation easement together provides a nice package that then they can sell it and right now there's a good market for this, for instance; we made a spectacular financial, I should say very good financial recurrence even during the 2008, 2009 years because the market was there even so for the majority of real estate it was a very, very difficult market in that time. That gives you another sense of where we combine financial recurrence with clear benefits for land conservation which in this instance we measure as acres preserved or restored. We have many, many more examples. Our foundation KL Felicitas Foundation is considered a leader in this space and they are very, very transparent about all of our investments and all of our asset classes.

I think we've done about thirty eight investments across our asset classes and each one of them has an explicit positive ecological and or social recurrent.

Carol: There's one other player or set of players in this space that I wonder how you relate to them and that are the regulators. There's this security exchange commission which is looking right now at whether or not they should raise what an accredited investor means. That's of course creating chaos and confusion and even fear among many startups which have depended on different models of people investing in them. How do you thing about what the SEC's role is in particularly this question of what the role of the accredited investing is and moving more people into being able to think about how they spend their money, even if they are not fully accredited investor?

Charly: That's a very good question and I love that one because it allows me to discuss a little bit the challenges of different segments of investors. All the way from institutional capital to the retail investor. Let's start with the retail investor because retail investors will soon have the opportunity to participate in the impact economy through crowd funding and crowd investing platforms. The jobs act of 2014 that the Obama administration enacted provided the legal framework for enabling crowd investing to move beyond the accredited investor. I think the last update actually enabled accredited investors to participate in crowd funding platforms and crowd investing platforms in the US like Crowd Funder and Indiegogo are already allowing accredited investors to participate in the fund raising in the investments of these deals.

I think in Quarter Four or at the latest 2015 the last piece of the jobs act to be implemented which will enable non accredited investors to participate in crowd investing activities. We believe that the collaboration between let's say the economic network and the crowd would be one opportunity for making sure that the crowd actually participates in the wisdom and the due diligence information gathering and sharing of more experience investors like Toniic members are and indeed we've made Toniic members in this instance, have already experimented and invested together on crowd investing platforms. I think it's a major movement all the way, also in Europe as well that enables ultimately more people to

participate in supporting these impact entrepreneurs and impact enterprises. The opposite of the SEC, the opposite spectrum of investors, institutional capital has a very different challenge.

There all the institutional capital a lot of times has a very narrow interpretation of the fiduciary responsibility in particular in the US. So that the legal folks and the trustees right now consider their view is to look short term as opposed to and long term, right? I think the pension funds in Europe are starting to actually change that but it won't be the really [inaudible] for the SEC and the Regulators to actually make sure that the definition of what people share responsibility really means, includes long term responsibility of not messing up the payment. I talked to pensioneers, here and there about the responsibility of pension funds and if you ask the question to the pensioner, did you actually want to mess up knowing the payment for your grandkids by drawing your pension, of course they would say no.

However, if I then paid them to go to their pension fund, and paid them not to invest in this and this and this knowingly messes up the payment. The pension fund threw back and says well you don't understand real risk. Do you want your pension or do you want to do good? That usually silences the pensioners. What they should say in response to that, is I want it both. I want to have my pension and I don't want to mess up the payment. The system right now portrays an either or choice and it's not. We have shown with our portfolio, with the report that just came out five months ago with Sonen Capital that you can actually have a portfolio that is fully invested in impact and have competitive financially incurring, in each one of the asset classes. That's what we do with one hundred percenter's, is we would document half a billion dollar portfolios.

Our foundation represents about ten billion dollars, where we invest about fifty billion according to the same guidelines the absorption capacity of all the investments that we've done is thirty eight billion dollars. So the argument that it's not enough product out there to invest is wrong as well and we think that our portfolio approach takes from five million to half a billion, which it does, and that what the hundred percenters are doing and once that

we prove that we can actually invest a half a billion dollar portfolio, with financial recurring impact then there's no reason why the single digit billion dollar endowments and pension funds could not be forged into making sure that they actually not knowingly mess up the payment anymore.

I think the first move on the regulatory frameworks should be foundations. Foundations actually get the tax benefits from society for accomplishing the mission that they care about. It's paradoxical to me that some foundations actually claim to society that they care about the environment yet they are contributing in their investment strategies to climate change, right? There is an invest campaign [ph], going on which the hundred percenters support to make sure at least that foundations that get the tax benefit for society for actually doing something for the environment without knowingly [inaudible] their investment strategies. I think those are first [inaudible] opportunities for the regulators to actually move into.

To me it should go of course a lot further, I don't see any reason why in ten or fifteen years, a CEO of a publicly held company would not have to be sued when this company actually knowingly messes up the payment.

Carol: Yes, great. It's interesting; I hear you definitely redefining fiduciary responsibility in this and much more inclusive. I hear you redefining something else which is what I call financial literacy because the literacy is limited by the way foundations and regulars and so forth are thinking. Are you conscious of trying to bring about this, and literacy happens at the institutional level and it's limited all the way down to [inaudible] and the pensioners. It feels to me like that's where one of the big gaps we have is this ability to understand how finances work and what they produce.

Charly: Yes Carol, that's a very, very important observation. Right now the impact investors need to be conversing in both languages. In the old language of modern portfolio theory which is typically wrong, we need to cast our arguments in the old terminology in order to be heard in order to make our arguments while we of course prepare the new system. What I

mean by this is it gets a little bit technical, but not too much. Modern portfolio theory. I keep it on the very high level. Modern portfolio theory is clearly wrong on a number of levels. First of all, it claims that the rational investors who are only out to maximize our financial return. Me and my wife and all the hundred percenters and all of the Toniic members clearly don't fall into this category.

I think if everybody had a choice an open choice that they would not [inaudible] so clearly wrong. The secondarily modern portfolio theory pretends that's there's anything close to perfect markets. There are no perfect markets. Thirdly and that really is one of the biggest failures is, that anything they cannot explain they consider outside the system as externalities; externalities conveniently not having to [inaudible] into the system. We do not accept that as a working theory. We demand that these externalities are actually internalized into the macroeconomic [ph] system with the way that the financial system works. [Inaudible] of course but many macroeconomists and financial analysts, they pretend as if the system is a godsend system as if it was always there and would always be there.

To me it's just really amazing at best that seemingly very, very intelligent people who study these things pretend that a system that was invented ten or fifteen years ago for a planet with seemingly unlimited resources where maybe one point one billion people live on the planet would not have to be majorly restructured where eight to nine billion people and clearly limited resources. Yet the majority of the people who are in the driver's seat pretend as if nothing weird is happening. We need to define modern portfolio theory to put positive impact first and foremost into everything that we do on the investment side. That will require a fundamental reimagining of the relationship between risk, return and impact.

The conventional system pretends that it is okay to invest in mines that leave an awful amount of chemicals on the planet, on the surface and inside the planet and they don't treat the workers well. They say that, well that risk interest recurring, we say it is not. You have to pay for clean up, you have to pay for treating the workers at least decent and then they say well we don't get the risk adjusted returns. We don't accept the notion that risk

adjusted return is cracked if you knowingly mess up the payment and you don't treat your workers right. You need to refrain from the discussion that nobody can get away with that. Then we say with the hundred percenters, what if we were to create a new fund for us from the real asset side that we capitalize with two to three hundred million and start investing in [inaudible] mines.

Start investing in mines where everybody is treated correctly and the cleanup is done correctly. Where we've been the first to creation of this fund, we would have to take inter conventional wisdom [inaudible] financial return. We don't see it that way, its risk adjusted rate of return in the conscious of cleaning up your mess, right? We believe in the next generation then, we give hopefully the politicians enough fire power to stand up against the big corporations to say no we have to clean up your mess. We are not going to foot the bill anymore with tax payer's money and have to get away with that. If the sense of impact investors really don't take the conventional wisdom, as conventional wisdom and almost like it's a religion of the macroeconomists who [inaudible].

Carol: That's excellent. I think that one of the words that I wish you would spell for me because I know people are going to go try and Google this and find it. Are you saying connect group or what is the word of the group that you are talking about and how do you spell that?

Charly: Was that the hundred percent? No, sorry I didn't…

Carol: The connect?

Charly: No it was not connect.

Carol: What is the name? You said there were two groups, the hundred percent club and there is the second one.

Charly: Oh, toniic, sorry tonic, t o n i i c.com.

Carol: Okay good, because that was the final question I wanted to ask you was; you are a most intriguing person and I think of a million other questions that can follow from everything and there are going to be people who want to track you further. Maybe even try and reach out in some way. What is the best way for people to find out more about either of these organizations, the work they are doing, the way you think, and to pose something to you as a question? If you would be so kind as to tell us how to do that.

Charly: Absolutely, so my name is Charly Kleissner and that's spelled C h a r l y and my last name is K l e I double s, like Sam, n e r. My email is Charly@Kleissner.com. You should feel free to use my email and send me email. You can also login to Toniic which is t o n i i c .com. There is not yet a website for the hundred percenters because we have to officially launch it. We will probably launch this next year when we have some [inaudible] portfolios from single digit millions to half a billion in order to make it really more meaningful and then in order to inspire other family offices and tie it with individuals and [inaudible] with investors to follow.

Carol: What about the foundation that you and Lisa set up?

Charly: Yes, so the foundation, we are very, very transparent with respect to like I said to all of our investments and the financial recurrence and the impact report that's going to come out soon. Our foundation is KL Felicitas Foundation let me spell that for you, that's K L F e l i c I t a s, KL Felicitas, one word, foundation.org. If you Google Charly Kleissner, you will probably find the foundation as well if it's too hard to find.

Carol: I think you are probably right. This has been a wonderful conversation. Thank you so much for joining me and I'm going to disconnect us now, and just follow up for one…

[End of Transcript]