

## Harmon Wilfred

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**From:** brendan howley/twinfish [inkfish@orc.ca]  
**Sent:** Thursday, 26 April 2001 4:07 a.m.  
**To:** Harmon & Carolyn  
**Subject:** an interesting development FYI  
**Importance:** High

Hey guys  
I still haven't heard from Neil. I'm seeing his closest CBC colleague for breakfast in TO Sunday am. Will update then.  
This surfaced on a listserver I subscribe to on intelligence matters. It struck me that your experience, Harmon, is eerily close to what's detailed in this Financial Times article...looks like your friend Austin \*really\* knew stuff...  
bye  
Brendan

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Monday Apr 23 2001

### 1. FRONT PAGE - WEEKEND FT: Mischief or conspiracy?

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FRONT PAGE - WEEKEND FT: Mischief or conspiracy?  
Financial Times; Apr 7, 2001  
By GILLIAN TETT

Japanese certificates 'worth' trillions of yen have been turning up in financial centres around the world, But their origin is the subject of secrecy and controversy: are they-part of a complex political plot, or a ploy to trap foreign investors? Gillian Tett reports

It looks innocuous enough: a simply worded warning about "fictitious bonds" sits on Japan's Ministry of Finance website. In fact, it is a gateway into a world swirling with explosive accusations of fraud, conspiracy and political interference.

The site carries a picture of what looks like a Japanese government bond, slashed by two diagonal red lines and warns that such certificates have never been issued by Japan.

But that hasn't stopped these mysterious "quasi-bonds" from turning up in financial centres around the world. In total, their purported face value comes to trillions of yen.

And their origin is the subject of mystery and controversy. Are these

quasi-bond certificates part of a complex political conspiracy, or are they simply a ploy to trap foreign investors?

One man convinced the certificates are real is Norbert Schlei, a senior US lawyer and former adviser to President John F. Kennedy. In 1995, he was apprehended in Florida for handling these certificates and charged with securities fraud.

In his defence, he told the courts the certificates were legitimate and owned by a dozen of his Japanese clients. Then he dropped his bombshell by claiming Japan's Ministry of Finance had secretly issued the certificates in the 1980s to conceal a hidden political slush fund. And this slush fund was linked to money that the CIA allegedly had used to fund rightwing political groups in Japan, as part of an anti-communist drive.

Schlei is now 71 and works from small law offices in Los Angeles, decorated with pictures of himself working with President Kennedy. He was given a five-year suspended prison sentence in 1995, but the conviction was mostly overturned on appeal. "I am absolutely convinced that these certificates were issued by the MoF," he still says.

If he is right - and Japan's MoF vehemently denies his account - the repercussions could be huge. For a start, the Japanese hate the idea of the US meddling in their political affairs. And there would be a marked reaction in the bond markets if it emerged that the MoF had secretly issued extra bonds.

The ministry claims it is a simple case of fraud, with criminals using the certificates to fool naive investors. "The idea (that we) could have secretly issued hidden bonds is crazy and shows how gullible people can be," argues one senior MoF official.

But Schlei's version of events is the one supported in a book, yet to be published, by Sterling and Peggy Seagrave, two US authors who have written extensively on Asia.

"When the American and Japanese public find out what has been going on all these years, particularly with regard to covert financial mischief, there will be a huge public outcry," they say.

In fact, finance and politics in Japan are deeply murky and the complete truth may never emerge. But there are two main theories as to where the bonds came from.

The official explanation, by the MoF, is that a gang of Japanese crooks printed them in the 1980s. Some of the gang were convicted in Japan for fraud in the mid-1980s, given a suspended sentence, and have now disappeared. But the certificates were distributed to criminals overseas, who continued the fraud, say Japanese police. Indeed, police records noted more than 20 occasions between 1986 and 1993 when foreigners were caught handling the certificates overseas, sometimes in connection with fraud cases in the UK and the US.

It sounds credible - but contains odd details. No financial institution has

ever admitted losing money as a result of these bonds. And the MoF did not declare the certificates counterfeit until 1993 - a decade after they first appeared. It has also seemed reluctant to permit its bureaucrats to testify that the certificates were fake. At one trial in the US, an MoF witness disappeared early, and the tape recorder collecting his evidence broke. The ministry blames this on a "misunderstanding".

Another oddity is the certificates' design. Criminals usually make fake bonds identical to real bonds and in small denominations, to avoid attracting attention. The "quasi-bonds", however, do not even pretend to be a Japanese government bond, but an IOU - of a type not seen in Japan.

Each certificate is dedicated to a specific Japanese person, and says it can be exchanged for 15-year bonds in the future, via the Bank of Japan 'and Dai-Ichi Kangyo Bank as an agent of the Bank'. They claim to have been issued in 1982 - or Showa 57 in the Japanese calendar (they are sometimes called "series-57 bonds" by Americans). Their denominations range from Y10bn to Y500bn - a ridiculously large amount for a counterfeit certificate.

But if that looks suspicious, the other explanation is far stranger and begins in the early 20th century, when Japan invaded its Asian neighbours and looted vast wealth.

After the second world war, US intelligence forces secretly seized this wealth and later used it to finance covert anti-Communist operations - paying bribes, for example, to right-wing members of Japan's Liberal Democratic party. Schlei told the Florida court that in the postwar US, "we came to feel that (such payments) were OK because the Russians were subsidising the communists and socialists".

In the 1960s, the US returned control of this fund - called the "M-fund" - to Japan. Japanese politicians, such as Kakuei Tanaka, a former finance minister and later prime minister, grabbed it.

stole large sums and used it for their personal use and to buy political support with bribes.

"For 25 years Tanaka was known as the money man of Japanese politics. My clients say the reason he had so much money was he got control of this M-fund," Schlei said.

In the 1960s, Tanaka tried to hide some of the fund by buying JGBs and registering them in the name of his cronies and supporters. But in 1976, he was sucked into a corruption scandal and convicted of receiving bribes from the US Lockheed company.

In the following years, his cronies wanted extra money and, in the late 1970s, the Tanaka clique decided secretly to print what have become the disputed certificates, as part of a complex financial scheme.

Tanaka then double-crossed some of the holders of these certificates: in the mid-1980s, the MoF indicated it would not honour the certificates, and rumours circulated that the M-fund money had all been stolen. When some

certificate holders believed they had been tricked, they began seeking ways to obtain financial compensation for their paper.

This is where Schlei says he became involved. He had spent the 1970s and early 1980s working as a senior partner of Hughes, Hubbard and Reed, a Wall Street law firm, representing blue-chip clients such as Howard Hughes, the billionaire, and Morgan Stanley, the US investment bank.

This followed a spell in the 1960s when he worked with Kennedy - he is credited, for example, with having played a key role in advising on the Cuban missile blockade. However, he decided not to go into politics full-time because he became disillusioned after Kennedy was assassinated.

By 1985 he was semi-retired but in touch with a Japanese businessman called Toshio Takahashi.

Takahashi knew of several holders of the certificates who wanted to use a US lawyer to press their claim against the MoF. Schlei said in court: "(My clients) felt that if they could prosecute their claim from outside Japan, they would do better than inside, because in Japan the government controls the financial world so totally." Schlei says he accepted the case, lured by promises of large fees (which he says he never received). And in the following years he worked on the matter sporadically. He created a company in Panama to handle the certificates and persuaded Alan Cranston, a US senator, to ask the MoF to recognise them.

He openly consulted the CIA and the US ambassador to Japan, and visited Tokyo, where he claims the MoF held occasional negotiations with holders of the certificates.

Most controversially of all, he tried to persuade non-Japanese institutions to buy the certificates for a nominal fee - apparently unsuccessfully. US banks, such as Morgan Stanley, and government officials in Taiwan and South Korea, were approached. Schlei even attempted to involve the US Young Astronauts Association.

He says he approached 135 banks, not because he wanted to conduct a fraud, but because he believed the MoF would feel more pressure to redeem the certificates if they were held by foreign institutions.

In the early 1990s, however, FBI agents approached three US entrepreneurs who were contacts of Schlei's client, Takahashi, and offered Dollars 100m to buy some disputed certificates. A deal was struck, and the FBI arrested the entrepreneurs for fraud. A year later they dragged Schlei into the case, arguing that he had handled the certificates as well.

Schlei denied knowing anything about the deal with the FBI agents, and says the case unfairly "destroyed my life and career".

The Seagraves agree: they say Schlei was only involved in the case because he was a trophy "catch" for the FBI, due to his past links with the Kennedy administration, and because some US officials wanted to stop Schlei asking "potentially embarrassing" questions about the M-fund.

"Schlei was unjustly charged and tried," they say.

The FBI, however, insisted Schlei was part of a criminal ring and that his "explanation" for the certificates was just a cover for fraud.

Indeed, parts of Schlei's tale seem suspicious: he has refused to name his mysterious clients, citing confidentiality clauses; no Japanese has publicly admitted to owning these certificates or openly come to his defence; nor have any US officials backed Schlei. Stanley Sporkin, a former CIA official, dubs the M-fund "a crazy idea, preposterous". Daniel Russel, a US diplomat, told the Florida court that it was 'totally unbelievable that such a conspiracy could have been in progress for decades without it becoming widely known'.

At the same time, many parts of Schlei's tale look plausible: the LDP has been entangled in corruption scandals in recent years, sometimes linked to violent yakuza gangsters; Japan's national accounts are very opaque; and Schlei is not the only foreigner talking about these certificates.

Some former Wall Street bankers, who insist on remaining anonymous.

say that in the early 1990s they were hired by government officials in Paraguay who had acquired some "bonds" and wanted to offset them against Paraguay's debt to Japan. They hired Alexander Haig, a former US secretary of state, to find out whether Japan's finance ministry would accept a deal. The Seagraves claim a deal was struck. An aide to Haig confirmed he held discussions "on behalf of the government of Paraguay" but concluded that the project was "without merit".

Odder still, these bankers still hold documents about a "Welfare Fund", or the alleged cover for the M-fund. These papers tally with the "quasi-bonds".

These documents could be clever forgeries. But Edmond Lausier, assistant professor for business studies at the University of Southern California, thinks not. He has compared these papers with official records on Japanese government bond issuance. (He says he did this because he heard Schlei's story and "likes solving puzzles".) And he says his findings support the theory that Tanaka was playing financial games with the disputed certificates.

But the most curious part of Schlei's tale is the allegations about the CIA and the M-fund. There is no concrete proof that an M-fund did exist, since the CIA is refusing to release its files on Japan for the period, and most politicians allegedly involved are now dead. Even so, some US academics suspect that an M-fund did exist.

"Evidence of an M-fund between 1947 and 1972 rests on more than the statements... of Schlei and his clients," says Chalmers Johnson, a former professor at the University of California.

And in the mid-1990s, former CIA officers told The New York Times they gave funds to rightwing politicians in Japan - prompting criticism that the US distorted Japanese politics. Or as John Dower, professor of Japanese

history at the Massachusetts Institute of Technology, has said: "We look at the LDP and say that it is corrupt and it's unfortunate to have a one-party democracy in Japan. But we (Americans) have played a role in creating that misshapen structure."

The CIA says it is unable to comment on whether it gave any funds to the LDP in Japan and has no knowledge about an M-fund under Japanese control.

So where does this leave the mysterious certificates?

Some foreign bankers remain convinced they are fake. After all, they argue, an M-fund might have existed - but unconnected to the certificates. "Japan is a paradise for fraudsters," argues one US banker. On the other hand, some bankers believe the MoF may eventually be forced to honour the certificates.

Meanwhile, the bankers involved in the alleged Paraguay-Haig discussions have found their own solution to the mystery - of sorts. They have written a novel, loosely based on their experiences with the certificates. Ominously, many characters are murdered by yakuza.

"Our story was so weird that fiction seemed the best way to talk about it," one of the former bankers explains.

"Who would believe it?" In Japan, it seems, truth and fiction can be closely entwined.

Golden Lily, published in November by Transworld (Bantam) (UK); Random House (US); the M-Fund novel can be found at [www.oldmenswar.com](http://www.oldmenswar.com); the MoF website warning is at [www.mof.go.jp/english/bonds/bon001.htm](http://www.mof.go.jp/english/bonds/bon001.htm)

<http://timeoff.ft.com/weekend>

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