
THE MILITARY'S FUNDING AND ECONOMIC INTERESTS

Discipline, organization, and unity are three important keys to the TNI's strength, both as an institution and as a major player in national politics. A fourth key to its strength is its economic power. The TNI receives only a fraction of its funding from the central government budget. Most of its funds come from off-budget sources that no outside observer has been able to quantify. As Samego et al. (1998a, pp. 25–26) point out, not only does the military require complementary resources for its national defense mission but, in the view of some observers, the military's sociopolitical role requires it to be involved in all fields of public life, including the economy. In fact, much of the TNI's involvement in "politics" centers on its business operations and the huge territorial structure that lends power to those operations.

The military's business empire has important political, economic, and social ramifications. Its involvement in business activities seriously hinders military's professionalization. Moreover, military funding is an important issue in civilian control of the military. Without complete control of the military budget, parliamentary control of the TNI and the police remains fragile. By refusing to adequately resource the TNI, the parliament and the government have abdicated their responsibilities to properly maintain the armed

forces and empower those in uniform who distrust civilian oversight.¹

The 2002 Indonesian defense budget is about US\$800 million, less than 1 percent of Indonesia's GDP and less than 4 percent of the government budget. It is estimated that this amount covers less than one-third of the operational expenses of the armed forces.² In fact, the Indonesian central budget has never fully funded the armed forces. The paradox of the New Order was that even though in its early stages it very much had the characteristics of a military regime, the military budget as a percentage of the state budget declined steadily from 27 percent in 1969–1970 to 7 percent in 1993–1994 (Kristiadi, 1999, p. 102). The reason for the military's unwillingness to seek a larger share of the state budget was that by the 1960s a structure of military-run businesses and economic activities was in place that filled the gaps left by the inadequate state budget.

Military business is, of course, not unique to Indonesia. Militaries in many other countries—such as Thailand, Pakistan, and Brazil—in what used to be known as the “developing world” have been heavily involved in economic activities. Only as their economies developed and their militaries became more professionalized did they begin to withdraw from direct participation in the economy. In some Communist and post-Communist societies, the military has been the dominant player in the economy and the main source of skilled business managers.³ In China, the People's Liberation Army was ordered to withdraw from the business sector in 1998, but the practice

¹Comments by Colonel (retired) Charles D. McFetridge, graduate of the Indonesian Army Command and General Staff School and former U.S. Defense Attaché in Jakarta, June 2002.

²Most of the military budget is for personnel and welfare costs. There is an inherent uncertainty in quantifying the Indonesian military's off-budget income, but most estimates concur that it is about two-thirds of total TNI income. Some military sources question this figure and argue that off-budget TNI income is lower than the percentage of TNI income usually cited (interview with Lieutenant General Agus Widjojo, Washington, D.C., February 2002).

³In Cuba, military-run enterprises generate 89 percent of exports, 59 percent of tourism revenues, 24 percent of productive service income, 60 percent of hard-currency wholesale transactions, and 66 percent of hard-currency retail sales, and employ 20 percent of state workers (Espinosa and Harding, 2001).

is still prevalent in states such as Cuba and Vietnam (Mulvenon, 2001).

The military's business empire does many things for the TNI. It funds some operational and minor capital requirements, as well as health care, schools, and the type of social services supported in the U.S. military through nonappropriated funds. It provides a social safety net and supplements the abysmally low salaries of its personnel, from junior enlisted men to its most senior officers.⁴ The military, therefore, has little choice but to protect this resource. It will take many years for Indonesia to generate a modern system of taxation that will adequately fund its government operations. Until then, the TNI will not give up one rupiah from its off-budget sources that it does not have to surrender.

The Indonesian military's involvement in the economy, as already noted earlier, was consistent with common practice in other countries and with the national strategy that stressed territorial defense and self-sufficiency. As Major General Suhardiman stated, "During the war, the military were engaged in business to carry out economic guerrilla war against the occupiers. The aim was to undermine the occupiers' economy and seek funds needed to finance the war and revolution."⁵ The armed forces' participation in the economy took a quantum jump in 1957 when Dutch enterprises were nationalized. Military personnel were placed in prominent positions in these enterprises, allowing the military to develop an economic network that it was able to use to generate income in the deteriorating economic climate of the later Sukarno years. The military's economic role expanded again in 1964, when British enterprises were also placed under military supervision, and again in 1965, when some American properties were taken over (McCulloch, 2000, p. 11).

In the period of fiscal retrenchment in the early 1960s, military salaries, never overly generous, began to fall farther to the point that they no longer met even subsistence requirements. As a consequence, commanders bridged the funding gap in various ways.

⁴Military equipment purchases, capital and operational expenditures, uniforms, salaries, and certain allowances are covered by the military budget (discussion with Lieutenant General Widjojo, Washington, D.C., February 2002).

⁵Cited in Samego et al., 1998, p. 47.

Military officers assigned to manage state enterprises were ordered to channel enterprise funds to the military directly, in addition to the income diverted to them and to their subordinates (McCulloch, 2000, p. 12). At the local level, the military resorted to a policy of “communal provision.” Local units raised their own funds by levying unofficial taxes and becoming involved in myriad commercial activities. To feed and shelter his battalion, Lieutenant Colonel Rudini (later general and army chief of staff) used military trucks to transport commercial products, set up a chicken farm that supplied meat to the troops, and established a discount-price store in the base’s cooperative that sold eggs, among other things (Samego et al., 1998a, p. 52).

As commander of the Diponegoro Division in Central Java from 1957 to 1959, Colonel Suharto created a veritable business-military empire. Suharto and his associates set up a number of companies, with capital from two charitable foundations, or *yayasan*, one ostensibly for the economic development of the region and the other for the support of retired military personnel. The scope of these economic activities exceeded the tolerance of the High Command and Suharto was removed from his position and assigned to the armed forces staff college in Bandung (Vatikiotis, 1993, pp. 15–16).

From these beginnings, the military-run businesses developed under the New Order into an extensive structure including natural-resource extraction, finance, real estate, manufacturing, and construction. The military’s machinery for mobilizing funds can be illustrated as a pyramid (see Figure 7.1). The top of the pyramid is the official defense budget that, as noted later in this chapter, represents perhaps one-third of the military’s overall income (but no one knows for sure). Below the official budget is the income derived from state enterprises. In the next level down are the TNI-run cooperatives and the businesses owned by the military foundations (the *yayasan*). Like the rest of the Indonesian economy, these businesses have been battered by the 1997–1998 economic crisis. In the tier below are all other sources, including the businesses organized by individual local commanders. These commanders mobilize funds through services or contributions to local businessmen. Fundraising activities at this level are not necessarily known, at least in detail, to the senior army leadership.

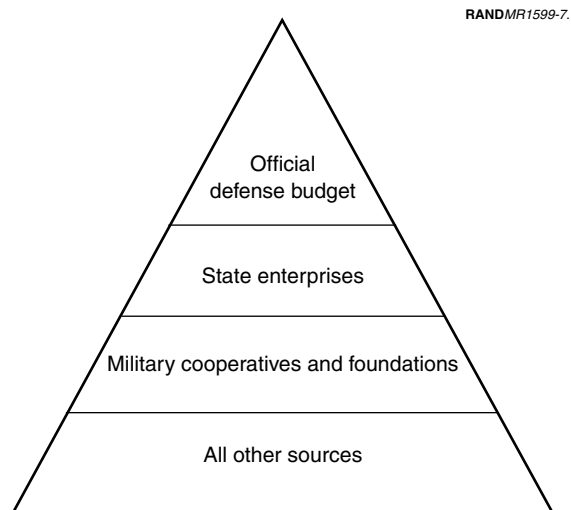


Figure 7.1—TNI Economic Support Structure

The main components of the structure, described here in more detail, include:

1. **State Enterprises.** The expansion of state-owned enterprises came about as the result of the nationalization of Dutch and other Western assets under Sukarno. The most important of these companies for the military are Pertamina, the state oil corporation, and the Badan Urusan Logistik (or *Bulog* for short), the state logistics agency, which controls the distribution of rice and other commodities. There are also large state enterprises operating in the infrastructure (telecommunications and electricity) and banking sectors. In addition to military management or control of state enterprises, retired senior officers were routinely appointed as directors of both public and private firms (Crouch, 1993, pp. 275–282; Samego et al., 1998a, pp. 72–77; McCulloch, 2000, pp. 23–25).
2. **Cooperatives.** The cooperatives function at both the national and local level. They run wholesale distribution businesses that provide affordable basic necessities and relieve operational and personnel costs not covered by the central budget. The structure of the cooperatives is hierarchical. The main level is at the TNI

headquarters. The Kodam (regional headquarters) maintains the central level, and the Korem maintains the primary level. Funding for the cooperatives comes from two sources: member dues and holding companies.

3. **Foundations (Yayasan).** The yayasan are chartered as charitable foundations exempt from taxation and also from the law that forbids active-duty military officers from being involved in business activities. The TNI headquarters, army, navy, air force, Kostrad, and Kopassus all have their own yayasan; the Ministry of Defense has two of its own.⁶ Each yayasan has at least one and often more holding companies, generally organized as joint ventures with private businessmen, that generate the foundation's income (Crouch, 1993, pp. 282–284; Samego et al., 1998a, pp. 77–79; McCulloch, 2000, pp. 18–23).

ARMY BUSINESS INTERESTS

The army's business network includes the army foundation, the Yayasan Kartika Eka Paksi (YKEP), the main army cooperative (Inkopad), and a primary cooperative (Primkopad). YKEP's business activities are managed by a holding company, PT Tri Usaha Bhakti. The various army interests include the Sudirman Central Business District, which owns 44 hectares in what is known as Jakarta's "Golden Triangle," the Artha Graha Bank, Cigna Indonesia Assurance, Danayasa Artatama (the Hotel Borobudur), other real estate, timber, golf courses, and manufacturing. The foundation is used primarily to provide for soldiers' welfare, especially housing, but it also supports the Army University Ahmad Yani in Bandung, and distributes Muslim New Year and Christmas bonuses to army personnel. Inkopad has business interests that include the Kartika Plaza Group, which owns the Kartika Plaza hotels in Jakarta and Bali, and recreation, construction, fisheries, and forestry businesses. Unlike other sectors of the military's business structure (such as Kopassus)

⁶The main military foundations are as follows: Ministry of Defense: Yayasan Sudirman and Yayasan Satya Bhakti Pertiwi; TNI headquarters: Yayasan Manunggal ABRI; army: Yayasan Kartika Eka Paksi; Kostrad: Yayasan Darma Putra Kostrad; Kopassus: Yayasan Korps Baret Merah; air force: Yayasan Adi Upaya; navy: Yayasan Bhumi Yamca; and police: Yayasan Brata Bhakti ("Foundations of the Indonesian Military," in Singh, 2001, p. 16).

many of the army's businesses successfully weathered the 1997 to 1998 Asian economic crisis (Samego et. al, 1998a, pp. 79–81; Singh, 2001, pp. 17 and 21; Kristiadi, 1999, p. 104; "Red Beret Business," 2002).

The Kostrad foundation, through its holding company, PT Darma Kencana Sakti, acquired interests in Mandala Airlines, a chemical storage company partially owned by Mitsubishi, a plastic bag company that was a supplier to the state oil company Pertamina, a furniture company, a luxury car importer, and a real estate contractor (Samego et al., 1998a, pp. 82–83; Singh, 2001, pp. 19–20).

Kopassus's Red Berets Welfare Foundation, known by its abbreviation *Kobame*, was founded in 1993 and flourished under the tenure of Suharto's son-in-law Prabowo Subianto when he was Kopassus (and subsequently Kostrad) commander. The foundation teamed up with a private businessman to establish PT Kobame Propertindo. The consortium built the Graha Cijantung, a 55 billion rupiah commercial real estate project, on land belonging to the Jakarta military command. Halfway through the project, the private-sector partner resigned his interests and the business became wholly owned by the Red Berets. However, the interest rate on the bank debt incurred by the project rose above 70 percent as Indonesia suffered the effects of the Asian economic crisis and the project became insolvent. The project's debts were assumed by the Indonesian Bank Restructuring Agency and as of this writing are awaiting disposal. Kobame also set up a shipping business—KMP Tribuana Antar Nusa—but it failed in the economic crisis. Another subsidiary, Kobame Super Sentra, which was in the wholesale business, also went bankrupt ("Red Beret Business," 2002).

NAVY BUSINESS INTERESTS

The Navy established the Yayasan Bhumi Yamca (Yashbum), a main cooperative (Inkopal), and a primary cooperative (Primkopal). Yashbum owns Admiral Lines (shipping), resorts, and an oil refinery, and has businesses involved in property rental, import-export, cocoa plantations, maritime electronics and telecommunications, a taxi company, and diving services. The foundation operates two orphanages for the children of deceased seamen, provides scholarships for naval personnel, and operates the Hang Tuah school system with

approximately 22,000 students on naval bases. The marines, although formally under the navy, successfully ventured into the real estate business with the Plaza Cilandak joint venture in Jakarta (Samego et al., 1998a, p. 83; Singh, 2001, p. 23).

AIR FORCE BUSINESS INTERESTS

The air force's foundation is the Yayasan Adi Upaya, which manages its business interests along with its main cooperative, Inkopau, and its primary cooperative, Primkopau. The foundation owns the Bank Angkasa, together with the National Electricity Company Pension Fund and private investors. The foundation's other interests include golf courses, container services, hotels, and logging, aviation, and aerial photography enterprises. The foundation provides scholarships and health care for air force personnel and has built houses of worship at air force bases (Samego et al., 1998a, p. 84).

POLICE BUSINESS INTERESTS

The national police, a part of the armed forces until 2000, also established its foundation, the Yayasan Brata Bhakti Polri, and cooperatives, Inkoppol and Primkippol. Businesses included the Bimantara office building in central Jakarta, the Yudha Bakti Bank, and a majority interest in the Bhakti Bayangkara insurance company. The proceeds from these ventures are used to improve police barracks and station houses and to provide housing, medical services, and scholarships for police personnel and their families (Samego, et al., 1998a, pp. 85–87; International Crisis Group, 2001a, p. 20).

NONINSTITUTIONAL BUSINESS ACTIVITIES

There is also a large category of profit-seeking activities conducted by retired and active-duty military personnel and their families outside of the official military business network. This range of economic activities encompasses business operations in both the formal and the informal or “gray” economy. The military as an institution is not involved at this level, but individuals and groups of individuals are. An analyst in an independent Jakarta think tank has suggested that the value of military business is greater in the informal sector than it

is in the formal one. Informal sector practices include collecting commissions on goods and services produced by business partners; hiring out of military vehicles, aircraft, or ships; selling fuel and spare parts; and selling commodities from military cooperatives to local communities. These practices extend to illegal and sometimes criminal activities on the part of rogue individuals (McCulloch, 2000, pp. 26–32).

Active duty officers were prohibited from engaging in business activities in 1974, and this ban was reiterated several times—for instance, by Defense and Security Minister General Edi Sudrajat during a parliamentary hearing in 1997. In practice, enforcement was lax and in any event the prohibition does not prevent officers' family members from entering into partnerships with (usually) ethnic Chinese businessmen. In addition, the distinction between authorized and prohibited military business practices is difficult to ascertain. A study of Indonesian military business determined that the most successful retired generals in business were those who had developed strong connections to the private sector while on active duty.⁷

THE DEBATE OVER MILITARY SELF-FINANCING

Until the fall of the Suharto regime, the military's involvement in the economy was not a major issue. The thrust of the criticism of the business practices under the New Order was directed at the predatory actions of Suharto, his family, and his cronies, actions from which, it should be mentioned, the military itself was not immune. (In the early 1990s, Suharto's son Sigit Hardjojudanto and his crony Bob Hassan gained control of a majority of the shares in the Kostrad holding company PT Dharma Kencana Sakti. Kostrad did not regain full control until after Suharto's fall [Singh, 2001, pp. 19–20]). With the onset of reformasi, the rationale for the military's involvement in business began to be questioned. Reformers, including senior officers, recognized that the system of military self-financing had a seri-

⁷Businesses conducted by military personnel outside of the official framework (foundations, cooperatives, and enterprises) are discussed in Samego et al., 1998a, Chapter 4. The chapter deals primarily with large-scale enterprises run by retired military personnel, e.g., the business empires of former Pertamina CEOs and other senior officers. Private business activity is carried on at all levels of the TNI.

ous downside. It fostered corruption and illegal activities, harmed readiness, created disparities in the compensation of officers with varying access to off-budget funding, eroded ethical standards, permitted unhealthy independence from government budgetary oversight and control, and produced commercial values inconsistent with military professionalism.

The military's involvement in business activities stands as a major roadblock to the TNI's evolution into a modern professional military force. At the same time, it is widely recognized that it would be difficult to wean the military from its economic activities without substantially increasing the defense budget. This, in turn, as former minister Juwono noted, cannot be done without economic recovery.⁸

Given these constraints, there is a school of thought that argues that initially the focus should be on increasing transparency and accountability in the military's economic activities.⁹ Some efforts have been made by the post-Suharto governments to address this issue. Criminal Corruption Law 31/1999 includes the money available to the *yayasan* in the definition of state finance, thus strengthening the authority of the state auditing agency to audit the foundations. The process of auditing the army's business enterprises began in February 2000. The army hired Ernst & Young to audit the 39 companies under the army's foundation. The audit and evaluation were completed in October 2000, but as of this writing the results have not yet been made public ("Kiki Syahnakri: ...," 2002). Achieving transparency will be an uphill battle, however, given the military culture that allows commanders wide discretion in the use of funds raised through business activities and the inadequacy or lack of records.

⁸Angel Rabasa's interview with Juwono Sudarsono, Jakarta, February 2002.

⁹The confrontation between the reformist Kostrad commander, Lieutenant General Agus Wirahadikusumah, and TNI conservatives began in fact when Agus instigated an investigation of his predecessor Lieutenant General Djaja Suparman's expenditure of Kostrad funds. Wirahadikusumah was forced out of the Kostrad position and Suparman was cleared of allegations of corruption after an army investigation.