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Marine Corps University  
2076 South Street  
Marine Corps Combat Development Command  
Quantico, Virginia 22134-5068*

# ***MASTERS OF MILITARY STUDIES***

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## **THE BUSINESSES OF THE INDONESIAN ARMED FORCES**

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OF THE REQUIREMENTS FOR THE DEGREE OF  
MASTER OF MILITARY STUDIES

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## EXECUTIVE SUMMARY

Title: The Businesses of the Indonesian Armed Forces

Author: Major Chia Choon Hoong

Thesis: This paper traces the origins and evolution of the Indonesian military's businesses since 1945, examines the scope of these businesses and assesses the impact on Indonesia. With mounting pressure for the reform of the military, the paper will discuss the challenges of tackling the issue of the military's businesses and the prospects for change.

Discussion: Since the end of more than three decades of autocratic rule under President Suharto in May 1998, Indonesia has undertaken and continues to undergo significant changes in the political, social and economic spheres. One of the most pressing tasks had been political reforms aimed directly at reducing the military's influence in politics and its dominant position in government institutions and bureaucracy. While there has been a lot of focus on severing the links between the military and politics, the future of the military's extensive business interests, by contrast, has received little attention. The latter cannot be ignored as the military's extensive business interests act as a source from which the military derives a degree of political power through active involvement in the country's economic activities and relative independence from government funding. It also serves as a means through which the military is able to exert its political influence via business transactions between the military and the Indonesian people.

While the military's involvement in businesses has provided some tangible social and economic benefits for the country, there has been more harm done than good. Corruption, reduced combat effectiveness, weakened civilian control and disruption of

the real economy and current reform efforts stand out as the key problems that far outweigh those benefits. In the short term, the biggest challenges to the Indonesian leadership ability to deal with the military's businesses are the current economic downturn, internal security problems, particularly in Aceh and Irian Jaya, competing priorities for modernization of the military vis-à-vis improving pay conditions, and the lack of resolve to clamp down on the military's businesses. A possible approach to divest the military's businesses is to tackle corruption and find ways to compensate the military for lost income.

Conclusion: The divestment of the military's businesses is a crucial part of Indonesia's national reform efforts. While the immediate objectives are to reduce corruption through the ranks, erode the political power of the military and allow the civilian leadership to take greater responsibility in enhancing the pay and welfare of the military, what is more crucial is that these actions will send out clear messages that the government is committed to stamping out corruption, improving the professionalism of the military, and asserting greater control of the military. Addressing the military's businesses through tackling corruption, compensation and creation of oversight agencies will be critical not only for the success of the military's reforms, but also to the country's future.

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## INTRODUCTION

Straddling the narrow Malacca Straits and confined waterways through which 40 per cent of the world's maritime traffic and over half its oil trade passes, Indonesia assumes strategic importance second to no other country in Southeast Asia. In addition, its status as the world's largest archipelagic nation (comprising 13,000 islands) and the sheer size of its population of 212<sup>1</sup> million ensure that the growth, peace and stability of the region are closely intertwined with the country. Since the late 1960s, Indonesia's Gross Domestic Product average annual growth of 6.8 percent <sup>2</sup>, low inflation and relative political stability have contributed to the overall prosperity of the region.



Map 1: Indonesia

<sup>1</sup> Jane's Sentinel Security Assessment, 2001.

The devaluation of the Thai baht that triggered off the 1997 Asian economic crisis came as a rude awakening, as the effects rippled across the region, shattering the fast growing but fragile Indonesian economy. The economic collapse was attributed to the myriad banking, funding, and accounting problems that were endemic in the Indonesia economy. As international investors pulled out and public confidence dipped, public displeasure with the way the government mishandled the swelling crisis eventually forced the resignation of President Suharto on May 21, 1998. The end of more than three decades of iron-fisted Suharto rule precipitated a dramatic turn of events that destabilized the entire country.

Political instability was marked by the rapid succession of 3 different presidents<sup>3</sup> and cabinets in the last 3 years, severely impairing the ability of the government to govern effectively. Economic turmoil took the form of massive capital flight out of the country and a heavily devalued currency, with the Indonesian rupiah tumbling from about 6,500 rupiah to US\$1, at the start of 1998, to more than 16,000 by the middle of the same year. Social unrest also broke out in the separatist provinces of Aceh, Irian Jaya and East Timor (which separated from Indonesia in 1999), while ethnic tensions exploded throughout the archipelago, such as the victimization of the minority ethnic Chinese population, and the Christian-Muslim clashes in the Moluccas islands.

Why did this happen? The roots of the crisis are a conjunction of many factors: political, social, economic, structural, domestic and international, and it would be impossible to address all of them in this short paper. It would suffice to point out here that

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<sup>2</sup> Booth, Anne. "Development: Achievement and Weakness," in *Indonesia Beyond Suharto*, ed. Donald K. Emmerson (Asia Society, 1999), 113.

many of these problems could be attributed to Suharto's extreme centralized control and flawed policies that focused on the pursuit of economic growth at the expense of institution building and the social and political development of the country. Laksamana Sukardi, Indonesia's State Minister for Revenues and State Companies, termed Suharto's legacy a "hollow development boom"<sup>4</sup> as economic success was accompanied by destruction of political and economic infrastructure, the spread of corruption throughout government and society, and nepotism.<sup>5</sup>

In the past three decades, the Indonesian Armed Forces or TNI (Tentara Nasional Indonesia)<sup>6</sup> played a key role in supporting Suharto's regime. The relationship between Suharto and the military was one of mutual benefit. In return for supporting Suharto's policies, the military was rewarded with a large representation in government and bureaucracy, and an active social-political role in the country's affairs. With Suharto's fall, ordinary Indonesians' disenchantment with the military increasingly led to pressure for its reform. Calls for political reforms aimed at reducing the military's influence in politics had been the most vociferous, and have had some measure of success. The most visible signs have been the reduction of the military's guaranteed representation in Parliament, and the appointment of the post of the defense minister, traditionally belonging to an ex-military officer, to a civilian.

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<sup>3</sup> Suharto was succeeded by vice-President Habibie. Elections in 1999 installed Abdurrahmann Wahid as Indonesia's fourth President. His impeachment in July 2001 paved the way for his vice-president, Megawati Sukarnoputri, to take over.

<sup>4</sup> Laksamana, Sukardi, USINDO Workshop, Washington D.C. 13 March, 2001.

<sup>5</sup> According to a highly publicized estimate Time magazine (24 May 1999), Suharto's family fortune amounted to about US\$15 billion. Hill, Hal, *The Indonesian Economy in Crisis*, (Singapore: Institute of Southeast Asian Studies, 1999), 68.

<sup>6</sup> In April 1999, the police force was separated from military command and placed under the Department of Defense with the aim of reducing its military image and refocusing on police functions. The term ABRI (Angkatan Bersenjata Republik Indonesia) which collectively referred to the three armed Services (TNI) and police (POLRI) has since been dropped and the armed forces are now known as the TNI. In July 2000,

However, while there has been a lot of focus on getting the military out of politics, the future of the military's extensive business interests, by contrast, has received little attention. The phenomenon of the military's business interests is a fundamental and unique feature of the Indonesian military that cannot be underemphasized or overlooked in efforts to overhaul or reform the military. Having been "forced upon" the military out of necessity in the 1940s, the military's business interests have developed extensively in conjunction with the expanding political influence of the military, such that both factors are closely inter-related and inter-dependent. Just as business interests support the military's political power and clout in national affairs, political power helps to establish the conditions for the business interests to expand. Over time, these two aspects of the Indonesian military have become so closely coupled that reform in one must affect the other.

The purpose of this paper is three-fold. First, it will examine the military's involvement in business by tracing the origins and evolution of the military's businesses since 1945. Second, it will examine the extent and scope of the businesses and the impact that these have on Indonesia today. Finally, the paper will discuss the challenges and the prospects for change.

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police operations moved to the office of the President, with final transfer to the Department of Home Affairs in 2001.

## **CHAPTER 1**

### **A BRIEF HISTORY OF THE INDONESIAN ARMED FORCES**

This chapter does not aim to provide an exhaustive account of the rich and colorful history of the Indonesian military since its formation. What it does is to highlight the key events that led to the military's involvement in the political life of the country, and thus provide the backdrop against which the origins and evolution of the military's involvement in business can be better understood in the following chapter.

#### War for Independence (1945 - 1949)

The Indonesian Armed Forces was formed on 5 October 1945 during the war for independence against its Dutch colonial masters. The military mobilized the Indonesian people and served as their rallying point for the struggle that was to last for over 4 years. During the first three years of the war, under the leadership of General Soedirman, the military played a largely military role while President Sukarno, Indonesia's first President, and his government waged the political battle. This was to change in December 1948 when Sukarno and his government were taken prisoner by the Dutch in the capital Yogyakarta because of their refusal to leave and wage a guerilla war, as had been agreed upon earlier between Sukarno and Soedirman. Despite being critically ill, Soedirman disregarded Sukarno's orders to surrender, and provided exceptional leadership by waging a successful guerilla war against the Dutch, and at the same time, headed a military government that was later to become the basis for the current territorial command structure. His actions arguably provided the single greatest influence on the military's self-perception and signaled its first significant foray into politics. The rift between the military and the civilian government also started to appear as the military felt that Sukarno

and his government had “...betrayed the nation at a time when they were needed most.”<sup>7</sup> By the time the Dutch handed sovereignty to Indonesia in 1949, “a mindset had developed among the army that they were not merely the executive agents but shareholders of the corporate body”.<sup>8</sup>

#### Parliamentary Democracy & “Guided Democracy” (1949 - 1965)

The 1950s were a tumultuous period as Indonesia experimented with parliamentary democracy. During this period, in response to the growing disenchantment of the military with a democratic government to effectively govern the country, the military took steps to take a more assertive role in government.

The military’s confidence in the civilian leadership dipped further in 1957 as regional uprisings in Sulawesi and Sumatra broke out in response to dissatisfaction with the unequal distribution of political power and economic returns from regional exports of raw materials.<sup>9</sup> This impending crisis was only defused after Sukarno declared martial law and the military once again stepped in to “save” the nation by putting down the rebellions. At the same time, the military also grew increasingly impatient with the civilian government’s decision-making capability, which they saw as being too slow and inefficient, and therefore an impediment to national development.

In response to increasingly leftward leaning civilian politicians close to President Sukarno and the rash of regional revolts, then Army Chief of Staff General Nasution delivered a speech on 11 November 1958 at the army’s officer training college that marked

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<sup>7</sup> Lee, Terence, “The Nature and the Future of Civil-Military Relations in Indonesia,” in *Asian Survey*, Vol. XL, Issue No. 4 (July/August 2000), 694.

<sup>8</sup> Ibid, 694.

<sup>9</sup> Ibid, 694.

the genesis of the “dual function” role of the military.<sup>10</sup> Nasution called for the military to be given a role not just in cabinet, but in every state institution, and added that the military was “to be neither just a “civilian tool” as in Western countries nor a “military regime” that dominates state power”.<sup>11</sup> This approach earned the label the “Middle Way”. The result was the institutionalization of a 1956 army doctrine that declared the armed forces as both a “military force” and a “social-political force” in cognizance of its embryonic role in the country’s independence. As a social-political force, the military’s activities covered “the ideological, political, social, economic, cultural and religious fields.”<sup>12</sup>

In 1959, Indonesia transitioned to a period known as “Guided Democracy” after the military supported Sukarno’s decision to liquidate Parliament and adopt a style of government that concentrated power in the President.<sup>13</sup> The military’s support for Sukarno, coupled with the implementation of the dual-function doctrine led to the installation of increased numbers of active and retired military personnel in the political (assembly, parliament), legislative (provincial and district), administrative (executive and staff positions in the provinces and districts) and economic functions of the government. However, Sukarno’s government, comprising fragile coalitions, remained weak and came under constant pressure from the Communist Party of Indonesia (Partai Komunis Indonesia or PKI). Against this backdrop of growing communist influence, the military became increasingly alarmed at the country’s political direction.

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<sup>10</sup> Vatikiotis, Michael R. J., *Indonesian Politics Under Suharto*. (Routledge, 1993), 69.

<sup>11</sup> Lee, 695.

<sup>12</sup> Crouch, Harold, *The Army and Politics in Indonesia*, (Cornell University Press, 1978).

<sup>13</sup> Agus Widjojo and Bambang Harymurti, *Understanding Political Change and The Role of The Military in Post Suharto Indonesia*, (Singapore: Institute of Southeast Asian Studies, Feb 2000).

### Suharto's New Order (1965 – 1998)

An attempted coup by the PKI on 30 September 1965, which took the lives of seven high-ranking Army generals, gave then Major General Suharto, commander of the country's special forces *Kostrad*, the chance to outlaw the PKI, seize power and eventually force Sukarno to step down.<sup>14</sup> Declaring a period of New Order, he restricted political parties to mainly three entities that were permitted to contest elections,<sup>15</sup> and quelled ethnic and separatist unrests in the archipelago through the use of oppressive military force.<sup>16</sup> Having risen to power on the back of the military, the military was his obvious instrument to exercise control of the country.

In 1966, the *dwifungsi* (dual function) doctrine was endorsed.<sup>17</sup> According to this doctrine, the armed forces has two closely related roles: to defend the country not only from conventional military threats originating abroad, but also from domestic dangers of any kind, military, political, socioeconomic, cultural or ideological. The formalization of the military's dual role legitimized its defense and social-political functions. This served to further consolidate Suharto's and the military's power.

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<sup>14</sup> There are actually two conflicting versions of events surrounding the attempted coup. The official Army version insists that the PKI was behind the coup attempt, while the communist version asserts that the coup was an internal matter of the Army, which it exploited to destroy the PKI.

<sup>15</sup> The three entities were: the state party, called Functional Groups (*Golongan Karya*, or Golkar); the Development Unity Party (*Partai Persatuan Pembangunan*, or PPP); and the Indonesian Democracy Party (*Partai Demokrasi Indonesia*, or PDI).

<sup>16</sup> In the first 15 years of Suharto's rule, nearly all provinces were headed by governors with military background. Many key diplomatic posts and directors of state corporations were held by military officers. During the 1980s and 1990s, the number of such appointments declined sharply, but military officers (retired and active) still made up about half of the provincial governors and around 40% of *bupati* (regent). Altogether, about 6,000 officers were serving in civilian positions in the late 1990s. Crouch, Harold, "Wiranto and Habibie: Military-Civilian Relations Since May 1998" in *Reformasi: Crisis and Change in Indonesia*, ed. Arief Budiman, Barbara Hatley and others, (Victoria: Monash Asia Institute, 1999), 127-148.

<sup>17</sup> Alagappa, Muthiah, "The Military: Professionalism and the Developmental Role" in *Soldiers and Stability in Southeast Asia*, eds. Soedjati Djiwandono and Yong Mun Cheong, (Singapore: Institute of Southeast Asia Studies, 1988), 25.

By the late 1970s, about half the cabinet and over two-thirds of the regional governorships were military appointees (see Table 1). The pervasiveness of the military

|                 | Period    | No. of People | Military Status      | Percentage of Total |
|-----------------|-----------|---------------|----------------------|---------------------|
| Cabinet members | 1969-1973 | 8             | All active           | 30                  |
|                 | 1974-1978 | 6             | All active           | 23                  |
|                 | 1979-1983 | 15            | 14 active, 1 retired | 41                  |
|                 | 1984-1988 | 17            | 4 active, 13 retired | 10                  |
|                 | 1989-1993 | 14            | 4 active, 10 retired | 10                  |
|                 | 1994-1998 | 10            | 4 active, 6 retired  | 10                  |
| Governors       | 1969-1973 | 19            |                      | 73                  |
|                 | 1974-1978 | 20            |                      | 77                  |
|                 | 1979-1983 | 16            |                      | 59                  |
|                 | 1984-1988 | 14            |                      | 52                  |
|                 | 1989-1993 | 12            |                      | 44                  |

Table 1 : Proportion of Military Members in Development Cabinets and Governorships<sup>18</sup>

was further magnified by the fact that 56 percent of district officers, 78 percent of director-generals and 84 per cent of ministerial secretaries were military appointees. Even in the diplomatic service, almost half the country's ambassadors in 1977 were from the military.<sup>19</sup>

One of the most important political developments during the New Order was the consolidation in 1969 of hundreds of disparate functional groups, including civil servants, and their transformation into a single government-sponsored political entity: Golkar. Golkar had its origins during "Guided Democracy" when both Sukarno and the military decided to mobilize under military auspices all of the noncommunist organizations that had been given representation by President Sukarno in the national and regional legislatures in response to the growing communist influence, as well as provide "an alternative to the

<sup>18</sup> Kristiadi, J., "Indonesia: Redefining Military Professionalism," in *Military Professionalism in Asia: Conceptual and Empirical Perspectives*, ed. Muthiah Alagappa, (Honolulu: East-West Center, 2001), 101.

seemingly insurmountable divisiveness of the political parties”.<sup>20</sup> As such, the military also became the most powerful political force next to the President.

#### Post New Order (1998 onwards)

After Suharto’s fall in May 1998, major upheaval in the political landscape occurred as more than 60 political parties were formed within a span of 3 months.<sup>21</sup> Although the military had been quietly aware of the need to prepare itself for a post-Suharto Indonesia, the rapid turn of events in 1998 took it by surprise. Realizing the need to adjust itself to the political realities and demands of the new era, the military issued a document entitled *ABRI in the 21<sup>st</sup> Century* during its 53<sup>rd</sup> anniversary in October 1998. In it, rather than denying past abuses, the military apologized for them, and also acknowledged that it had “exceeded its dual-function role” during Suharto’s rule.<sup>22</sup> It also articulated a new paradigm based on four principles<sup>23</sup>, the essence of which was that the military will relinquish some of its political power, reduce its social-political role and accept greater civilian control. This was a significant shift for the military. Nevertheless, as Agus Widjojo, the military’s Chief of Territorial Affairs, stated, the military remains concerned about the “reality of the Indonesian state and nation” and the “unity of the republic.”<sup>24</sup>

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<sup>19</sup> Vatikostis, 71.

<sup>20</sup> Pabottingi, Mochtar, "Indonesia: Historicizing the New Order's Legitimacy Dilemma," in *Political Legitimacy in Southeast Asia (The Quest for Moral Authority)*, ed. Muthiah Alagappa, (Stanford University Press, 1995), 248.

<sup>21</sup> Kristiadi, J., “The Future Role of ABRI in Politics,” in *Post-Suharto Indonesia: Renewal or Chaos*, ed. Geoff Forrester, (Palgrave, 1999).

<sup>22</sup> Lee, 699.

<sup>23</sup> The 4 principles are that the military will (1) no longer be in the forefront of politics; (2) influence the political process indirectly; (3) shift its sociopolitical position from that of occupier to that of influence; (4) concede some of its sociopolitical functions to nonmilitary partners. Pereira, Derwin, “ABRI Concedes It Was Tool Of Suharto”, *Straits Times*, 7 October, 1998. Imanuddin, “1998: A Year of Questions and Turmoil for ABRI,” *Jakarta Post*, December 31, 1998.

<sup>24</sup> Widjojo, Agus, Seminar on Trends in Indonesia, (Singapore: Institute of Southeast Asian Studies, 7 October 1999).

## CHAPTER 2

### ORIGINS AND EVOLUTION OF MILITARY BUSINESSES

The military's involvement in business dates back to the war for independence, when many Army and militia units were forced to look for means to sustain and finance themselves. While revenues were raised by milking local business activities or by imposing tolls and taxes in operational areas,<sup>25</sup> business ties, particularly those between Indonesian officers and ethnic Indonesian Chinese businessmen or *cukong*<sup>26</sup> were established.

After the war, these ties were suspended or dissolved as troops were demobilized, and units and senior officers redeployed. However, faced with ongoing insurgencies and drastically reduced budgets after 1952, regional military commanders were forced to revert to their old business ties to help finance personnel and other operating costs. However, it was not until the declaration of martial law in 1957 and the subsequent nationalist furor that led to the seizure of Dutch businesses that the military's involvement in the economy expanded. With military men put into positions of considerable power, especially in the outer islands where countervailing civilian forces were relatively weak, the military began running large-scale commercial enterprises in the profitable oil, mining, agribusiness and banking sectors, often with the help of Chinese businessmen. These renewed relationships were symbiotic as they provided the ethnic Chinese with access to business opportunities and protection from a resentful and Muslim-dominated society, which in turn generated funds for the military to supplement their meager official budgets and individual needs.

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<sup>25</sup> Vatikostis, 71.

<sup>26</sup> *Cukong* is Chinese for Master or Lord. The master of capital was the Chinese and the master of politics was the Indonesian, almost always military men. The most capital generating *cukong* relation was between

However, towards the end of Sukarno's rule in the early to mid 1960s, many of the businesses that the military looked after, such as plantations, sugar mills and hotels went into rapid decline along with the rest of the national economy.<sup>27</sup> This was due to unsound government economic policies that had led to high inflation, financial chaos and widespread poverty.

### Military Business in the New Order

Military businesses were revitalized in the New Order due to a confluence of factors. In addition to its rising political influence in a military-dominated Suharto government, the appointment of more military personnel into government and bureaucracy, and the confiscation of the property and assets of the "Old Order", the military capitalized on the opportunities and a pervasive territorial command structure that stretched throughout the country to ensure that the local bureaucracy worked in their favor to further expand its business empire-building in timber extraction, fisheries, plantations and other areas. During this period, the original motivation of the military's businesses, which was based on pragmatic considerations of insufficient government budget and funding, gradually became overshadowed by ideological and personal fiscal motivations.

Suharto and senior military officers felt that the expansion of commercial opportunities for the military was vital for the military's role as a stabilizer. Having inherited a chaotic administration and a declining economy, the new government felt that it had little prospect in raising adequate funds for the military through conventional means. Fully aware of the failure of the governments during Sukarno's era to adequately provide for the economic well-being of the military had led to discontent and open rebellion, the

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President Suharto and Liem Sioe Liong (also known as Salim), owner of one of the world's largest conglomerates. Lowry, 134.

senior military leadership decided to permit the continuation of well-established military business practices. Furthermore, Suharto's own active and profitable involvement in the business system in when he was based in Central Java probably convinced him that the military was well placed to provide the country with a much-needed economic boost.

The ability of the military to extend its business interests rapidly during the New Order was, in part, also due to the ideological stress on and promise of economic development. In contrast with the Sukarno government's emphasis on the "1945 Revolution" and the "struggle" against "imperialism", Suharto offered "stabilization" and "development". The ideological stress was further reflected in Suharto's cabinet being termed as the "Development" cabinet, in contrast with Sukarno's "Dwikora" cabinet connoting struggle against Malaysia. The military claimed not only the role of "stabilizer" but also that of "dynamizer", and perceived that "its own mission required it to play an important role in the economy". Presenting itself as a national force that identified with the interests of the people, the military believed that its involvement in the country's political life would bring about the political stability that was needed for economic development.<sup>28</sup>

This ideological stress was further demonstrated by the fact that even when the military assumed a central powerful position in the New Order, it did not use its position nor the improving economic situation to rectify its long-standing budget shortfalls. The proportion of the national budget allocated to defense and security had continually declined, from 27% in 1969 to 7% in the 1990s (see Figure 1). One of the reasons for its

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<sup>27</sup> Lowry, 134.

<sup>28</sup> Crouch, Harold, *The Army and Politics in Indonesia*, (Cornell University, 1978), 273, 274.

reluctance to press for a larger share of the budget was due to its ideological commitment to give priority to the country's economic recovery and development.

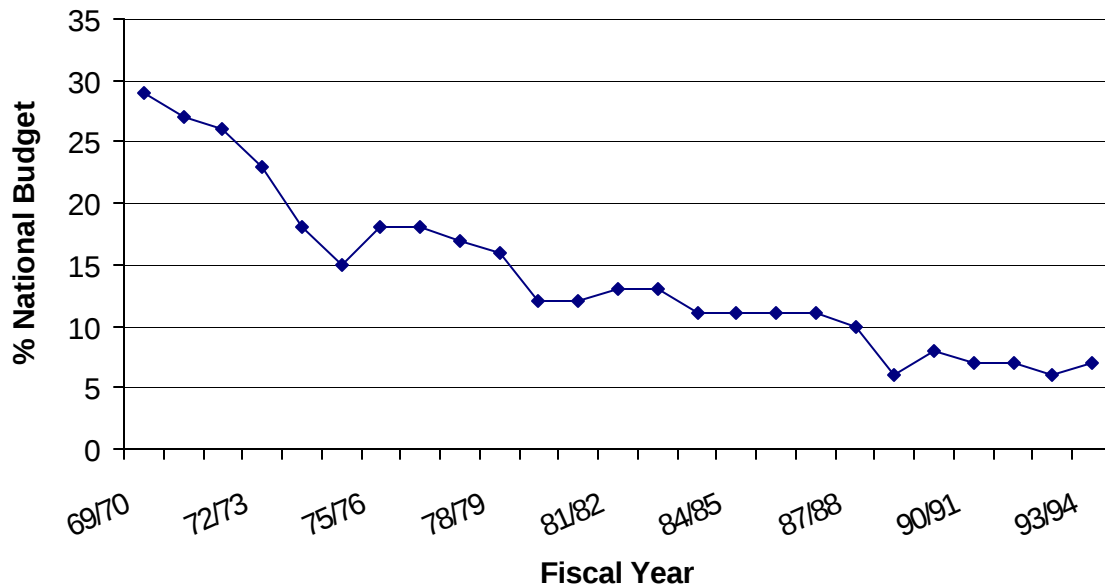


Figure 1: Proportion of National Budget Allocated to Defense and Security

However, a more likely reason was that by the mid 1960s, the military had a well-developed “unofficial” system of financing military operations, providing for soldiers’ welfare and meeting procurement needs.<sup>29</sup> By retaining the system of “unconventional” financing, the military-dominated government was able to create the impression that military expenditure was being held back in the interests of the country’s economic development. In fact, the government’s defense budget allocation in the 1960s only covered about a third to a half of the actual expenditure - a fact that was never officially stated.<sup>30</sup>

<sup>29</sup> Kristiadi, J., “The Armed Forces” in *Indonesia: The Challenge of Change*, (New York: St Martin’s Press, 1999).

<sup>30</sup> Crouch in *The Army and Politics in Indonesia*, 274.

In the regions, local commanders exercised great autonomy in raising funds for their own needs, such that “the range of activities undertaken is limited only by the imagination of the military commanders.”<sup>31</sup> In Sumatra and other export-producing areas, army-protected smuggling was an important activity. Other activities ranged from the use of military ships and vehicles for transport of passengers and freight, involvement in a variety of ventures such as rice milling, building construction and cinemas. It was also common for units and their associated foundations to establish their own banks, such as Bank Bukit Barisan in Medan and the Bank Brawijaya in Surabaya. One of the most imaginative initiatives was undertaken by a police foundation, which presented bullfighting in Jakarta in 1969.<sup>32</sup>

The oil boom of the 1970s increased the flow of money into military enterprises through the expansion of projects undertaken by Pertamina, and other businesses with military connections involved, such as the construction of buildings, roads and ports. Senior officers took advantage of their considerable political power and influence over the granting of licenses, permits and bank loans, to establish lucrative enterprises and enter joint ventures with experienced businessmen, particularly the Chinese.

Many military officers were appointed as directors into many large state enterprises, such as the state oil company, Pertamina. Elsewhere, powerful state regulatory bodies such as the National Logistics Board (Bulog), and government-owned companies such as PT Berdikari, had the mission of channeling money to a cash-strapped military.<sup>33</sup> It was apparent that this technique was also Suharto's method of rewarding and paying off those who had been loyal to him and "buying allegiance". In fact, many of them had

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<sup>31</sup> Ibid, 284.

<sup>32</sup> Ibid, 284.

already been involved in business through the Financial and Economic (Finnek) sections that the military had established in the 1950s to run its smuggling and other business interests at the provincial level. Now, these “financial generals” were given access to lucrative export and import monopolies, forestry concessions and Indonesia’s black gold: the oil industry. The strength of the relationship between the executive and military interests ensured that it took relatively little time for the military to achieve a dominant position in the economy. Ibnu Sutowo, a military colleague of Suharto, was appointed head of a new state oil company, North Sumatra Oil Exploration, in 1957. By 1968, he was head of the Pertamina company, under which all state oil companies had been incorporated. By the height of the oil boom in the early 1970s, Pertamina had become not only the major source of funding for the military, it accounted through tax payments for almost 40 per cent of the domestic revenue.<sup>34</sup>

Former Defence Minister Juwono Sudarsono noted that the turning point in military attitudes came in the early 1980s as Indonesia rushed towards economic development and modernization. “Old values binding the military to civilians since independence gradually faded as “consumerism” permeated the lifestyles of senior officers, promoting patron-client relationships and an emphasis on money and protectionism”.<sup>35</sup>

However, the rise of the military’s influence in business was checked in the mid to late 1970s as Suharto started to distance himself from military businesses and drew his *cukongs* with him.<sup>36</sup> As *cukongs* were normally linked to individual officers rather than to particular points in the organization, they would move together with the individual

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<sup>33</sup> Ibid, 275.

<sup>34</sup> Vatikiotis, 72.

<sup>35</sup> McBeth, John, “Hard Hearts, Bitter Minds”, *Far Eastern Economic Review*, Aug 30, 2001.

<sup>36</sup> Lowry, 135.

officers. The departure of senior military officers meant that their business interests and connections also moved with them, with the result that the military had less access to capital and the know-how of the *cukongs*. At the same time, Pertamina, Bulog and PT Berdikari reduced their contributions to the military as technocrats battled to regulate the state's finances. The result was the hollowing out and decline of military businesses. Nevertheless, the relationships in the provinces between smaller Chinese businesses and the military continued to be important due to the "smaller" *cukongs*' lack of access to capital and more localized business interests.

### The Situation Today

Estimates on the exact size and extent of the military's businesses vary widely as there are no central records and even those that exist are not made available to the public.<sup>37</sup> There are about 50 military-owned businesses and 7 foundations associated with each of the armed services and major commands.<sup>38</sup> However, according to former Defense Minister, Juwono Sudarsono, there are more than 300 companies controlled by the military foundations and cooperatives.<sup>39</sup>

The value of the military's business interests are even more difficult to estimate. The government began the first-ever audit of the military's businesses in June 2000 and has already uncovered many irregularities, especially in the areas of bookkeeping and procurement.<sup>40</sup> Nevertheless, estimates of the military's corporate wealth have placed it at more than US\$8 billion, and this excludes the tens of thousands of cooperatives across

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<sup>37</sup> Lowry, 142.

<sup>38</sup> The Indonesian Armed Forces headquarters (distinct from the Ministry of Defense) owns two foundations; the Army, Navy, and Air Force each own one; the Army Strategic Reserve owns one; and the Army Special Forces owns one.

<sup>39</sup> Current Data on the Indonesian Military Elite January 1, 1999 - January 31, 2001, *Indonesia*, April 2001, 136.

<sup>40</sup> Sinaga, Shinta NM, "Defense Department Audit Reveals Many Irregularities," *Detikworld*, June 24, 2000.

the country and the security and debt-collection services stretching from small corner stores to big companies.<sup>41</sup>

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<sup>41</sup> McCulloch, Leslie, “Business as Usual”, *Inside Indonesia*, No.63, Jul-Sep 2000.

## Network of the Military's Businesses

The military's business interests may be grouped into four main categories: cooperatives, which focus mainly on troop welfare; unit business; businesses run by non-profit charitable foundations, known as *yayasan*; and 'influence and facilitation', which may take place outside a formal business structure (see Figure 1).<sup>42</sup>

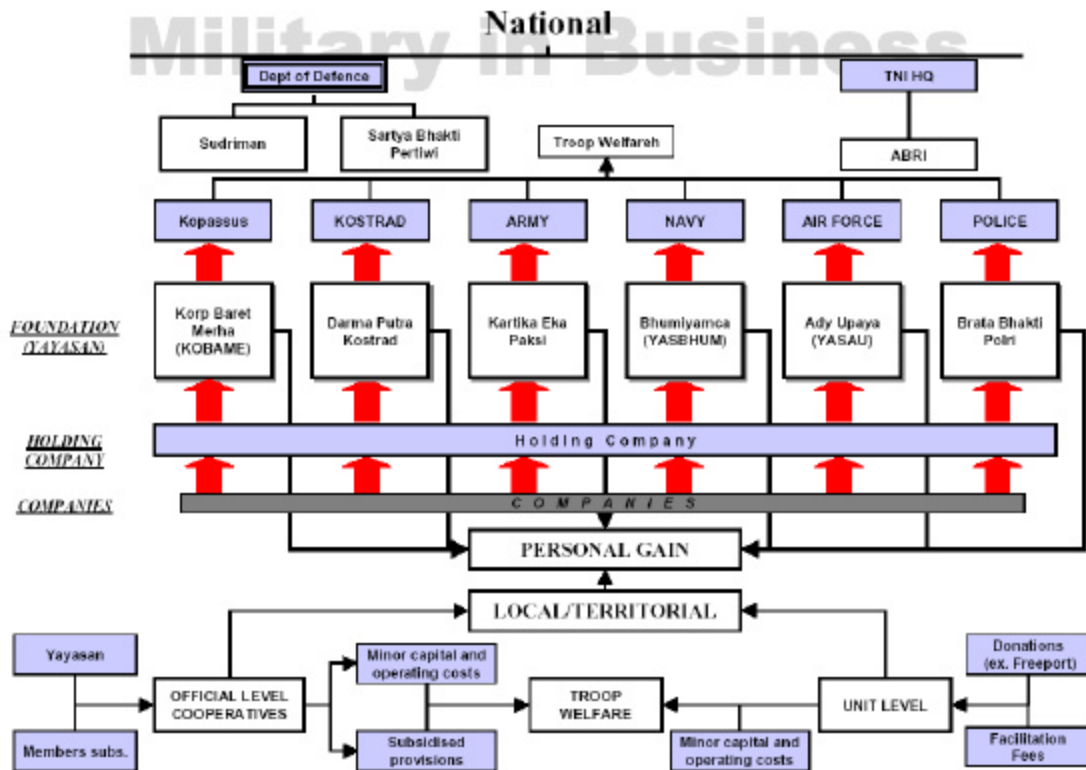


Figure 2: Structure of Indonesia's Military Businesses<sup>43</sup>

Cooperatives. Cooperatives operate retail outlets that provide basic goods to members at low cost, not unlike the U.S. military's Post Exchanges, and to finance minor capital, operating and personnel costs not covered by the defense budget. The cooperatives have two sources of capital: one, from member subscription, and the other (and more important source) from business enterprises often run through holding companies known

<sup>42</sup> Lowry, 137.

<sup>43</sup> Extracted from [www.bicc.de/budget/events/milbus/confpapers/mcculloch\\_chart.pdf](http://www.bicc.de/budget/events/milbus/confpapers/mcculloch_chart.pdf)

as *yayasan*. The military's access to land is an economic resource commonly used by leasing out to sharecroppers or to business operators to establish and run golf courses, recreational centers, hotels, and other businesses. Other cooperative-owned companies may also be involved in a wide variety of domestic enterprises such as transport, educational institutions, hotels and restaurants.<sup>44</sup>

Unit Business. Unit business involves the use of a unit's assets for either the personal gain of the officers involved or in support of cooperative activities or both. In addition to the rental of unit land, and sale of military items such as fuel and spare parts, one of the more common practices is the use of military ships, aircraft or vehicles to transport people and materiel for a fee.

Yayasan. Not all *yayasan* are subordinate to cooperatives. The independent ones are normally formed by the senior commands at the national and provincial levels. Such *yayasan* usually obtain funding from their own businesses and contributions from the business community. To give an indication of the size of such foundations, the Army headquarters's *yayasan* and one of the biggest, YKEP (Yayasan Kartika Eka Paksi), was estimated in 1994 to rank 138<sup>th</sup> among the top 200 conglomerates in Indonesia, with 47 subsidiaries, a capital base of Rp240billion (US\$114million) and an annual turnover of Rp110 billion (US\$52million). The other services have similar foundations and are also reported to have extensive holdings. The YKEP reportedly contributed US\$11.5 million in 1993, mainly for the repair and maintenance of barracks and housing. However, the size and distribution of most *yayasan* are unknown given their tax-exempt status and the absence of public accounting, and it is likely that the reported capital bases for the foundations are understated.

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<sup>44</sup> Ibid, 138, 139.

Influence and Facilitation. The last form of the military's business interest - 'influence and facilitation' - involves officers or military enterprises receiving financial rewards for influencing events in favor of other businesses, such as winning contracts or gaining access to land or other resources on favorable terms.<sup>45</sup> Many such businesses are of Chinese origin, as the ethnic Indonesian Chinese often find it prudent to keep the military on their side because as a minority group, they are proportionally more successful in business than other Indonesians, but also more politically more vulnerable. The income from 'facilitation' is not generally channeled through cooperatives but instead goes into a discretionary fund, or in the case of individual officers, into their own pockets. The relationship with the ethnic Chinese illustrates a long-standing pattern of "ethno-economic bargaining".<sup>46</sup>

In summary, two key features of the military's business interests stand out: the evolution of the underlying motivations, and the extensive pattern of mutually co-operative business relationships developed between ethnic Chinese businessmen and military officers, which became more entrenched during the New Order.

Initially motivated by pragmatic considerations, military businesses gradually came to acquire important ideological significance in line with its *dwifungsi* doctrine. Over time, they came to offer strong fiscal appeal and was perceived as an avenue for personal advancement and wealth.<sup>47</sup> While the first two motivations were sufficiently justified by the poor state of the country's economy up to the 1960s, the fast improving economic conditions of the 1970s through to the 1990s presented opportunities for the military to

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<sup>45</sup> Lowry, 141.

<sup>46</sup> Liddle, 51.

<sup>47</sup> Scobell, Andrew, *Going Out of Business: Divesting the Commercial Interests of Asia's Socialist Soldiers*, (East-West Center Occasional Papers, Politics and Security Series, No. 3, Jan 2000), 6.

gradually give up its hold on its businesses. Furthermore, it was also clear that more qualified civilians, who were better educated and trained, would be more competent and efficient in managing the country's economic affairs and assets. However, the military's reluctance to free itself of its economic "obligations" strongly suggest that the personal benefits, especially for the senior military leadership, had become too attractive to give up.

## CHAPTER 3

### IMPACT OF MILITARY BUSINESSES

*“The main objective of ABRI business - the cooperatives, the foundations, the corporations - is to help soldiers. To help the families of our soldiers with education and by providing basic human needs.”*

Lt Gen. Susilo Bambang Yudhoyono<sup>48</sup>

The revenue from the military’s involvement in business has brought about some tangible and visible social and economic benefits for the military as well as the community. For example, YKEP runs medical clinics and hospitals. In addition to having built 13,700 houses and several schools, including Ahmad Yani University in Bandung, the foundation also grants high school and college scholarships to the children of military personnel and veterans, and contributes to bonuses given to the troops during Christmas and Lebaran, the end of the Muslim fasting month. In the 1990s, the foundation is estimated to have spent US\$1.5 million on what it terms “army welfare”.

Before the fall of Suharto, the institutional stability and cohesiveness associated with the military provides both external investors, interested in a long-term stake in Indonesia, and the politically-vulnerable ethnic Chinese Indonesian population with a stable business platform. As such, business partnerships with the military were seen as a sound investment strategy.

However, the negative impact of corruption, reduced combat effectiveness, the weakening of civilian control, and disruption to the real economy and reform efforts stand out as the key problems that far outweigh the benefits that accrue from the military’s business interests.

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<sup>48</sup> Yudhoyono, Susilo Bambang, “What Role for the Military,” interview by Asiaweek in 3 July, 1998.

*“ABRI’s involvement [in business] is a brake on economic and political reform”*

Bob Lowry

The contagious effects of corruption stand out as the most debilitating impact, permeating all levels of the military. While the objective of the military’s businesses to ensure a steady flow of funds into the military’s coffers without causing disruption in the economy is not entirely wrong, the key problem lies with the methods, which had been largely left to the discretion of the officers involved. Although officers were expected to avoid “excesses” which would bring disrepute to the military, the senior leadership did not object to part of the proceeds being channeled to private accounts. As the majority of the senior leadership are also involved in and profit from such dubious methods of financing, there is general consensus and self-delusional belief throughout the ranks that the money siphoned off to private accounts and the petty corruption of the soldiers were not large enough to have any significant impact on the economy.

For example, an estimated 65 percent of the revenue from military-owned businesses is siphoned off to private accounts, most probably to senior officers.<sup>49</sup> The present Army Chief of Staff, General Tyasno Sudarto, stands accused of coordinating the largest counterfeiting operation in Indonesia’s history, while many other officers are believed to be involved in illegal activities and innumerable questionable businesses independent of their military duties.<sup>50</sup>

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<sup>49</sup> Weiss, Stanley A., “Indonesia: The Military Can Shape Up if Washington Helps,” *International Herald Tribune*, August 20, 2001.

<sup>50</sup> Bhakti, Ikrar Nusa, “Government Must Act on Military Businesses,” interview with *The Jakarta Post*, May 20, 2000.

Legitimate business activities have often served as a front for illegal business dealings such as unlawful logging, animal poaching, fuel smuggling and marijuana production, and the top military leadership is known to actively support such activities. Another example is the state-run Pertamina oil company providing the army with facilities to help protect Aceh's gas fields, but the soldiers are involved in everything from protection rackets and marijuana smuggling to illegal logging and contract fixing. All this helps to explain why troop levels remained higher than necessary after the separatists were crushed in the early 1990s.<sup>51</sup>

“The military's local financing dealings not only served to keep troops well-fed and loyal, but padded the pockets of the commander and those who assisted him in his dealings. The fact that many of the most lucrative arrangements involved smuggling from the export-producing border areas only increased the tendency of military men to draw the conclusion that soldiers need not take the law too seriously and did not provide a particular example of honesty. There thus began, at quite an early stage, the process of personal corruption and entanglement with civilian concerns that has plagued the military ever since.”<sup>52</sup>

Ruth McVey

Another negative impact of the military's preoccupation with preserving and maintaining its business interests and access to funds is that it reduces its combat effectiveness by degrading combat readiness and creating factionalism within the military.

While the degradation of the military's combat capabilities and readiness cannot be easily measured, it is not difficult to postulate the level of military inefficiency that results from troops effectively having 2 occupations – soldiering and seeking to augment their base incomes. For example, the status of Aceh, one of Indonesia's troubled provinces, as a Military Operations Area from 1990 to 1998 created opportunities for the emergence of a

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<sup>51</sup> McBeth.

semi-official mafia with close links to the military and to *Kopassus*, the elite special forces, in particular. As *Kopassus* became firmly established in Aceh in the mid 1990s, stories abounded that members of the units stationed there were able to enrich themselves by serving as enforcers, debt collectors, security guards and extortionists.<sup>53</sup> In 1997, a local human rights organization reported the case of several *Kopassus* soldiers who were apparently hired by a local government official to “resolve” a private dispute.<sup>54</sup>

Hasnan Habib, a retired general and former ambassador to the US pointed out that “the [widening] gap between the haves [the officers] and the have-nots [the soldiers] has become a problem.”<sup>55</sup> Even amongst the officer corps, there are differences as those in the elite *Kopassus* and *Kostrad* forces (the Army Strategic Command) have historically been better endowed than the rest of the forces. Inequitable profit distribution from the military’s business interests may thus not only intensify intra-elite competition for power and influence, and hence fuel factionalism within the military, but the jealousy and resentment that build up as a result of the widening income gap will also have an impact on weakening morale. Furthermore, in an environment of tight budgets, “internal schisms and rivalries [come] to the surface in an open open, bitter intra-army war for positions of power [and claims to the pots of gold].”<sup>56</sup>

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<sup>52</sup> McVey, Ruth, “The Post-Revolutionary Transformation of the Indonesian Army”, *Indonesia (Ithaca)*, No.11 (April), 1971, 152-153.

<sup>53</sup> Alagappa, Muthiah, ed. *Coercion and Governance: The Declining Political Role of the Military in Asia*, (Stanford University Press, August 2001), 242.

<sup>54</sup> “In 1997, a local human rights organization reported the case of a man named Abdul Hamid bin Itam, who had been detained by three *Kopassus* soldiers late at night on September 14, 1996, in the town of Sigli. After being taken to the local *Kopassus* post, Abdul Hamid had been badly beaten and then shot in the head; his mutilated body was found a few days later about 200 kilometers from Sigli. Although at first this appeared to be a standard summary execution of an Aceh Merdeka suspect, it was later discovered that the dead man had been detained in connection with a private dispute he had had with a local government official in Pidie. The official had evidently hired the *Kopassus* soldiers to “resolve” the dispute.” Ibid, 242,243.

<sup>55</sup> McCawley, Tom, “Bullets and Bottomlines,” in *Asiaweek*, 5 Feb, 1999.

<sup>56</sup> Current Data on the Indonesian Military Elite January 1, 1999 - January 31, 2001, *Indonesia*, April 2001, 136.

With only an estimated 25 percent of the military's overall expenditure coming from the nation's small defense budget, control of the military through budgetary means by the civilian government will be difficult.<sup>57</sup> Without substantially increased government funding for the military, the government's policy objectives will be distorted by the demands of a diverse band of paymasters. For example, troops stationed in the troubled Moluccas islands to prevent ethnic clashes between Christians and Muslims are not paid by government but by the local people. The result is that units tend to be either Christian or Muslim, and are stationed in a village of the same religion. Thus, instead of being objective keepers of the peace, they become beholden to their paymasters.<sup>58</sup> In such an extortionist environment, as long as the security forces are self-financed they have no real incentive to work toward a stable civil society that would not require military or police protection.

Financial independence of the military and the lack of transparency of its other sources of funding allow the military to free itself from domestic criticism and foreign pressure by creating the impression that military expenditure was less than it really was. Proceeds from businesses could further enhance the power of the military leaders, as they would be able to distribute rewards according to their own political ambitions and inclinations without being subject to bureaucratic control and international pressure.

While military businesses have arguably contributed to the rapid economic progress in the 1970s to the 1990s, there are fundamental weaknesses in the military's business strategy that disrupt not only the real economy, but also the country's economic reform efforts. Instead of being able to plough profits back into their businesses, the

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<sup>57</sup> Indonesia: Next Steps in Military Reform, 11 Oct 2001, International Crisis Group Report.

<sup>58</sup> Crouch, Harold, USINDO Workshop, Washington DC, 29 November, 2001.

practice of paying hefty dividends back to the military stunts and restricts the growth potential for both state owned enterprises and ethnic Chinese businesses. For instance, until 1994, a company linked to General Benny Murdani, the former ABRI commander who was a key figure in the 1975 invasion of East Timor controlled coffee production, the major cash crop of the province. When controls were lifted, farm profits increased 350%.<sup>59</sup> The significant loss in government revenues as a result of the military's businesses, much of whose profits are siphoned off into individual bank accounts, must be of concern to the government. Such individual profit-seeking also erodes the defense budget and is a disincentive to the introduction of modern systems of management and accountability, which are key tools in the reform of the economy.

Ironically, the military, instead of being the guardian of security and stability in Indonesia, has turned into a source of internal disturbances. For example, after the economic crisis hit the country, the army could not support its own men, with the result that hundreds of soldiers were arrested on various criminal charges. The army high command lacked the authority to control much of what was happening on the ground and suffered from a "dual command structure" as individual generals with their own sources of money funded their personal campaigns, hiring "rogue elements" and "deserters" and causing widespread violence, provocations and killings.<sup>60</sup>

For example, in Aceh, troops support themselves through their protection rackets, illegal logging, the marijuana trade and other sources. Thus rather than negotiating

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<sup>59</sup> Sidwell, Thomas E., *The Indonesian Military: Dwifungsi and Territorial Operations*, Fort Leavenworth, 1995.

<sup>60</sup> Current Data on the Indonesian Military Elite January 1, 1999 - January 31, 2001, *Indonesia*, April 2001, 136.

solutions to separatism, they fight in order to have an excuse to stay (incite and prolong internal conflicts to assure its continued role and maintain the practice of extortion) <sup>61</sup>

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<sup>61</sup> Crouch, Harold, USINDO Open Forum, Washington D.C., 29 November, 2001.

## CHAPTER 4

### CHALLENGES AND PROSPECTS FOR CHANGE

In the short term, some of the biggest challenges that will delay efforts to address the issue of the military's businesses are the current economic downturn, the brewing internal security problems, particularly in Aceh and Irian Jaya, competing priorities, and the lack of resolve by both the military leadership and government to clamp down on the military's businesses.

In the absence of a return of foreign investments into Indonesia, the government will find it difficult to increase the defense budget. With a total debt burden of US\$140 billion, which is evenly split between domestic and international debts, the high interest payments will take a huge bite out of the budget.<sup>62</sup> The picture is even more grim when one considers that the size of the official military budget for 2002 is not even one-third of the pre-crisis levels in 1996 and 1997 (see Table 2).

| 1996                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 | 1997                    | 1998                     | 1999                    | 2000                    | 2001                         | 2002                         |
|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------|--------------------------|-------------------------|-------------------------|------------------------------|------------------------------|
| \$4.7bil <sup>(2)</sup>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              | \$4.8bil <sup>(2)</sup> | \$0.95bil <sup>(3)</sup> | \$1.5bil <sup>(3)</sup> | \$1.2bil <sup>(3)</sup> | \$0.837bil <sup>(3)(4)</sup> | \$1.445bil <sup>(3)(5)</sup> |
| <b>Notes (All figures in US\$)</b><br>1. The official budget is believed to represent only about one-third of actual military expenditures; the remainder comes from the extensive military business empire and other off-budget funding sources.<br>2. Including expenditure on procurement and the defense industry.<br>3. Excluding expenditure on procurement and the defense industry.<br>4. Estimated, based on a nine-month adjusted fiscal year.<br>5. Estimated expenditure for both military operations and equipment purchases, but not yet appropriated. |                         |                          |                         |                         |                              |                              |

Table 2: Indonesia's Official Defense Budget (extracted from Jane's Sentinel Security Assessment)

According to internal research carried out by the military in July 1999, the lowest-ranking soldier only took home 590,000 rupiah per month (or US\$74 at the prevailing exchange rate of 8,000 rupiah per US\$1). Contrast this with the Indonesian army's survey

<sup>62</sup> Kuntjoro-Jakti, Dorodjatun, Briefing at USINDO, Washington D.C., 5 February, 2002.

finding that the minimum subsistence for the same soldier should be 1,017,000 rupiah (US\$127 at the same exchange rate), the current take-home pay is grossly insufficient. The survey showed that the problem was worse if the soldier were married as the pay only met 41 percent of his subsistence needs, or even worse at 29 percent for a corporal if he has a wife and two children.<sup>63</sup> It is therefore no wonder that soldiers have little choice but to resort to other means to supplement their meager incomes. At the “higher end”, these could include offering personal protection, hiring out military vehicles and ships for commercial purposes, and leasing military land for golf courses. At the “lower end”, these could be illegal logging or mining, smuggling, gambling, drugs, prostitution, and extortion. Such side jobs and activities can only drastically damage the professionalism and image of the military.

While Indonesia is in no immediate threat of breaking up, the internal security problems resulting from secessionist movements and ethnic clashes remain and need to be closely monitored. The present civilian and military leadership have already demonstrated their willingness to delay further reform of the military until the threats to Indonesia’s integrity are substantially reduced. What this means is that military reforms such as the divestment of businesses which will have a direct impact on the capability of the military to respond to such threats will take a back seat. In addition, the military has also insisted that effective civilian institutions be in place before it withdraws its territorial structure.<sup>64</sup>

The concerns of the military are understandable. A sudden withdrawal from its existing commercial interests, without assurance of a corresponding increase in the defense budget to cover the present government funding shortfalls, would further erode the morale

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<sup>63</sup> Kristiadi, J. “Indonesia: Redefining Military Professionalism”, *Military Professionalism in Asia*:

and the capability of the military, and could lead to widespread discontent and perhaps even open revolt.

During a recent talk in Washington D.C. on 21 February 2002, Lt. Gen Agus Widjojo, Deputy Speaker of the People's Consultative Assembly (MPR) from the armed forces faction, pointed out that assigning the police the task of domestic security had been ineffective as "the other institution [police] is not yet ready" to handle the authority formerly with the military. In fact, he felt that the separation of the police from the military was a mistake, and that parliament has realized this to some extent and had thus returned several areas of responsibility such as separatist movements, terrorists and smuggling to the military.

Another challenge is the need to apportion scarce resources to competing priorities to fulfill both internal and external security requirements. Shortfalls will continue to be made up through the military's "unofficial" sources of financing just to keep up with the welfare needs and pay of its soldiers, much less the ability to fund requirements for force modernization and procurement. However, recent events have shown that the budgetary priorities of the senior military leadership would allow force modernization to take precedence over welfare and pay. In 2000, Armed Forces chief Admiral Widodo announced a 'wish list' of naval vessels and aircraft upgrades, specifically mentioning the planned purchase of two Parcham-class corvettes and upgrades of seven F-16A/B jet fighters, while Navy chief Admiral Sucipto revealed plans to increase naval personnel numbers by 20,000 over five years to facilitate the expanding role of the navy.<sup>65</sup> These are, by no means, ambitious plans for a country struggling to pay off huge domestic and

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Conceptual and Empirical Perspectives, ed. Muthiah Alagappa, (Honolulu: East-West Center, 2001), 107.

external debts. Although the external threats to Indonesia remain small in the near term, the military remains concerned over possible Chinese military expansion into the South China Sea, and the threat that this could pose to the security of Indonesia's oil-rich Natunas Islands. In 1995, China extended its claims to territorial waters within Indonesia's exclusive economic zone (that included the Natunas)<sup>66</sup> and had shown the resolve to use force to stake its claims, such as the exchange of fire between a Philippine gunboat and 3 alleged Chinese vessels in 1996, and the naval confrontations between China and Vietnam in 1994 over oil exploration areas. In addition, the years of neglect towards force modernization (as shown by the poor state of the military's equipment) will also mean that force modernization would compete for scarce funds with improving soldiers' pay.

The weak economic conditions have also had an impact on the ability and resolve of the government to make drastic changes. Even former President Wahid, who instituted a wide series of changes to strip the military's power, said in an interview that the military's dual function has to continue for the next five years because "...the double function is related to the personal income levels of military personnel. First, we have to solve that problem." He appears to have decided to "solve that problem" by ensuring that the military, the army in particular, has its businesses, investments, and jobs protected by ministers from the army.<sup>67</sup>

A lack of resolve on the part of both the military and the civilian leadership to tackle the issue of the military's businesses poses another challenge. This can probably be attributed to 2 factors. The personal financial benefits that officers and soldiers alike

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<sup>64</sup> Jane's Sentinel Review, 2001.

<sup>65</sup> McCulloch.

<sup>66</sup> Introductory Survey on Indonesia, The Europa World Year Book, Vol I, Europa Publications 2001.

accrue from businesses have become too profitable for them to give up, especially so for senior officers who, having been accustomed to the good life, would be unwilling to risk the disappearance of privileges and a drastic plunge in their lifestyles. As such, there is much at stake for them in maintaining the status quo of the military's involvement in businesses. Lt. Gen Agus Widjojo's insistence that military businesses were necessary as long as the economy was not strong enough to permit government funding, and that the problem was not businesses, but "public accountability",<sup>68</sup> is an indication that the military is adopting a wait-and-see attitude and unwilling to kick off reforms in this area yet. This argument was similar to what an army general once predicted in 1970s, that "[o]nce we raise living standards, corruption [and with it, the need for businesses] will disappear."<sup>69</sup> Instead, what happened was that the military got even greedier and corruption became even more rampant.

Resolve by the civilian leadership is lacking as the government continues to be wary of the impact of removing the military's businesses. As such, there is a danger that it might just adopt a wait-and-see attitude. In the last year or so, President Megawati's combination of a weak personality and her nationalist stance favoring the use of military means to suppress secessionist tendencies in the country has allowed the military to slowly regain positions of power and influence.<sup>70</sup> Megawati's priority to maintain the territorial

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<sup>67</sup> Roosa, John, Notes on the Indonesian Military and the New Government, 3 November, 1999. May be accessed at (<http://www.etan.org/news/99c/01news.htm>)

<sup>68</sup> Deputy Speaker of the People's Consultative Assembly (MPR) from the armed forces faction during a recent talk in Washington D.C. on 21 February 2002.

<sup>69</sup> Weinstein, Franklin B., *Indonesian Foreign Policy and the Dilemma of Dependence*, (Cornell University Press, 1976), 246.

<sup>70</sup> "Sources also say that [Megawati] shared {and still shares) the view of senior generals on the importance of the military in maintaining national unity and the need to deal decisively with threats to Indonesia's territorial integrity in Aceh and Irian Jaya/West Papua. Army generals thus could and did rely on the Vice-President [when Wahid was still President] to stave off presidential intervention in the military and to protect

integrity of Indonesia will mean that she will need to continue to rely heavily on the military, and this will undermine her government's resolve to tackle the sensitive issue of the military's businesses.

### Prospects for Change

In the absence of a quick economic recovery and improved security environment, the divestment of the military's business interests will be a difficult task. However, several factors will mitigate these. On one hand, there are the growing middle class, better-educated masses, and increasing demands for government/corporate transparency and wider political and economic participation. On the other, there are the declining political clout of the military and the aspirations of the younger generation of military leadership to instill greater professionalism to the military. Both these external and internal factors combined will have tremendous impact not only on the ability of the military to maintain the status quo of its involvement in business, but also the political capital of absorbing the negative repercussions arising from them.

A possible approach to divesting the military's businesses is to tackle the two most daunting and complicated issues: finding appropriate measures to tackle corruption, and how to compensate the military for lost income.<sup>71</sup> Concurrently, independent oversight agencies could be established to oversee the entire process.

A low-key but resolute approach needs to be adopted to root out corruption in the military. However, it should not overshadow compensation and the overall focus of divestiture as the military leadership would likely band together against what they would perceive to be threats not only to weaken the organization but also to punish them for their

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military interests." Current Data on the Indonesian Military Elite January 1, 1999 - January 31, 2001, *Indonesia*, April 2001, 136.

past excesses. This is a sensitive matter to soldiers whether they are involved in it or not. While corrupt soldiers would want to escape punishment, honest soldiers would want this to be kept low-key, without great fanfare, to prevent further erosion of public confidence, reputation and self-esteem in the military. The most egregious violators should be severely punished and in some cases, these should be well publicized to demonstrate to the public that a clean-up is indeed taking place. Minor offenders can be fined, demoted or disciplined while serious offenders can be discharged, given “early retirement” or stripped of their pensions and benefits.

For example, ex-President Abdurrahman Wahid, even in his capacity as the military’s supreme commander, was unable to promote pro-reform Lt. Gen. Agus Wirahadikusumah as Army chief to replace GEN Tyasno Sudarto in October 2000. Many of the generals went against Agus, citing his move to reveal irregularities in the foundation belonging to *Kostrad* that implicated a number of generals during his brief tenure at the command. Agus was eventually given no job in the massive reshuffle<sup>72</sup>.

There is a prevailing argument that seems to justify the continuation of corruption in the military. First, the imposition of stringent measures to eliminate ubiquitous petty corruption would cause internal rifts within the military ranks, as soldiers need this additional source of income to survive. In addition, any serious efforts to root out the widespread corruption at higher levels would raise unacceptable political risks, not only for the military, but also for the civilian government as many political parties and prominent figures are also involved. However, the present wave of crackdown against corruption by the political elite (former Trade Minister, Rahardi Ramelan, and Parliament Speaker and

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<sup>71</sup> Scobell, 18.

<sup>72</sup> “Skepticism remains over TNI internal reform,” *Jakarta Post*, 3 January 3, 2001.

leader of Golkar party, Akbar Tandjung, detained over scams related to Bulog; Indonesia's central bank governor Sjahril Sabirin) could offer some insights into the approach that could be applied to the military.

In the past, while the move against corruption would result in jeopardizing the military-dominated government legitimacy and the military's unity, the circumstances have changed. Not only is the government gradually shedding a military-dominated image, there are also sufficient indications that the next generation of military leadership are more keen for the military to adopt a more professional outlook by ridding itself of the legacy of its businesses.

The assumption that improvement of the country's economic conditions will naturally lead to the eradication of corruption is wishful thinking. The root of corruption does not stem from poor economic conditions, although it appears that corruption is most endemic in countries that have a poor economic record. Rather, corruption springs from the lack of institutional systems of checks and balances and from the greed and selfishness of humans. Waiting for corruption to naturally fade away as economic progress is made is therefore a flawed and dangerous argument that would lead the military down the same road it has trodden for the past few decades. The first glimmer of recovery must not be a signal to return to the good old days of unbridled excess.

The military must be assured that it will be fairly compensated for the value of the divested enterprises and the revenues it derives from them. This is likely to be the top concern of the military leaders, from those who are genuinely concerned about minimizing any negative fallout on the organization, and from those who have benefited personally and therefore concerned about the impact on their own incomes and lifestyles to which they

have been accustomed to. The details and mechanics of compensation must be made explicit to them at the outset. China's approach to the divestment of the People's Liberation Army's (PLA) extensive business interests could offer some insights into the viability of this measure. A bargain appeared to have been struck in mid 1998 that the PLA would receive a one-time dividend and a permanent hike in the defense budget.<sup>73</sup>

A temporary agency, possibly headed by an army veteran and/or a highly respected figure, could be set up to oversee the process of divestiture. The entity should be a joint civilian and military venture not beholden to any bureaucratic interest. It could be fashioned after the US Resolution Trust Corporation that disposed of the assets of failed savings-and-loan institutions or the Federal Republic of Germany's Treuhandanstalt that supervised the privatization of state firms in the former German Democratic Republic. The State Economic and Trade Commission (SETC) of China set up in late 1998 might provide some insights into the challenges: PLA leaders have complained the military was only being compensated for a fraction of the actual value of the assets being turned over (suggesting that costs had been contained?); PLA leaders have refused to part with certain enterprises, arguing that certain companies should be exempt, and claiming that these operations are engaged in military rather than civilian production; the PLA also appears to have succeeded in winning significant increases in the level of compensation.

The presence of effective, non-politicized and independent regulatory bodies is necessary to ensure that the military operates within its boundaries and that reforms continue to be on track. The military needs watchdogs that do not only know how to bark and alert the government, but also to be courageous and tenacious in biting in order that the military can be firmly put on the right track.

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<sup>73</sup> Scobell, 15.



## CONCLUSION

The immediate objectives of reducing the military's businesses are clear: reduce corruption throughout the ranks; erode the political power of the military as part of the overall political reform efforts; and enable the civilian leadership to take greater responsibility in enhancing the pay and welfare of the soldiers through legitimate means.

More importantly, it sends broader messages at the national level. First, an active role by the government to tackle corruption in the military sends clear warning signals to corrupt politicians, encouraging signals to both the Indonesian people and the international community of its resolve to combat corruption and the determination not to return to past excesses. A positive effect on the latter group is important as Indonesia desperately needs investments to stimulate economic recovery. The urgency of the task cannot be overemphasized as the emergence of China as a great economic power will draw away investments from Indonesia if China is perceived to be more attractive and Indonesia continues to be plagued by inefficiencies and corruption.

Secondly, divestment of the military's businesses would remove the commercial orientation of the organization and allow officers and soldiers alike to devote more time to their professional military tasks. The short term benefit is the restoration of the military's standing in society and morale within its ranks. The longer term benefit is a military that is more capable of focusing on contributing to regional stability, and tackling the issues of piracy and refugees.

Thirdly, a military that is much more financially dependent on the government will be unable to challenge the legitimacy of the government, therefore minimizing the possibility of its future interference in the political life of the country.

All these factors work towards addressing the country's national priorities of economic recovery, normalization of political life, and restoration of law, security, and public order, which President Megawati highlighted during a speech at the annual session of the People's Consultative Assembly on 1 November 2001.

Because of the impact on both the military and the country, the divestment of the military's businesses must be a key aspect of the military's reform efforts. Not only does it play a role in buttressing the military's political power, it has a detrimental impact on combat readiness, a negative effect on civilian control, damages the morale and cohesion of the military and disrupts the real economy. However, the most undesirable impact has been the corruption borne out of both greed and necessity. Addressing the military's businesses through tackling corruption, compensation and the creation of oversight agencies is therefore critical not only for the success of the military's reform, but also to the country's future.

## CHRONOLOGY OF KEY EVENTS IN THE MODERN HISTORY OF INDONESIA

(Extracted from Jane's Intelligence Review 2001)

| <i>Date</i> | <i>Event</i>                                                                                                                                                                                                                                     |
|-------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1945        | Sukarno proclaimed Indonesia's independence.                                                                                                                                                                                                     |
| 1949        | Indonesia's full sovereignty recognised by the Netherlands following bitter four-year war.                                                                                                                                                       |
| 1957-8      | Regional revolts in Western Sumatra and Sulawesi.                                                                                                                                                                                                |
| 1959        | Sukarno proclaimed 'guided democracy'; reverted to 1945 Constitution granting president wide powers.                                                                                                                                             |
| 1962        | The Netherlands agreed to cede Irian Jaya to Indonesia after 12-month UN administration.                                                                                                                                                         |
| 1965        | Major General Suharto suppressed attempted coup by PKI.                                                                                                                                                                                          |
| 1966        | Sukarno conceded effective power to Suharto.                                                                                                                                                                                                     |
| 1967        | Suharto formally became Indonesia's second president.                                                                                                                                                                                            |
| 1975        | Indonesia invaded East Timor, formally annexing it the following year.                                                                                                                                                                           |
| 1991        | Shooting of dozens of civilians in Dili focused attention on human-rights problems in East Timor (November).                                                                                                                                     |
| 1995        | Fiftieth anniversary of declaration of independence.                                                                                                                                                                                             |
| 1995-6      | Strikes and disturbances in East Timor and Irian Jaya.                                                                                                                                                                                           |
| 1996        | Government attack on breakaway PDI offices causes riot in Jakarta (July). East Timor Catholic bishop, Dom Carlos Filipe Ximenes Belo, and self-exiled opposition figure Jose Ramos-Horta shared the Nobel Peace Prize (October).                 |
| 1997        | Economic recession began; IMF bail-out programmes began but resistance by the Suharto government exacerbated economic problems.                                                                                                                  |
| 1998        | Suharto elected president for seventh term (March). Widespread violence forced Suharto to resign. Vice President B J Habibie takes over as president in May. Parliament met in special session to begin electoral transition process (November). |

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|------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1999 | <p>Habibie offered East Timor the opportunity to choose between autonomy or independence (January).</p> <p>First free elections in 40 years held (7 June).</p> <p>East Timor ballot held amidst unprecedented violence (30 August).</p> <p>Parliament elected Abdurrahman Wahid as president and Megawati Soekarnoputri as vice president (October).</p> <p>East Timor formally removed from Indonesian sovereignty and placed under United Nations control (October).</p>                                                                                                                                                                                                                                             |
| 2000 | <p>Sustained violence occurs on the Maluku Islands (January).</p> <p>National Human Rights Commission implicates 33 people in East Timor violence (January).</p> <p>``Humanitarian Pause" brought reduction in Aceh violence (May); later extended until March 2001.</p> <p>President Wahid handed over daily control of the bulk of governmental business to Vice President Megawati (August).</p>                                                                                                                                                                                                                                                                                                                    |
| 2001 | <p>President Wahid censured by parliament for alleged involvement in corrupt practices (February).</p> <p>Major ethnic violence flared in central Kalimantan (February).</p> <p>Exxon-Mobil ceased operations of Arun natural gas field in Aceh because of security concerns (March-July).</p> <p>Government initiated major political-military programme to address security problems in Aceh (April).</p> <p>President Wahid received a second letter of censure from parliament, who subsequently voted to commence impeachment proceedings (May).</p> <p>Parliament approved wide-ranging autonomy bill for Aceh (July) and Irian Jaya (October).</p> <p>Wahid impeached; Megawati became president (23 July).</p> |

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