

## Summary

*The [business] involvement of army officers is a fundamental trigger for conflict, abuses of power, crime, and human rights violations.*

—An Indonesian human rights activist, email message to Human Rights Watch, September 26, 2005

*Up to now, benefits from military business are still enjoyed by the upper echelon of the military elite.*

—Minister of Defense Juwono Sudarsono, quoted in *Tempo Interactive*, February 23, 2005

*Business is autonomy... It is not good for the command hierarchy.*

—Lt. Gen. Sjafrie Sjamsoeddin, secretary-general of the Ministry of Defense and former spokesman for the Indonesian military, in an interview with Human Rights Watch, April 12, 2006.

*Civilian governments can't control the military if they don't control the budget. It's as simple as that.*

—A foreign military reform expert, speaking to Human Rights Watch, September 7, 2004

It matters how militaries get their money. Civilian control over a state's armed forces is fundamental for the development of a professional military that respects human rights. The more a military's revenue and spending are outside civilian government control, and the more funds it raises itself, the harder it is for civil authorities to engage in meaningful oversight of the military. The result is a government that lacks the power to demand accountability from its armed forces and to implement needed reforms. Particularly when a military has a record of exercising political power and of committing human rights abuses with impunity, financial autonomy can lead to abuse.

Military self-financing is an established practice in Indonesia. From the first days of independence, Indonesia's armed forces have found their own means. Successive governments have endorsed or chosen to ignore the military's economic activities. In recent years, Indonesian officials have contended that the military budget is sufficient only to meet half the military's minimum requirements. A thorough review would be needed to determine appropriate levels of government financing but it is true that

Indonesia's official military budget is low compared to many of its neighbors in Southeast Asia.

The Indonesian military deals with its budget constraints using a combination of approaches. In part it acts by deferring or reducing its spending in some areas, such as equipment purchases. At the same time, it seeks funds for that purpose from other government accounts, often acting outside approved budgeting processes and with little transparency. In addition to juggling government funds in this way, Indonesia's military also independently raises money through a complex web of commercial ventures whose profits bypass the treasury. It is these independent revenue sources that are the focus of this report.

The Indonesian military draws on off-budget (extra-budgetary and unaccountable) funds derived from military-owned enterprises, informal alliances with private entrepreneurs to whom the military often provides services, mafia-like criminal activity, and corruption.

Much of the revenue from such ventures goes directly to commanders, specific units, or individual soldiers. Ostensibly the funds are to support troop welfare, but often they are destined for personal enrichment instead. Some of the funds are used for day-to-day operating expenses of the armed forces. Irrespective of the purpose to which they are put, off-budget funds are not monitored or subject to financial controls. Such are the budgetary pressures and weak controls in Indonesia that it is common for government agencies to raise funds independently to help meet expenditures, which in turn helps fuel widespread corruption. Yet the problem of self-financing and its consequences are most serious with respect to the security forces, especially the military. (The question of police self-financing merits close scrutiny but is beyond the scope of this study.)

This report provides a human rights analysis of military self-financing in Indonesia. The first part of the report reviews how the Indonesian military came to be involved in business activity, and explains how such activity has spread over time. It also examines the failure of government authorities to enforce rules against military commercialism.

The second part of the report offers a detailed look at how the Indonesian military finances itself, providing the most comprehensive account to date of the nature and scope of the problem as viewed through a human rights lens. It identifies the four broad categories into which the self-financing activities fall and details how each works.

We find that the military supplements official funds using profits from its own businesses, payments from private-sector allies (often for security services), income from

black market activities, and money skimmed from corrupt dealings. Formally-established businesses have performed poorly in recent years, leading the military to increasingly rely on irregular and illegal fundraising. We provide examples to illustrate the military's different economic entanglements and some of the human rights abuses associated with them.

The third part examines obstacles to change and reform efforts to date. It identifies the absence of transparency and accountability regarding military finance issues as a serious impediment to reform. Official data on military budgets and spending are unreliable and incomplete. When it comes to off-budget matters, including revenue from military businesses, no reliable figures exist and estimates have varied wildly. The difficulty in establishing credible statistics is but one indication of the need to improve financial management of military affairs. Some changes are underway, as part of wider efforts to improve public financial management, but additional, targeted measures are needed to ensure adequate oversight and reporting on military finances. The military's revenue and spending remain one of the least transparent and accountable elements of the government's accounts.

This part of the report also addresses three myths often trotted out to explain the slow pace of reform: that funds from official government sources are sufficient to meet only a fraction of the needs the military; that military businesses generate substantial revenue that goes most of the way toward filling the gap; and that the proceeds of military businesses largely are spent on troop welfare.

While it is true that official Indonesian government spending on the military is relatively low, it is higher than military budget figures suggest. Additional government outlays are hidden in other budget lines, there is a significant level of waste, and government support levels have increased substantially in recent years.

As for the second myth, the evidence we have shows that many military business ventures have been great failures and that, on net, even the businesses in which the military has a direct ownership stake contribute only modest sums to help cover unbudgeted expenses—as government officials have begun to acknowledge. In the permissive environment engendered by the expectation that the military will generate income to contribute to its costs and by the absence of monitoring of that income, the weak performance of the “regular” businesses owned by the military has contributed to the spread of informal and illegal military economic activities that are more hidden and more difficult to control.

There are also strong indications that, contrary to those who espouse the third myth, much of the funds the military raises independently (particularly but not exclusively funds raised through systemic corruption and other criminal activity) goes into pockets of individuals, instead of to improve conditions for the troops.

The report's assessment of reform efforts to date focuses on the 2004 law that is the basis of current efforts. That law mandated that the military end its business activity within five years. To make the most of the opportunity, civilian and military officials alike must commit themselves to comprehensive reform. Unfortunately, as announced to date the government's plans would not address the full scope of the problem. They focus exclusively on a subset of one type of military economic interest: formally-established businesses in which the military has a documented ownership share.

Military leaders similarly have sought to limit the scope of financing reform in order to retain many business ventures that they argue—contrary to the evidence—are independent of the institution of the military, do not make use of government resources, or only serve to support soldier welfare. All indications are that they have succeeded: at this writing, the government's draft proposal provided all these exceptions. The result would be a superficial reform that would leave untouched many military business enterprises, as well as the military's stake in irregular and illegal business activity.

The report concludes with detailed recommendations for reform. It argues that for military finance reform to succeed the government must define the problem accurately, recognize the true human rights costs of self-financing—including in terms of weakening the government's ability to bring military personnel to justice for crimes that violate human rights—and commit fully to stamping it out. That will require concrete steps to impose financial accountability on the military, ban all forms of military commercialism, develop and implement a comprehensive strategy to withdraw the military from business activity, and fund the military at appropriate levels (following a close review of actual needs and bearing in mind other national priorities).

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It is nearly impossible to determine the total value of the Indonesian military's various economic activities. The military's extensive network of economic interests is scattered across the country and includes businesses large and small, centralized and locally controlled, legal and illegal. No one, including top military leaders, has a full grasp of the sums involved. For years government officials repeated informal estimates suggesting that funds formally allocated to the military in the national budget covered only 25-30

percent of actual military expenditures and that the remainder was paid from off-budget funds, but by 2005 they dismissed these estimates as outdated and inaccurate. Nor is it clear if more recent estimates placing the figure at about 50 percent are any more reliable, since officials have not undertaken an analysis of the extent of off-budget activity and in any case give inconsistent information.

There is equal confusion over the number of military businesses. An initial military inventory in 2005 first put the figure at 219, but a subsequent one in 2006 gave the number as 1,520. Some government officials have questioned the credibility of the revised data and suggested the actual number of military businesses was far lower than indicated. There is equal reason to think that the official inventory undercounted the number of military businesses, since it excluded informal and illegal economic activity. The inability to quantify the extent of the military's fundraising and the exact number of its business, however, does not detract from the need for change. There is general agreement that military self-financing is a dangerous practice that should not be allowed to continue.

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### ***Opportunity for Reform***

The Indonesian military (Tentara Nasional Indonesia or TNI) is now required by a 2004 law to withdraw from economic activity. Under that law, the Indonesian government must take over military business holdings by 2009. The law also bars the military from engaging in business activity and receiving funds outside of the state budget. Indonesia's military leadership has pledged to cooperate and expressed willingness to give up some of its business interests before that deadline. Civilian officials have acknowledged that pervasive military economic activity takes a heavy toll on the armed forces and the country, and that it should be brought to an end. These policy commitments represent an important shift after years in which various governments made excuses for inaction and military officials actively resisted reform.

The stakes are high. If implemented fully and in a timely manner with transparency and accountability, reform of military finance could mark a major step toward structural reform of the TNI. Many in Indonesia's military share the view that they should get out of the business of private moneymaking. They recognize that the focus on fundraising reduces military professionalism and readiness. Senior military officers continue to publicly defend some types of military business activity as a way to support the basic needs of soldiers, but they are increasingly likely to acknowledge that many military businesses have given way to self-serving ventures that offer little to the troops and

instead only sully the military's reputation. A growing number of military personnel at all levels would prefer not to engage in self-finance and would rather the state took responsibility to fund the military appropriately.

There are other important reasons to end military self-financing. Military economic engagements are bad for the economy: they introduce market distortion and irrationalities; provide a platform for corruption and rent-seeking behavior (defined as the extraction of excess profits, such as through privileged access to lucrative natural resources); add to the cost of doing business (through the payment of protection money); and contribute to environmental degradation that impedes sustainable development.

The compelling human costs of the military's economic activities also must be considered. Civil society groups have long drawn attention to the many ways in which military economic entanglements fuel abuses of power, including corruption and human rights violations. The Indonesian military has a dismal human rights record, and it is widely recognized that military self-financing plays a role in facilitating such abuses. Economic incentives can motivate certain military abuses—including extortion, property seizures, and profiteering—and also can help fuel or sustain violence in conflict areas where the armed forces have access to lucrative natural resources or money-making ventures. More generally, the military's financial autonomy undermines civilian authority and accountability. Effective reform of military finance would serve to enhance accountability and help curb military abuses in Indonesia.

The drive to end the military's economic activities forms part of a wider agenda to move the military more firmly under civilian control. Indonesian policymakers and military leaders have acknowledged the public demand for military reform and have begun to carry out some structural changes. Notably, the withdrawal of the military from parliament, designed to help reduce the military's political influence, was completed in 2004. Progress to date has been limited and highly selective, but top Indonesian officials, including President Susilo Bambang Yudhoyono, the defense minister, and the chief of the armed forces, have expressed a firm commitment to advance the military reform agenda. Reform-minded officials and military officers have the support of the public. A 2005 opinion poll by the Indonesian Survey Institute found that a majority of Indonesians support a variety of reforms to reduce the military's power in society. Consistent with that view, a majority also believe that the armed forces should be funded solely by the government and that the military should not engage in business activities.

The recent recognition by Indonesian leaders of the need to address military finance and business dealings is welcome, but the pledges to undertake serious reform have not been

matched by concerted action. Government moves to begin addressing the military's economic entanglements have been slow, half-hearted, and incomplete. Proposals to address self-finance have failed to comprehensively deal with the problem and its human rights aspects. To fulfill the promise of the 2004 law, the government should radically rethink its approach.

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### ***Note on Methodology***

This report and associated advocacy efforts form part of a wider program of work by Human Rights Watch. Our research on business and human rights issues has resulted in reports on many countries and a range of issues. We have prepared reports that examine the activities of private companies in light of international standards on corporate behavior. We have documented widespread violations of the human rights of workers. We also have analyzed how mismanagement, corruption, and the absence of transparency over government finances can undermine human rights. We work internationally to press for public accountability of government funds, for corporate accountability for human rights abuses, and against off-budget financing mechanisms that are rife with corruption and ultimately undermine human rights protections.

The research for this report was conducted over the course of two years and entailed four research trips to Indonesia. We investigated military financing issues and researched several examples that showcase some of the human rights abuses associated with military economic activity. We also sought to understand the financial pressures experienced by the military and the difficult choices faced.

The report is based on more than two hundred interviews and extensive additional research carried out in Indonesia and from abroad. We spoke to a wide range of people to gather information. We met with government officials from the Ministry of Defense, TNI headquarters, and numerous other government ministries or agencies. We also exchanged correspondence with some of these officials. Additional sources included scholars, professional analysts and researchers, military experts, community activists, retired military officers, and journalists. We also spoke to businesspeople, diplomats, and international finance experts. We traveled to Aceh, North Sumatra, and South Kalimantan provinces to carry out detailed field research with the assistance of Indonesian colleagues. We also have relied on public disclosures, other published research, and unpublished materials to supplement our original research. We have benefited especially from the work of the many independent experts, human rights campaigners, and other civil society activists whose efforts to raise awareness of the

phenomenon of military business in Indonesia and to advocate for its abolition helped generate the political will to begin to tackle this serious problem.