

Building Integrity and Reducing Corruption in Defence

A Compendium of Best Practices



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Chapter 11

The Involvement of Defence Personnel and Assets in Economic Activities

Introduction

In transition democracies, the military remains influential in the country's political and economic system. The dark past of political and security situations in some transition democracies successfully established the military as the core actor in these countries. The military created the social and political basis for their supremacy over civilian oversight through their domination of the effective legal control of violence. Thus, it is not surprising if the military still has strong power within the society. Ironically, sometimes civilian politicians also took advantage from this situation by creating mutual relationships with the military through the politics of violence to maintain their power and create uncertainty in the democratization process.

One of the most significant impacts of military intervention in the political and economic system is the transformation of the military as an economic actor. In this sense, the military uses its resources (personnel and assets) to get involved in economic activities. From this short explanation, it can be understood that these economic activities cover both personal and institutional aspects of the military. Later, these economic activities violate the essential role of the military within the state system and also threaten human rights.

This chapter is specifically intended to analyze the involvement of defence (military) personnel and assets in economic activities through the conceptual discussion of the military as an economic actor and the perverse impact of military economic activity using the case study of the Indonesian Military's (TNI: *Tentara Nasional Indonesia*) business activities.

The Transformation of the Military as an Economic Actor

Defence is the most expensive and complex feature of the state. It is widely recognized that to develop an ideal defence capability the state should spend a huge amount of funds from its national budget. On the other hand, the state should also prioritize spending on other areas such as education, public welfare and health, which

are increasingly costly. This dilemma does not automatically stipulate the transformation of the military into economic actors in order to create sustainable financing for the defence budget. In short, the military is not trained to be profit-oriented but to be a professional security actor even with the minimum budget. However, the trend of military economic activity has not decreased yet. In fact, in countries such as Bangladesh, the Philippines, Pakistan, China and Russia, the military is still actively involved in profit-oriented activities, whether legal or illegal. Such a trend shows that there is still growing discourse on the logic behind the transformation of the military as an economic actor.

According to Brömmelhörster and Paes, there are several common reasons for the involvement of the military in economic activity. First, the military has access to material and human resources that are less accessible to civilians and that enable them to carry out other tasks. Secondly, the military often turns to private enterprise to make up shortfalls in defence budgets. Thirdly, weak states and poor civilian control of the military create an added incentive for military elites to undertake commercial enterprises. Fourth, the roots of some military businesses can be traced back to measures taken in order for insurgent forces to be self-sufficient. Finally, even when security threats have subsided, downsizing of the armed forces is difficult to achieve and militaries are therefore used in secondary roles.¹ Based on these explanations, we could generalize more specific situations for military involvement in economic activities.

There are two types of situations that stimulate militaries to transform into economic actors; namely, the politico-economy nexus and the lack of state budget fulfilment. Politics and economy are like two sides of a coin. Hence, it is widely accepted that if military actors have the political power then they will also play a significant role within the economic sphere in the state and *vice versa*. In this case, the economic activity of the military substantially contributes to the political power of their civilian ally or their military leaders. Such a relationship between the military and the politico-economy power frequently happens under oppressive governments; for example, in Indonesia during General Suharto's regime.

However, military economic activities do not always exclusively stand for their political power. In non-authoritarian countries or transition democracies, after the removal of their political power, the military is being pushed to be professional. Unfortunately, the pressure to professionalize the military is not backed by proper financial support from the government. As a consequence, the military obtains the justification to perform economic activities as their budget is not fully supported by the government. Such off-budget funds are claimed to finance the deficit of military budgets, even though in reality such economic activities tend to accumulate profit for high-ranking military offi-

¹ Jörn Brömmelhörster and Wolf-Christian Paes, eds., *The Military as an Economic Actor: Soldiers in Business* (New York: Palgrave Macmillan, 2003).

cers. Ball and Hendrickson argue that there are several factors that may encourage off-budget military spending: a strong executive decision-making culture; the role played by the military in the social and economic sectors; security problems; institutional fragility; and military involvement in protecting or selling natural resources.²

Both types of military involvement in economic activities are not independent. In fact, such situations are supportive in their nature, as can be seen in the case of Indonesian military business.

The Structure of Indonesian Military Business Activities

Historically, the TNI's business activity was established under General Suharto's oppressive regime from 1967–1998. During Suharto's leadership, the TNI was given the privilege of managing their budget and operations without any critical oversight from the parliament or civil society organizations. Through ABRI's (former name of the TNI) *dwifungsi* doctrine, the TNI was granted extensive social and political roles. According to the doctrine, the Indonesian Military were both defenders of the nation and a social-political force in national development.³ As a consequence, the doctrine justified TNI participation in the development agenda, especially regarding economic development in the country.⁴

Following the expansive role of the TNI, in the 1970s the TNI built their business empire, which was set up via the establishment of foundations and cooperatives. Based on the Human Rights Watch Report on the Indonesian Military's business activity in 2006, there are certain types of military personnel and assets that have been involved in economic activity since the Suharto era:⁵

² Dylan Hendrickson and Nicole Ball, "Off-budget Military Expenditure and Revenue: Issues and Policy Perspectives for Donors," Conflict Security and Development Group Occasional Papers (2002).

³ Leonard C Sebastian, *Realpolitik Ideology: Indonesia's use of Military Force* (Singapore: ISEAS, 2006), 323–325. See also: GlobalSecurity.org, "ABRI-Armed Forces of the Republic of Indonesia," www.globalsecurity.org/military/world/indonesia/abri.htm. In addition, ABRI also received non-electoral seats in the parliament and plays an important role as the gatekeeper for the Suharto government.

⁴ For details on TNI's intervention in the political and economic system under Suharto, see: Harold Crouch, *The Army and Politics in Indonesia* (Jakarta & Kuala Lumpur: Equinox Publishing, 2007); Sukardi Rinakit, *The Indonesian Military After the New Order* (Copenhagen: NIAS Press, 2005); Leonard C. Sebastian, *Realpolitik Ideology: Indonesia's Use of Military Force* (Singapore: ISEAS, 2006).

⁵ See for details: Human Rights Watch, *Too High a Price, The Human Rights Cost of the Indonesian Military's Economic Activities* 18:5(C) (June 2006), www.hrw.org/en/reports/2006/06/20/too-high-price-1.

a. Military-owned Business

- *Foundations (yayasan)*

The military foundations were established in the 1960s to provide social services such as housing and education for troops and their families. In the process, such foundations were expanded into business units presumably to finance the soldiers' welfare. In addition, these tax-exempt foundations supervise many important military business units. The army, through the Kartika Eka Paksi Foundation (YKEP), owns a total of 26 firms and seven joint ventures.⁶ YKEP's business activities are managed by a holding company, PT Tri Usaha Bhakti. The various army interests include the Sudirman Central Business District, which owns 44 hectares in what is known as Jakarta's "Golden Triangle," the Artha Graha Bank, Cigna Indonesia Assurance, Danayasa Artatama (the Hotel Borobudur), other real estate, timber, golf courses and manufacturing.⁷

Meanwhile, the navy, through the Bhumyamca Foundation, controls five firms with total assets of Rp 200 billion or \$25 million. The foundation's business interests include Admiral Lines (shipping), resorts, an oil refinery, property rental, import-export, cocoa plantations, maritime electronics and telecommunications, a taxi company and diving services.

Finally, the air force and the Adi Upaya Foundation manage 17 firms, including a bank.⁸ The foundation owns the Bank Angkasa, together with the National Electricity Company Pension Fund and private investors. The foundation's other interests include golf courses, container services, hotels, logging, aviation and aerial photography enterprises.⁹ Despite this institutional business, the TNI personnel, from high-ranking officer to low-ranking soldier were actively involved in businesses like forestry, mining, oil and security guards.¹⁰

- *Cooperatives (Koperasi)*

The military cooperatives were established to improve the welfare of soldiers by providing subsidized commodities, such as rice, to soldiers and families.

⁶ Rachel Langit, "Indonesia's Military: Business as Usual," *Asia Times Online* (16 August 2002), www.atimes.com/atimes/Southeast_Asia/DH16Ae06.html.

⁷ Angel Rabasa and John Haseman, *The Military and Democracy in Indonesia: Challenges, Politics, and Power*, Monograph Report (Pittsburg: RAND, 2002), 74.

⁸ Langit, "Indonesia's Military" (2002).

⁹ Rabasa and Haseman, *The Military and Democracy* (2002), 76.

¹⁰ *Ibid.*, 75.

Box 11.1. Racketeering

The practice of racketeering in the TNI took form as TNI personnel offering protection for criminal activity. For example, in Medan, North Sumatra, the military involvement in crime is well-organized. According to an interview conducted by Human Rights Watch, Medan residents said that the protection rackets are regularized, with shop owners and trucks paying monthly fees and showing stickers designating which military group or associated gang supported them. Another example is in illegal logging activity where TNI personnel, especially on the Indonesia-Malaysia border, were offering “protection” to illegal loggers in return for payment or were reaping the benefits of seized log cargoes, which they later sold for their own financial benefit. Another profitable activity is allowing illegal log transporters who have been captured to go free for a price (bribing).

Sources: Human Rights Watch, *Too High a Price, The Human Rights Cost of the Indonesian Military's Economic Activities* 18:5(C) (June 2006), 66, <http://www.hrw.org/en/reports/2006/06/20/too-high-price-1>; A.C. Casson, et al., *A Multistakeholder Action Plan to Curb Illegal Logging and Improve Law Enforcement in Indonesia*, WWF Indonesia, World Bank, DFID-Multistakeholder Forestry Program (October 2006), www.sekala.net/files/FLEGedit4Sept06.pdf.

However, like the foundations, the military cooperatives also expanded into wide-ranging business activities such as hotels and cargo companies.

- *Forestry operations*

In 1967, the Suharto government granted concession rights of more than one million hectares of forest along the Indonesia-Malaysia border to a military-owned company PT Yamaker. The decision was based on “national security considerations” during the preliminary border dispute between Indonesia and Malaysia. Since then, the number of military-owned companies and military personnel receiving this privilege has increased.¹¹

b. Military Collaboration with Private Business

This type of military economic activity covers the military business alliance with private companies, whether they are national or foreign companies. In this kind of relationship, the military acts as the business broker; for example, arranging government licenses and blocking other competitors, gaining access to goods and services, transporting on military vehicles for a fee and leasing out land. Private companies also contribute to

¹¹ Supto, a senior politician from the Prosperous Justice Party and a former secretary in the Department of Forestry once said that military members managed to get shares in approximately 550 logging concessions. Quoted from: Andreas Harsono, *Indonesian Military and Prostitution Racket*, www.globalintegrity.org/reports/2006/INDONESIA/notebook.cfm.

the military “acquaintance funds.” For example, a developer provided land and buildings worth Rp. 18.5 billion (\$1.95 million) to locate an army base inside a West Java industrial zone known as Jababeka. The donation made good business sense, an official of the industrial zone argued, since the presence of military personnel “can deter people from carrying out crimes here.”

c. Military Involvement in Criminal Activity

Some forms of this economic activity are illegal logging and racketeering (when the military acts as the protector of criminal activities such as gambling operations, drug trafficking and prostitution). Racketeering is the most popular form of low-rank to middle-rank economic activity in the TNI (see Box 11.1 above).

d. Military Corruption

In the military, the biggest potential area for corruption is defence procurement. For example, in 2004 the army planned to buy MI-17s from Russia. Accordingly, the Members of Commission I (defence commission) of the parliament (DPR) had received reports the helicopters should have been valued at only \$17.6 million, a price 25 percent lower than the \$21.6 million the army had agreed to pay. Later, the helicopters were due at the end of February but, as *Tempo* magazine reported, a Russian firm stopped assembling them as it had not received the down payment of \$3.2 million.¹²

However, the TNI's economic activity is not only pushed by their active role in the political sphere as the guardian of the Suharto regime but also by the fact that the government is only able to finance 25–30 percent of the total defence budget. Hence, the remaining 70 percent is derived from the practice of military business. The TNI's economic activity can be seen in a pyramid showing TNI's economic support structure (see Figure 11.1).¹³ At the top of the pyramid is the government's official defence budget which only covers about one-third of the total budget. At the second level are the state enterprises in which some retired high-ranking military officers filled the managerial positions and thus encourage the domination of military-owned enterprises to maintain contracts with the state enterprises such as *Pertamina* (the state oil and gas company). At the third level are the military cooperatives and foundations, which have already been explained above. Finally, at the lowest level are the other re-

¹² Quoted from: Munir, “Corruption threatens Indonesia's defense system,” *The Jakarta Post*, 3 January 2004, <http://www.thejakartapost.com/news/2004/03/01/corruption-threatens-indonesia039s-defense-system.html>. Further investigation by the National Team for Corruption Eradication (*Timnas Tipikor*) found the involvement of army officers in the procurement corruption scandal. See: “The Corruption in DoD involves TNI,” *Republika Daily* (25 March 2006).

¹³ Rabasa and Haseman, *The Military and Democracy* (2002), 73.

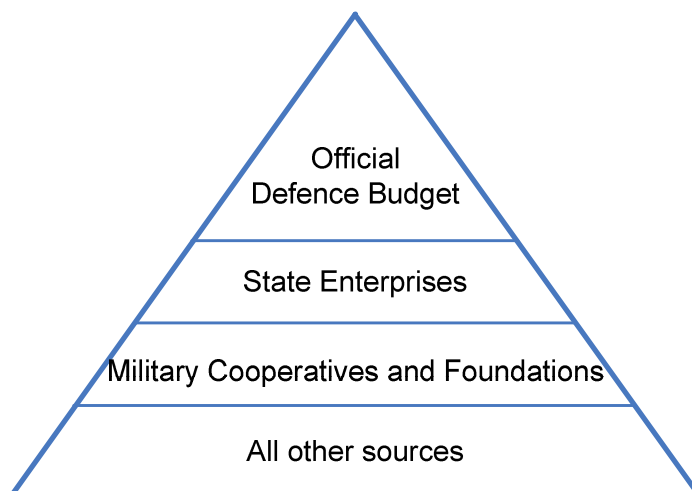


Figure 11.1. The TNI Economic Support Structure.

sources. Examples of this type of fundraising activity are military collaboration with private business and military involvement in criminal activities (racketeering).

In 1998, the Asian economic crisis hit the country and triggered a massive social movement targeting the Suharto government. The reformation movement (*gerakan reformasi*) led by students and activists ended with the resignation of Suharto in May 1998. Subsequently, the movement turned into a democratization process, which encouraged the TNI (and also the Indonesian Police) to reform its institutions and personnel. In 2004, the new TNI law (Law No.34/2004) was passed in parliament (see Box 11.2).

The new law stipulates the government should take over all business activities that are directly or indirectly managed by the TNI before October 2009. Subsequently, in 2005 the government established the TNI Business Supervision and Transformation Team (TSTB) to verify the TNI businesses and provide recommendations to the government on the TNI's business takeover issue. Based on the team report in 2006, the TNI owns 23 foundations, which are supervising 53 companies, and 1,321 cooperatives. The TNI also owns 1,618 properties, covering more than 16,500 hectares, and 6,699 buildings. Overall, the report shows the TNI's business assets are worth Rp 2.2 trillion (US \$235.4 million).¹⁴

¹⁴ "TNI Business Takeover 'Merely a Formality,'" *The Jakarta Post* (15 November 2009), www.thejakartapost.com/news/2009/10/15/tni-business-takeover-merely-a-formality039.html.

Box 11.2. TNI Law No. 34/2004

Chapter II, Article 2(d) states that:

Professional soldiers, that are well-trained, well-educated, well-equipped, do not involve in politics, do not involve in business and his/her welfare is guaranteed by the state, and support state political decisions that are based on democratic principle, civilian supremacy, human rights, national law and international law and that have been ratified by the state.

In addition, Article 39 of the law also states that any TNI member is prohibited to be involved:

1. As a member of a political party;
2. In political activities;
3. In business activities;
4. In any activities intended to gain parliamentary seats in the elections and/or other political positions.

Source: TNI Law No. 34/2004.

Even though the TNI business assets have been verified, the road to take over the assets is still rather long. Until now, the TNI business issue remains the major roadblock for military reform in Indonesia because the government has been acting sluggishly on the issue. The toughest challenge comes from the budget issue of defence personnel. The TNI budget is far from enough to finance the development of a professional cadre. From the overall budget, at least 45 percent is used for the soldier's welfare issue and around 30 percent is used for defence technology, maintenance and development.¹⁵ In addition, the current government is only able to provide half of the required defence budget. Hence, limited public finances impose further consideration on the process of taking over the TNI businesses.¹⁶

¹⁵ See: Eric Hendra, "The TNI's Business," in *Almanac on Security Sector Reform in Indonesia 2007*, ed. Beni Sukadis (Jakarta: LESPERSSI & DCAF, 2007), 121.

¹⁶ As Daniel Lev, an Indonesian expert from the University of Washington once said on the issue of the Indonesian military budget, "If your budget provides about one-third or one-half of what you need, you're going to steal the rest of it." Quoted from: Taufik Darusman, "Putting The Military out of Business," *The Jakarta Globe* (27 September 2009), <http://thejakartaglobe.com/columns/taufik-darusman-putting-the-military-out-of-business/332030>.

The Perverse Impact of the Military as an Economic Actor

Professionalism

The direct implication of the military transformation into an economic actor is their lack of professionalism. By involving themselves in profit-oriented activities, the military could lose its essence as the security actor of the state. In this sense, the military becomes more interested in profit-oriented activities than in providing security to the state and the citizens. The worst scenario from this lack of professionalism is that the military detaches itself from state control. The military's ability to finance the defence budget (even if it's only partially) will increase its sense of independence from the state and thus create the risk of wider military intervention in the social, political and economic spheres of society.

Accountability

The other negative impact of the military as an economic actor is the lack of accountability. If the military is able to fulfil its own budget through independent economic activities, then the issue of accountability of the military budget and operations to the state will potentially be diminished. The risk of this situation is high. If the state is unable to control the military budget and operations, then the military can perform other duties and responsibilities that violate state regulations or even threaten state and citizen security. In short, the military becomes a serious potential internal threat to the state and citizens.

In advanced democracies, the defence budget is actively controlled by democratic civilian oversight mechanisms such as the parliament and non-governmental organizations. This situation is based on the well-established understanding that the military is part of the state apparatus which is responsible for the provision of security and is fully supported by the government. However, in transition democracies, there are some difficulties in overseeing defence spending. There are several reasons for this problem but the most common one is the issue of secrecy of the defence posture, which is reflected in the budget. Sometimes, the military is afraid that their budget will spill into the public area and thus expose its capabilities to civilians or even to potential enemies.

Another reason is the lack of confidence from civilians, especially those in the parliament, to perform critical oversight of the military institution. The major issue here is the military image, which affects the mindset and the rules of the game in the state system. The image of the military as superior to civilians, exclusive, patriotic and controlling legal violence sometimes creates barriers for civilians to react on the budget issues. Indeed, the lack of knowledge on military budgeting and operations on the part of members of parliament also contributes to this situation.

Human Rights Violations

The wider impact of military economic activity is human rights violations. As mentioned above, the military represents the state apparatus, which represents the effective legal control of violence. However, when the military's economic activity combines profit-oriented efforts with the control of violence in a situation where there are difficulties with civilian oversight it may lead to a disaster. An example of military involvement in economic activity that violates human rights is the case of the Freeport security agreement with the TNI in West Papua, Indonesia (see Box 11.3).

Freeport's security arrangement with the TNI echoes the hidden alternative for the TNI to keep their involvement in economic activity. Under article 7 (2) of the new TNI law, the TNI's core function include security of vital national sites. In reality, such a function proved to be one of the main sources of off-budget funding for the TNI.

In January 2006, the Coordinating Ministry for Political, Legal and Security Affairs decided Freeport Indonesia, ExxonMobil and PT Arun LNG were vital sites for the country. Freeport Indonesia, which operates in West Papua Province, has publicly acknowledged destroying the environment less contributes to the welfare of the Papuan people. Later, the existence of Freeport Indonesia fuelled hatred from the West Papuan people and provided the impetus for the organization for the Papua's Independence (OPM: Organisasi Papua Merdeka). Unfortunately, due to its status as a vital national site, Freeport gets full security protection from the TNI (and also the Indonesian National Police). In this case the local people, especially the OPM, are seen by the TNI as the most pressing threat to Freeport.

Conclusion: Pulling the Military Out of Economic Activities

The Indonesian experience has shown that the involvement of the military in economic activities is extensive. The military's economic activities are destructive to their professionalism, affecting their budget transparency and even violating human rights.

Overall, the main problem in military economic activities is the defence budget. Of course, a budget scheme that supports soldiers and their families would insulate the military from economic activities. However, it should be noted that a transparent budget is more important than increasing the welfare of soldiers. Without any responsibility for the effectiveness and efficiency of the defence budget, it is impossible to keep the military out of economic activities.

Additionally, the military's economic activities, specifically in the case of the Indonesian Military's business activities, are not only related to the problem of soldier welfare and insufficient defence budgets. The Indonesian Military's business activity is very complex and deeply rooted in the society's day-to-day life. Since its long development and diffusion in the society, military business in Indonesia is viewed as an ac-

Box 11.3. Freeport's Security Arrangement with the TNI and Human Rights Violations

The presence of TNI in the Freeport area is ironic. While they maintained the security of the vital economic interests in a fashion which largely violated human rights by targeting local people or alleged OPM members, they also received payment from the company, which is not transparent. For example, in the mid-1990s, troops at the mine site allegedly used company vehicles, offices and shipping containers to transport and detain people they then tortured or killed, which were suspected security threats or members of the OPM. Unfortunately, the company said it bore no responsibility for how its equipment was used by the military. Indeed, the Indonesian Human Rights Commission (Komnas HAM) has stated that the involvement of the TNI in Freeport security measures violates human rights in West Papua.

The number of state security personnel in Freeport has risen in the recent year. As of 2005, more than 2,400 government security personnel (military and police) were located in the general area of Freeport's operations. In 2005, the company's spending for military and police security protection funds reached \$66 million. Freeport said that the money was used to pay for transportation, food and barracks for the security personnel. However, the investigative reports published in 2005 by the NGO Global Witness and the *New York Times* suggested that Freeport directed a large portion of its security payments to individuals. These reports alleged that the company had made large, direct payments to individual Indonesian military and police officers, as well as to units in the field. The *New York Times*, citing company documents it obtained and verified as authentic, said such payments totaled about \$20 million from 1998 to 2004.

Sources: Kurniawan Tri Yunanto, "Komnas HAM: Freeport Represents Colonialism in Papua," *VHRmedia* (2 December 2009), <http://www.vhrmedia.com/Komnas-HAM--Freeport-Represents-Colonialism-in-Papua-news2775.html>; Human Rights Watch, *Too High a Price, The Human Rights Cost of the Indonesian Military's Economic Activities* 18:5(C) (June 2006), 48–56, <http://www.hrw.org/en/reports/2006/06/20/too-high-price-1>.

ceptable form of military activity by most Indonesians. Given the situation and general attitudes, removing the military from economic activities in Indonesia could take a long time. In this case, the government should not only restrict the military from economic activities but also restrict or punish the Indonesians that are enjoying economic cooperation with military personnel or institutions. Such a strategy has never been pursued by the Indonesian government.

To conclude, economic activity basically involves two important features: supply and demand. In the military's economic activity, the military acts as the supplier and the demand comes from society. Therefore, in order to fully remove the military role in economic activity, then we should also cut the demand and not only restrict the supply.