The governance institutions of a drug trafficking organization

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Abstract

How do drug trafficking organizations organize? Drug trafficking organizations continue to operate effectively despite incentives for members to defect, pressure from damaged communities, and government interdiction efforts. This paper identifies the problem of defection in this context and applies insights from the literatures on club goods and extralegal governance institutions to explain the puzzling organization and activities of one of Mexico's most dangerous drug trafficking organizations, *La Familia Michoacana.* The group uses a reward and punishment scheme to prevent defection from members and to elicit cooperation from the community and government.

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1. Introduction

In October 2005, five human heads rolled onto the dance floor of a Mexican nightclub, with notes attached to them reading, "Only those who should die will die. Let everyone know, this is divine justice" (Stolberg 2009: A12). This gruesome message marked the emergence of *La Familia Michoacana* (LFM) as one of Mexico's most powerful, bizarre, and brutal drug trafficking organizations (DTOs). Since Felipe Calderón declared a war on drugs in 2006, more than 40,000 Mexicans have been killed and the production and trafficking of narcotics has largely remained unaffected (Molloy 2011). LFM, infamous for its public displays of brutality, or "corpse messaging," occupied the media coverage of the Mexican drug war (Stolberg 2009; Finnegan 2010). Though recent deaths and arrests of its top leaders have threatened LFM's presence in the Mexican drug market, the organization continues operating (Cave 2010; Beaubien and Montagne 2011; Otero 2011; Kouri 2011; Padgett 2011). This article identifies unusual features of LFM's organization and argues that these are a rational way to foster cooperation from its members and the community.

It is not surprising that people have depicted LFM's organization and operation as the result of non-rational actors. Even its founding leader, Nazario Moreno González, was known as *El Más Loco*, Spanish for "The Craziest One." He wrote a religious book expositing the values and philosophy of the organization, which was known by some as "The Sayings of the Craziest One" (Associated Press 2010). Despite the brutality of many of LFM's actions, when González died, the community held a march in his honor. Participants carried signs expressing their respect for González and LFM. The signs included messages such as, "Nazario will always live in our hearts," "Mr. Nazario, for students your ideals live on," and "Long live La Familia Michoacana" (Associated Press 2010: 1).

Several unusual features characterize LFM's organizational structure and activities. As an organized criminal group with experienced killers as members, the association actively promotes

religious devotion. It traffics and distributes narcotics but forbids its members from using drugs or selling them in Mexico. La Familia Michoacana is well known in the community for both "corpse messaging" and passing out Bibles. It stages daring attacks against government security forces, while also providing public goods, supporting local schools, and offering protection to citizens. Its internal organization is also unusual. The group intentionally provides very little information about their organization to some of its most capable members. It imposes substantial costs on recruits who wish to join, including a lengthy period of religious indoctrination and drug rehabilitation. Traditional models of criminal choice have not explained these behaviors. We argue that these activities are rational responses to the problem of governance that LFM faces.[1]

By studying the internal organization of a drug trafficking organization, this paper contributes to the study of extralegal institutions of governance. One vein in this literature argues that Mafia-like groups offer informal, but essential governing mechanisms for people who cannot rely on formal public institutions. The emergence of criminal organizations as governing gap-fillers often coincides with major changes in the political landscape. The Sicilian Mafia, for example, surfaced to protect property after land reforms and the end of feudalism led to increases in the number of land owners in late 19th century Sicily (Bandiera 2003; Gambetta 1993; Skaperdas 2001). Russian racketeering gangs evolved into powerful organizations during the collapse of the Soviet state. When the Soviet government failed to provide governance, gangs began to do so (Volkov 2000; see also Varese 2005, 2011). In the United States, gangs provide governance in illicit markets where people cannot rely on government protection (Sobel and Osoba 2009; Skarbek 2011).[2]

[1] In criminology, past work on drug traffickers focuses on network analysis explanations rather than internal governance institutions, and this work does not examine Mexican drug traffickers (Natarajan 2000; Klerks 2001; Kenney 2007).

[2] Just as traditional political bodies require mechanisms for facilitating internal cooperation and decision-making, criminal organizations must create internal governance institutions (Levitt and Venkatesh 2000; Leeson 2007, 2009a, 2010; Leeson and Skarbek 2010).

The second vein within the literature on unusual institutions of governance focuses on religion and superstition. As will be discussed below, an important component of LFM's institutions of internal governance is its use of religious indoctrination. Historically, superstition played an important role in aligning incentives and eliciting cooperation. Communities used religious and superstitious beliefs to determine a person's guilt (Leeson 2012b). In Liberia, where the formal legal system does not effectively meet many citizens' needs, the people turned to "trial by poison" to elicit information about one's culpability (Leeson and Coyne 2012). Medieval monastic communities used religious curses to protect themselves and their property from powerful neighbors (Leeson 2012a).[3] These institutions of governance appear irrational from the contemporary perspective, but each particular case was an efficient response to the need for governance. In the same way, LFM's bizarre actions are an efficient way to produce governance, given the group's unique context and constraints.

For criminal organizations to provide governance, they must solve the organizational and strategic problems of internal and external cooperation. Building on James Buchanan's (1965) pioneering work in public choice, research on radical religious groups finds that club goods provide the inducement that facilitates internal cooperation (Berman 2009).[4] They also impose large costs that screen out prospective members who are less loyal (Iannaccone 1992; Berman 2000; Munger 2006). We use these insights to explain LFM's internal mechanisms.

[3] In addition to drawing on superstition and religion, governance institutions have also used physical battles between individuals to adjudicate disputes efficiently. These operated as an all-pay auction that allocated a resource to the person who valued it most highly (Hillman and Samet 1987; Leeson 2011).

[4] Related work examines the similarities and differences between public and private action in the context of crime and punishment (Leeson 2009b; D'Amico 2010).

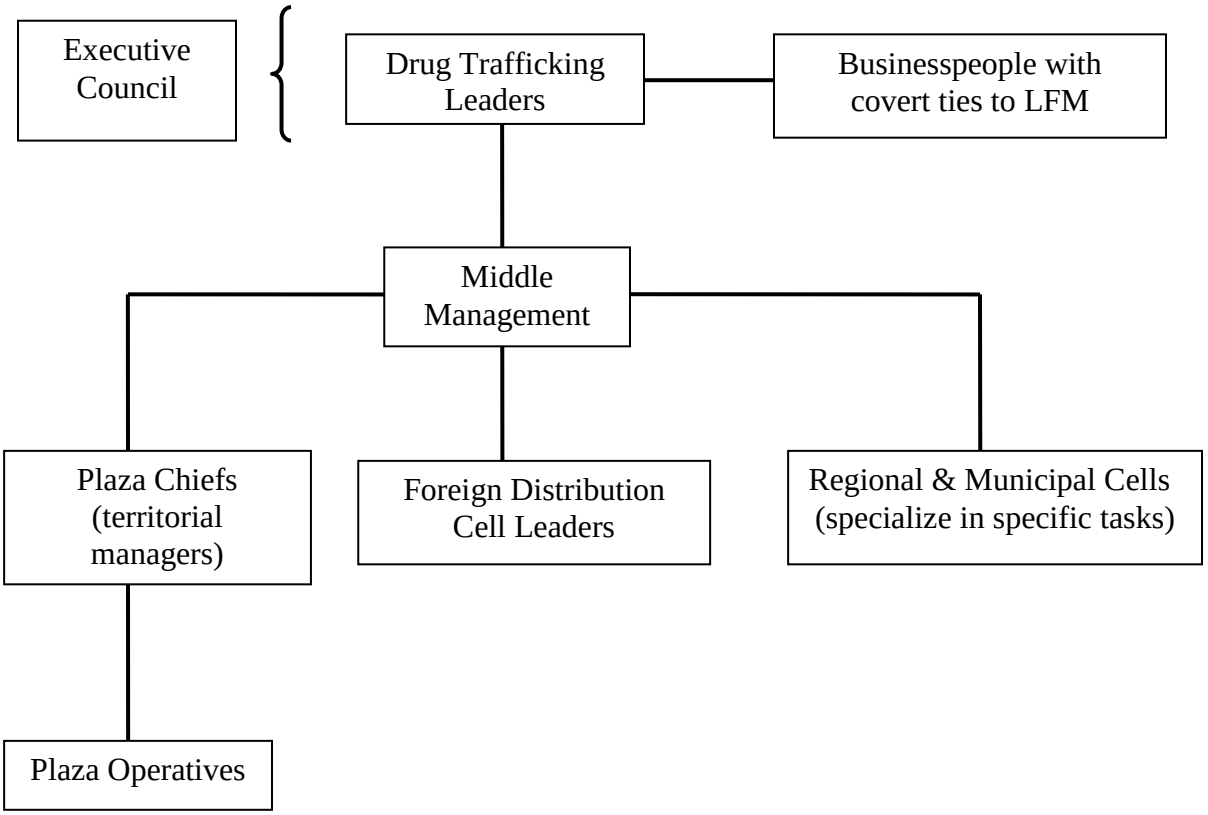
2. Organizational overview

In the past two decades, LFM grew from a small community organization into one of the most prominent drug trafficking organizations (DTOs) in Mexico. In the early 2000s, LFM grew more powerful and broke away from two allied DTOs (Drug Enforcement Administration 2009a; Grayson 2010: 14). LFM expanded rapidly, enlarging its operations into other areas of Mexico and eventually the United States (Grayson 2010: 21-22; Drug Enforcement Administration 2009a). In 2009, LFM became one of only three DTOs identified as "significant foreign narcotics traffickers" by President Barack Obama under the Foreign Narcotics Kingpin Designation Act (Stolberg 2009: A12).

LFM engages in the production and trafficking of methamphetamines, cocaine, heroin, and marijuana (Grayson 2010: 48). Though calculating the size of illicit drug markets is difficult, drug-money seizures suggest that is a lucrative business (Reuter 1997). In one instance, the United States Drug Enforcement Administration recovered $33 million from LFM operatives (Drug Enforcement Administration 2009b). A federal grand jury indictment reveals that a single subgroup within LFM generated more than $10 million in drug revenue (United States v. Ayala-German et al. 2009). A confidential source claims that the organization earns hundreds of millions of dollars annually (Grayson 2010: 49).

LFM also participates in extortion, kidnapping, and legitimate business ventures. Many local businesses in the Michoacán region must pay the organization for protection services. A timber business, for example, closed when it was unable to make its $600 monthly extortion payment (Grayson 2010: 49). LFM demanded five-figure ransoms by kidnapping Mexican family members of American immigrants (Knight 2010). The organization also owns a number of restaurants, nightclubs, and convenience stores in Michoacán (Grayson 2010: 52).

Figure 1: The organizational structure of La Familia Michoacana



As illustrated in Figure 1, the structure of the organization is headed by an executive council comprised of legitimate businessmen and drug traffickers (Drug Enforcement Administration 2009a). Middle management coordinates the executive council's orders. They direct foreign distribution cells as well as regional and municipal cells. These groups perform specific tasks, including narcotics distribution, extortion, and murder (Grayson 2010: 30). LFM divides its territory into plazas, each of which is controlled by a plaza chief (Grayson 2010: 59). A plaza operator works for the plaza chief as an enforcer (Grayson 2010: 59; see also United States v. Chaves-Salgado et al. 2010).

The inability to rely on formal legal institutions of governance creates a problem for illicit organizations. Mainstream institutions of governance provide the foundation for flourishing markets

(Dixit 2009). The government not only withholds access to formal institutions of governance, it also actively disrupts LFM's business enterprises. The violence that results from the drug war alienates DTOs from local communities. This gives the community a stronger incentive to cooperate with government agencies. Without the community's tolerance, criminal organizations operate less effectively (Akerlof and Yellen 1994). Additionally, DTOs must find a way to prevent their own members from defecting. Acts of defection by gang members include stealing drugs, not performing assigned duties, and becoming government informants. With the Mexican government offering $2 million for information leading to the arrest of top LFM leaders, individual members have an incentive to defect (Olson 2009). To be successful, therefore, LFM must devise mechanisms to prevent defection and to promote cooperation from the community.

3. The governance mechanisms of *La Familia Michoacana*

3.1. Internal cooperation

LFM utilizes several governance mechanisms to facilitate cooperation internally. First, LFM promotes a strong religious culture within the organization. It uses an intense indoctrination process to instill loyalty in new members. New recruits, who are often poor and have substance abuse problems, are forced to cleanse themselves of any drug or alcohol addiction (Grayson 2010: 38). Once sober, they begin an intensive six- to eight-week education program. The program includes periodic vows of silence aimed at fostering "spiritual concentration" (Grayson 2010: 38). Much of the instruction is based upon the teachings of American religious counselor John Eldredge (entirely unaffiliated with LFM) and a catechism called "*Pensamientos de la Familia*" written by LFM leader Nazario Moreno-Gonzalez (Grayson 2010: 38).

The indoctrination process facilitates cooperation by creating ties of loyalty among members and revealing hidden information. The initiation process and membership rules impose costs on a recruit, so they reveal unobservable information about a prospective member's dedication to the group's cause. If a recruit knows personally that he will be loyal, then the entry costs are relatively less costly for him than for a candidate who doubts his commitment. This sorts loyal members ex ante into the organization.

While LFM's prohibitions are costly to members, it supplies members with monetary compensation and club goods. LFM leaders also elicit members' compliance with the promise of promotions and larger future earnings. These benefits encourage cooperative, productive behavior by low-ranking members. The group also provides ongoing benefits—many are club goods—that members cannot obtain from outside of the group. Protection is an important type of club good that members enjoy. The group safeguards members and their families from local criminals, including robbers and rapists. Knowledge of an LFM affiliation deters victimization. LFM also provides a variety of other benefits to members. It supplies the neglected youth of Michoacan chances to rise above poverty and drug addiction to become parts of something they consider important. The organization's name itself, La Familia ("the family" in Spanish) exemplifies the appeal of the organization. While a drug dealer might face social stigma or ostracism from kin, LFM provides a new family to take its place—with the added benefits of money, power and in many circles, a reputation as a member of an influential organization.

As a member is promoted up the ranks of the organization, he faces a stronger incentive to defect. Because he learns more about the organization and has more responsibility in carrying out operations, he can receive greater compensation for informing to the government or rival gangs. New and more important information about the organization is more useful to the authorities, so it increases the authorities' willingness to pay. To address this greater risk of defection, LFM excludes members from protection and the other benefits of membership if they do defect.

In addition to the threat of excluding members from group benefits, LFM facilitates internal cooperation with the threat of violence.[5] Like many criminal organizations (Leeson and Skarbek 2010), LFM has a strict code of conduct that members must abide by, and it punishes harshly violations of the code. Although the content of the code is not available publicly in its entirety (Associated Press 2011), some information exists about the consequences of disobedience. Punishments are commensurate with a person's history of code violations. A first infraction results in a beating, a second infraction receives a more severe beating, and a third infraction is grounds for execution (Grayson 2010: 40). Exit opportunities for members are equally grave; the rules state: "whoever leaves La Familia dies" (Grayson 2010: 40-41). Thus, incentives for members to defect are met with strong counter-incentives to cooperate both through threatened exclusion from membership benefits and violent retaliation.

Politicians also play a role in helping LFM, and they too face an incentive to defect. Transforming a potential enemy into a covert ally helps LFM to function free of government interference. Politicians bring substantial benefits to the organization, and LFM supplies strong financial incentives to cooperate. While it is unclear how much LFM compensates politicians, one informant claims that the organization gives $155,000 to political candidates, and a $15,000 stipend if they win, provided they allow LFM to continue its operations within their jurisdiction (Grayson 2010: 63). In addition, politicians, as high-wage earners, face a higher opportunity costs of contributing to the production of the LFM's club goods and they also benefit less from membership. This means that they are more likely to defect than people with fewer outside opportunities (Berman and Laitin 2008: 1954). LFM limits control and information about the group from politicians, some of its most skilled conspirators, because club goods elicit full cooperation only from low wage earners.

[5] The ability to use violence is a distinguishing characteristic of criminal organizations and has important implications for their organizations (Leeson and Rogers 2012).

3.2. Eliciting cooperation from non-members

LFM also faces the threat of social repercussions from the community. The community has an incentive to resist LFM as the group becomes more integrated within the community. In addition to the potential for drug-related violence, DTOs often extort local businesses, leading to lower informal sector wages (Dell 2011). To elicit cooperation from members of the community, the organization produces private and public goods for them. LFM creates an image of itself as a positive member of the community. LFM's mission statement reflects the organization's aim of presenting itself as working to make Michoacán better. Having allegedly begun as an answer to kidnappings and drug dealing in Michoacán, LFM states that the organizational goal is to:

> Eradicate from the state of Michoacán kidnapping, extortion in person and by telephone, paid assassinations, express kidnapping, tractor-trailer and auto theft, [and] home robberies done by people like those mentioned, who have made the state of Michoacán an unsafe place. Our sole motive is that we love our state and are no longer willing to see our people's dignity trampled on. (Grayson 2010: 35)

In one of its first public proclamations, LFM wrote in a newspaper advertisement that "Some of our strategies are strong but this is the only way to impose order for the good of the people. Maybe some people won't understand at first, but they will" (Tuckman 2009: 16). Though LFM engages in activities like drug dealing and kidnapping in Michoacán, the organization attempts to dispel charges of engaging in these crimes, suggesting that their perpetrators were outsiders, rather than locals or LFM members (Grayson 2010: 47).

LFM goes to great lengths to demonstrate the value it adds to the community. LFM promotes an image of being guardians of Michoacán by punishing criminals who rape, rob, corrupt youth, and engage in other detestable crimes (Grayson 2010: 35). In one instance, men in Zamora were seen walking around shirtless, showing that their backs had been whipped severely. They held placards declaring their guilt as thieves and rapists (Grayson 2010: 36). These incidents depict LFM as an

organization committed to making Michoacán a better place, rather than as a criminal organization that victimizes the community.

LFM promotes itself as a model of religious piety and an economic benefactor with an attitude that has been described as a "Robin Hood-type mentality—steal from the rich and give to the poor" (Logan and Sullivan 2009: 1). Exemplifying its religiosity, LFM passes out bibles and money to the poor and engages new recruits in a highly religious indoctrination process (Drug Enforcement Administration 2009a; Grayson 2010: 37-40). Demonstrating its generosity, LFM donates a portion of its income to fund schools, drainage projects, and churches (Gibbs 2009). They provide loans to community members at lower interest rates than local banks (Rodriguez 2009). Both LFM's religious work and its charitable donations benefit the local community and enable the organization to carry out its operations with less local resistance.

LFM also reduces community resistance with threats of violence. With LFM's high-profile presence in Michoacán, it is unsafe for politicians to speak out against the organization's illegal activities. Explaining the extent to which politicians fear LFM, Fabiola Alanis, head of the Democratic Revolution Party in Michoacán, said: "If we know or hear that a candidate is mixed up with *narcos,* we are not going to denounce it. It is not my job. It would put my candidates in danger. There is nothing to guarantee that they would wake up alive" (Wilkinson 2009: 1). Indeed, there are many examples of politicians being murdered by LFM for refusing to cooperate with the organization, such as congressional candidate Gustavo Bucio Rodriguez or former mayor of Lazaro Cardenas, Nicolas Leon, both of whom were shot and killed by LFM in April 2009 (Wilkinson 2009). LFM's ability to intimidate politicians serves as a powerful reminder to the community that nobody is safe to resist them, not even the most heavily guarded politicians. In this way, the community is not only enticed to cooperate with

LFM in order to receive the benefits of private goods and local public goods, but they are also dissuaded from turning against the organization for fear of violence.

4. Conclusion

LFM faces cooperation problems that threaten its ability to operate effectively. These problems come primarily from two groups: the organization's members and the community. The organization uses several mechanisms to promote loyalty and discourage defection. Costly religious prohibitions and initiation processes allow the organization to identify prospective members who are most likely to remain loyal. Financial incentives and club goods are given to members who remain loyal. Violence is used against defectors. To elicit cooperation from the community, the organization provides protection to certain members of the community, produces local public goods, provides charitable funds, and punishes perpetrators of violent crime. The need to prevent defection explains many puzzling aspects of LFM's organization, including why the group makes it so costly for recruits to join, why a criminal group produces public goods, and why some of its most skilled members play minor operational roles.

Past research has demonstrated that illicit trade does not necessarily cause violence (Reuter 2009; Snyder and Duran-Martinez 2009). Rather, violence associated with organized crime is often a result of the political climate (Bailey and Taylor 2009; Villareal 2002). In the case of LFM, the reduction of state-sponsored protection rackets, the increase in local democratic elections, and the presence of conditions favorable to insurgency have cultivated a violence-ridden economy (Snyder and Duran-Martinez 2009; Villareal 2002; Fearon and Laitin 2003). The presence of drug trafficking organization-led violence signals the compromising of the state's monopoly on coercion and its ability to provide governance. Though previous research explains why violence has been so rampant in the Mexican drug market, it has been unclear how DTOs have continued their operations successfully in the

midst of such violence, or why they produce some regional law and order. This article demonstrates how the internal organization and operation of LFM allow it to function effectively in the extralegal sphere.

This conclusion has two implications for the future study of violence as it relates to cooperation problems, organized crime, and political corruption. First, the presence of widespread violence in a market does not necessarily preclude cooperation within criminal organizations. In fact, visible violence can allow an organization to issue credible threats of violence to both internal and external defectors. Second, the inability of the state to provide governance provides an avenue for criminal organizations to provide such institutions in exchange for cooperation from the community. If LFM can prevent defection by providing protection, then public policies that increases people's safety will weaken the organization. If the state can provide citizens with local public goods (including healthcare services) and protection, then LFM will have greater diffculty gaining their cooperation.

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