Leadership presents a puzzle for traditional economic theories of organizations. The theory of the firm recognizes advantages to centralizing authority through the facilitation of rule-based and delegated decision making. However, the benefits of centralized authority do not address the specific contributions leaders make when they exercise their decision rights. Put differently, if effective leadership within a hierarchy is simply a function of institutionally defining and constraining a given leader’s authority, why does it matter which specific individual is at the top of the hierarchy? Nonetheless, the importance of leadership searches on the part of private and public organizations, as well as the compensation for these roles, indicates that specific individuals matter for downstream contingencies. We develop a property rights/transaction costs theory of leadership, and use the economic logic of agency and coordination costs to test the effect of changes in leadership in private and public organizations.

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