

Summary of Paper: [Do CEO Implicit Incentives Affect Strategic Effort Reduction? Evidence from CEO Origin and Career Horizon](#)

What is this study about?

This study examines whether CEOs strategically reduce effort when strong performance could lead to more challenging future performance targets, a phenomenon known as the ratchet effect. Using data from 270 S&P 1,500 companies between 2012 and 2020 (1,491 firm-year observations and 5,928 firm-quarter observations), the researcher investigates how two sources of implicit incentives—CEO origin (externally hired versus internally promoted) and career horizon (distance from retirement)—influence CEOs' willingness to reduce effort near year-end. The analysis focuses on earnings per share (EPS) targets commonly used in executive compensation plans.

What are the major findings of the study?

The study finds clear evidence of target ratcheting: firms often raise future EPS targets when current targets are exceeded. CEOs appear to respond strategically to these incentives. When performance during the first three quarters substantially exceeds targets, some CEOs reduce effort in the fourth quarter to avoid triggering tougher future goals. However, this behavior is less pronounced among externally recruited CEOs and CEOs nearing retirement. The findings also show that the ratchet effect is stronger when a larger portion of executive compensation is tied to achieving EPS targets.

Why is the study important?

The findings are highly relevant to boards, compensation committees, management accountants, auditors, and regulators involved in designing and evaluating performance measurement systems. The research demonstrates that performance targets can create unintended incentives that influence managerial behavior. Understanding how CEO characteristics affect these responses can help organizations design more effective compensation and target-setting practices.

What is the impact on professional practice and society at large?

The study highlights the importance of balancing motivation and accountability when setting executive performance targets. Poorly designed targets may discourage sustained effort and long-term value creation. For shareholders and boards, the findings suggest that career concerns

and job-security incentives can significantly shape executive decisions. Better-designed incentive systems can improve corporate governance, align management actions with organizational goals, and support stronger long-term performance.