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Tariffs and Incentive Pay: Assessing the Impact on Annual and Long-Term Incentive Payouts

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On April 2, 2025, referred to as "Liberation Day," the Trump Administration announced a universal 10% tariff on all imported goods. In addition, the Administration imposed country-specific "reciprocal tariffs" on 57 nations, bringing total tariff rates to as high as 50% for certain trading partners. Major manufacturing hubs that account for a significant share of U.S. imports, including China, Vietnam, and India, were among the most significantly impacted, with certain categories of goods from these countries subject to materially higher effective tariff rates depending on industry and product type.

Background

Tariffs are commonly used as a policy tool to protect domestic industries, encourage local production, address perceived trade imbalances, and generate government revenue. In this case, the tariffs were also intended to incentivize companies to shift supply chains and manufacturing back to the United States or to countries with more favorable trade relationships. However, such shifts are often complex, time-consuming, and costly to implement.

These tariffs effectively functioned as a tax on imported goods, increasing input costs and compressing profit margins for companies that rely on overseas manufacturing or foreign-sourced materials. For example, companies importing consumer electronics or industrial components from China faced higher input costs, while apparel and footwear companies sourcing from Vietnam experienced margin pressure due to increased duties. Similarly, manufacturers reliant on raw materials or intermediate goods from India and other affected countries saw cost structures shift unexpectedly.

In response, some companies passed these higher costs on to customers through price increases, while others absorbed the impact, resulting in reduced profitability. Tariffs also disrupted established supply chains, forcing companies to reevaluate sourcing strategies, often at higher cost and with added operational complexity.

Importantly, these developments had direct implications on executive compensation. When companies established performance goals for their executives' annual and long-term incentive plans in early 2025 or 2023 or 2024 for 3-year long-term incentive plans, the scope and magnitude of these tariffs were not anticipated. As a result, many incentive targets, both short-term and long-term, were set based on financial expectations that did not reflect this significant macroeconomic shift, with potential implications not only for annual payouts but also for performance measurement over multi-year performance cycles.

Approach

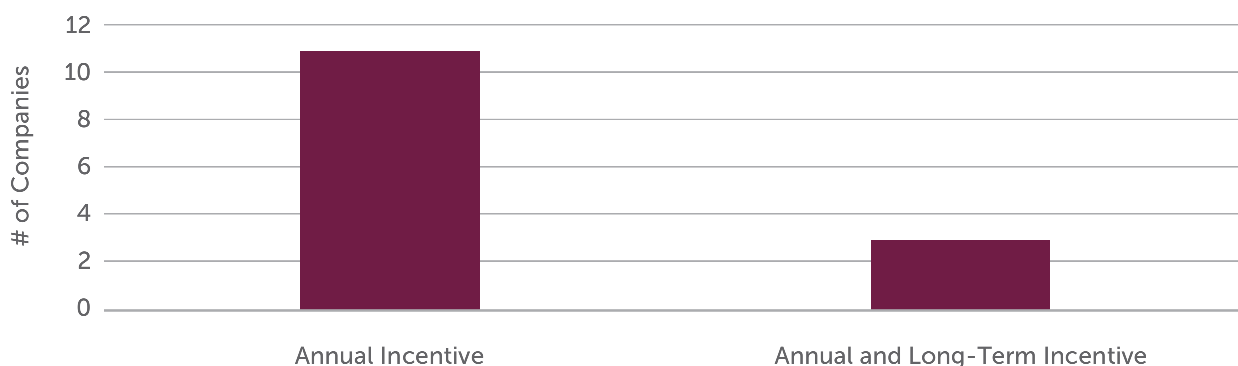
Given the potential for tariffs to distort financial performance and complicate pay-for-performance alignment, as companies file their 2026 proxy statements, CAP reviewed disclosures related to goal setting and payout outcomes to assess whether and how tariffs affected compensation decisions. Our analysis focused on 2023-2025 long-term incentive plan and 2025 annual incentive payouts. CAP selected a sample of 22 companies, focusing on those most exposed to tariffs due to their reliance on imported goods, overseas manufacturing, and global supply chains.

To conduct this research, we selected companies based on their exposure to tariffs and reliance on global supply chains. Specifically, we focused on companies that depend heavily on imported goods, manufacture products overseas, or source key materials from countries most affected by tariffs, such as China, Vietnam, and India. We also prioritized industries where tariffs were likely to have a direct and material financial impact, including industrials, consumer goods, and manufacturing. This approach enabled us to better understand how tariff-related disruptions influenced both business performance and compensation outcomes.

Our findings are based on proxy filings available as of April 17, 2026.

Key Findings

Of the 22 companies reviewed, 11 (50 percent) did not reference tariffs in their proxy statements. Of the remaining 11 companies (50 percent), 8 disclosed an impact on their annual incentive (AI) plan, while 3 disclosed impacts on both annual and long-term incentive (LTI) plan payouts. Therefore, 8 out of 22 companies (36 percent) made adjustments to annual and/or long-term incentive payouts.

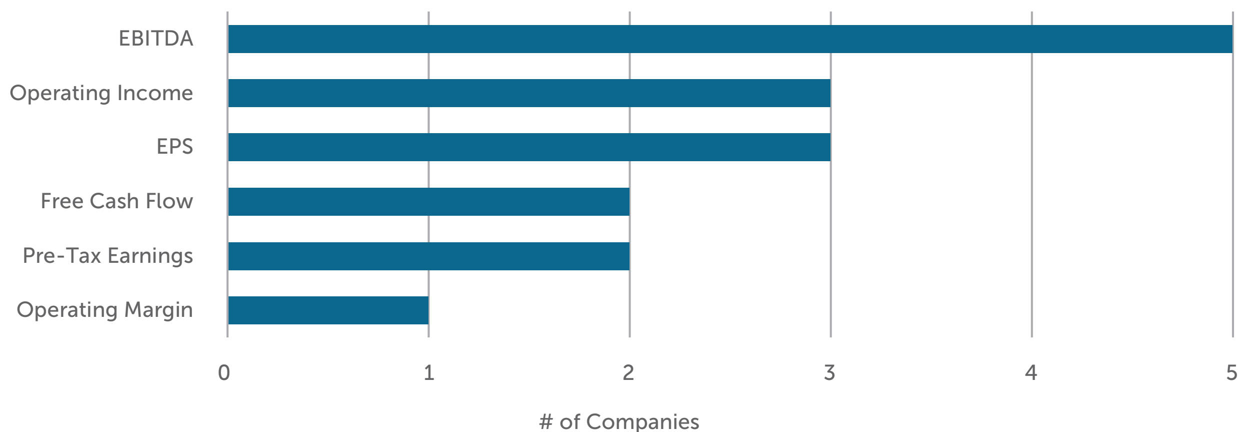


Across these disclosures, a consistent narrative emerged: performance goals for both AI and LTI plans had been established prior to the implementation of tariffs. Once tariffs were introduced, companies experienced a period of volatility during ongoing negotiations between the Trump Administration and the impacted countries. As a result, many companies characterized the negative financial impact as an unforeseen, extraordinary event and applied upward adjustments to incentive plan payouts.

Among the companies that did address tariffs and impact on financial performance, larger companies (Ford, PepsiCo, Pfizer) generally did not disclose any impact on their annual or long-term incentive plans. This likely reflects the greater scale, diversification, and cost absorption capacity of larger companies, which can mitigate tariff impacts through pricing, sourcing, and operational flexibility. In contrast, smaller companies are often more directly affected by such cost pressures, making them more likely to disclose and adjust incentive plans. For Pfizer, no adjustments were likely made due to a voluntary agreement with the U.S. government to lower prescription drug prices and align them with other developed markets, which provided a three-year exemption from certain tariffs.

The impact on payouts were disclosed as adjustments to their plan payouts in percentage points. In comparing annual versus long-term incentive plan adjustments, ICU Medical was the only company to disclose a quantitative adjustment to its long-term incentive plan, applying an upward adjustment of +50% to the payout percentage. Adjustments were more common for annual incentive plans, with reported increases ranging from +6% to +43% of the actual payout. Among the seven companies that disclosed a specific adjustment, the median increase was +13%, and the average was +12% to the actual payout.

Finally, companies adjusted annual and long-term incentive plans in different ways. Of the eleven companies that made adjustments, 5 companies modified adjusted EBITDA to exclude all or a portion of the tariff expense to increase incentive plan payouts. In addition, three companies adjusted multiple performance metrics rather than a single measure. These results are illustrated in the chart below.



Based on this review, we observed that the introduction of tariffs created a meaningful disconnect between predetermined incentive targets and actual company operating performance. This dynamic raises important questions about the integrity of pay-for-performance alignment, specifically, whether executives should be rewarded or penalized for outcomes driven by external factors largely outside of management's control. More broadly, the tariffs reflect a significant shift in U.S. trade policy away from decades of relatively free trade toward a more protectionist framework, introducing a new layer of structural uncertainty that companies must navigate.

Eight companies did not discuss tariffs in their proxy statements, despite being large organizations that we expected to be impacted, including Amazon, Archer Daniels Midland, CVS, Hasbro, Johnson & Johnson, Mattel, Merck & Co., and Wayfair.

The policy environment surrounding tariffs has also remained fluid. Subsequent legal challenges, including a Supreme Court ruling, have questioned aspects of the tariffs' implementation, creating more uncertainty for companies as they assess both operational and financial impacts.

Rationale for Adjustments or No Adjustments

When adjustments are made, the rationale is that tariffs are external, unpredictable shocks that were not included in the original target setting process, so adjusting helps isolate true operational performance and ensures executives are evaluated and compensated based on factors within their control. Adjustments also prevent key financial metrics such as EBIT, EBITDA, Free Cash Flow, and EPS from being distorted and help maintain a consistent pay-for-performance framework.

The rationale for partial/no adjustments includes:

- Ensuring performance metrics do not fully exclude real economic impacts of tariffs on profitability
- Maintaining accountability for management's response to tariff pressures
- Avoiding overstatement of performance by fully removing a real cost
- Preserving credibility with shareholders and consistency in reporting

Examples:

Company	Adjustment	Rational
Ford	No	Did not exclude tariff costs and instead included them in adjusted EBIT, treating tariffs as part of normal operating performance
RTX	Yes	Stated that tariff impacts should be "neutralized" for performance purposes because they are external, unpredictable, and unrelated to operational execution
Westinghouse Air Brake Technologies	Yes	Applied a partial adjustment to avoid understating performance due to external tariff headwinds, while still holding management accountable for overall business outcomes
Sylvamo	Yes	Added back only a portion of tariff costs because tariffs affected result but were still treated as real economic costs, not fully excluded
YETI	Yes	Treated tariffs as an "unforeseen extraordinary event" and recalculated performance to reflect true performance for incentive purposes

Looking Ahead

Companies are likely to continue adopting hybrid approaches to tariff treatment, with a growing emphasis on partial and rule-based adjustments rather than fully excluding or fully including tariff impacts. The evidence suggests companies will increasingly distinguish between anticipated tariffs, which are treated as normal economic costs, and unforeseen or newly imposed tariffs, which may be adjusted out using predefined mechanisms such as cutoff dates or specific cost factors. This reflects an effort to balance fairness in performance evaluation with accountability for real business outcomes, while also enhancing transparency and consistency in incentive design. As tariff volatility persists, companies are expected to formalize these practices further, embedding clearer guidelines into incentive plans to ensure that performance metrics remain both economically meaningful and aligned with shareholder value creation.

An additional emerging consideration is the potential for tariff refunds in 2026. The Supreme Court ruled that the tariffs imposed under the International Emergency Economic Powers Act (IEEPA) were unlawful, but it did not determine whether companies must be reimbursed for tariffs already paid. Many companies have filed lawsuits seeking relief and the Trump administration is expected to begin a refund process shortly. Assuming refunds are ultimately issued, they could create a one-time increase in reported profits, potentially inflating incentive payouts. As a result, companies will need to evaluate whether and how to adjust performance metrics to exclude or normalize the impact of such refunds, ensuring that executive compensation reflects underlying operating performance rather than a one-time boost.

APPENDIX

Companies Disclosing the Impact of Tariffs (n=14)

Company	Adjustment	Amount	Detail
Ford Motor Company Industry: Automobile Manufacturers Revenue ($mms): $187,267	None	0%	Adjusted EBIT Margin is the financial metric used in the AI plan. Ford generated $6.8B of adjusted EBIT for the year. This includes a net $2B tariff impact
PepsiCo, Inc. Industry: Soft Drinks and Non-Alcoholic Beverages Revenue ($mms): $95,449	None	0%	Given the cumulative impacts of inflationary pressures and tariffs on consumer budgets, the CEO of PepsiCo North America faced substandard organic revenue performance
RTX Corporation Industry: Aerospace and Defense Revenue ($mms): $88,603	AI and LTI	n/d	RTX noted that changes in laws and regulations impacting tariffs should be neutralized for AI plan performance purposes and performance share unit purposes, because they are externally imposed, unpredictable and unrelated to operational execution
Pfizer Inc. Industry: Pharmaceuticals Revenue ($mms): $62,579	None	0%	Pfizer reached a voluntary agreement with the U.S. government, supporting efforts to lower prescription drug costs and align prices with those in other developed countries. This removed uncertainties by providing greater clarity on pricing and a three-year grace period from certain U.S. tariffs
Ross Stores, Inc. Industry: Apparel Retail Revenue ($mms): $22,751	AI and LTI	n/d	Given the potential for tariff-related costs to drive reported results in ways that might distort underlying business performance, the Compensation Committee approved a defined set of cost factors as an additional adjustment to pre-tax earnings, designed with the intention to isolate tariff-related costs when evaluating performance relative to the established incentive goals
Becton, Dickinson and Company Industry: Health Care Equipment Revenue ($mms): $21,924	AI	+10%	Increased the corporate funding factor by +4% to reflect partial offset of tariff impact on financial metrics and credit management for its tariff exposure mitigation efforts. The company also increased corporate funding factor by +6% to adjust for tariff impact on gross margin percentage
The Gap, Inc. Industry: Apparel Retail Revenue ($mms): $15,366	AI	n/d	Adjusted the actual percentage achieved for their annual incentive plan to account for items that were not considered when goals was set, which included the impact of tariffs not considered when the company set its annual budget
Westinghouse Air Brake Technologies Corporation Industry: Construction Machinery and Heavy Transportation Equipment Revenue ($mms): $11,167	AI	+14.7%	The Compensation and Talent Management Committee determined that a partial impact of tariff-related headwinds should be considered in calculating financial performance for the purposes of annual incentive compensation. The impact of this adjustment increased annual incentive payouts for the named executive officers from 178.1% to 192.8%

Sylvamo Corporation Industry: Paper Products Revenue ($mms): $3,351	AI	+5.8%	The company faced a challenging business environment. Both price and mix were unfavorable due to the new tariff rules that impacted global trade flows. As a result, actual performance achievement for Adjusted EBITDA Margin was below target performance, while Free Cash Flow failed to achieve threshold performance. The Compensation Committee approved an Adjusted EBITDA Margin of 13.7%, which included an adjustment to add back $18 million in direct tariff impacts
ICU Medical, Inc. Industry: Health Care Supplies Revenue ($mms): $2,231	AI	+27.2%	The Adjusted EBITDA and Free Cash Flow results were adjusted by $4 million out of the $26 million of incremental tariff expense recognized and by $18 million of the incremental $30 million of incremental tariffs paid by the company during 2025, respectively
	LTI	+50.0%	
Callaway Golf Company Industry: Leisure Products Revenue ($mms): $2,060	AI	+5.8%	Solely for purposes of calculating compensation under the annual incentive plan, Adjusted EBITDA was adjusted to remove the impacts of tariffs implemented after January 20, 2025
YETI Holdings, Inc. Industry: Leisure Products Revenue ($mms): $1,868	AI	+42.6%	The Compensation Committee determined that the imposition of tariffs, together with the uncertainty surrounding the implementation and subsequent renegotiation of these tariffs, was an unforeseen extraordinary event that had a material impact on 2025 financial performance for incentive plan purposes. As a result, the Committee adjusted Operating Income by approximately $38 million to account for the net negative impact of tariffs, resulting in a 71.0% payout percentage.
Integra LifeSciences Holdings Corporation Industry: Health Care Equipment Revenue ($mms): $1,635	AI	+13.3%	After the tariffs were implemented, the Compensation Committee determined applying a limited, one-time tariff adjustment was appropriate to ensure incentive outcomes fairly reflected management's performance in navigating these external conditions. Absent the tariff adjustment, actual financial results under the annual cash bonus plan would have fallen below the adjusted EBITDA gate [resulting in 0% payout]
MGP Ingredients, Inc. Industry: Distillers and Vintners Revenue ($mms): $536	AI	n/d	The Committee approved further adjustments to Adjusted Operating Income and Adjusted EBITDA of $1.6 million and Adjusted Basic EPS of $0.05 related to tariff impacts that were not reasonably predictable at the time the targeted achievement levels were originally approved

Companies That Did Not Discuss the Impact of Tariffs (n=8)

Company	Revenue ($mms)	Industry
Amazon	$716,924	Broadline Retail
CVS Health Corporation	$399,834	Health Care Services
Johnson & Johnson	$96,362	Pharmaceuticals
Archer-Daniels-Midland Company	$80,269	Agricultural Products and Services
Merck & Co., Inc.	$65,011	Pharmaceuticals
Wayfair Inc.	$12,457	Home Furnishing Retail
Mattel, Inc.	$5,348	Leisure Products
Hasbro, Inc.	$4,701	Leisure Products