



MEMO

Date: January 13, 2006
To: Board of Directors
From: Tom Schrader
Subject: 2006 Variable Compensation Plan

Issue for the ERCOT Board of Directors

ERCOT Board of Director Meeting Date: January 17, 2006

Agenda Item No.: 15c

Issue:

Approval of the Variable Compensation Plan (applicable to ERCOT officers, directors and managers) for calendar year 2006.

Background/History:

At its regular meeting on February 16, 2005, the Board approved a Variable Compensation Plan for ERCOT officers, directors and managers, subject to the finding of the Mercer compensation study and confirmation that the plan would not be inconsistent with the Mercer study's finding. The Plan ties performance based pay to achievement of ERCOT's seven primary corporate goals. At its December 13, 2005 meeting, the Board reviewed and approved the possible percentage awards in the 2005 Variable Compensation Plan. The issue now before the Board is whether a Variable Compensation Plan and the associated set of ERCOT goals should be approved for use in 2006.

Consistent with the 2005 Plan, the Variable Compensation Plan for 2006 conditions performance compensation upon the achievement of corporate and individual goals and objectives. The Board has approval authority over the goals and measures used to assess performance and over the payout budget that will be determined after the end of the fiscal year. ERCOT management will be responsible for managing the program within the Board-approved budget amount, and the Board will retain authority to adjust Variable Compensation Plan payouts on a corporate or individual basis.

Key Factors Influencing Issue:

1. The considerable effort and initiative required of officers, directors, and managers to achieve the corporate goals of ERCOT.
2. The need to ensure competitive total compensation to attract and retain key talent.
3. The value of providing meaningful incentives for excellence in job performance.
4. The possible perception by some third parties that performance-based compensation is not appropriate for ERCOT employees.



MEMO

5. The 2006 Variable Compensation Plan is an improved version of the previously-approved 2005 Plan.
6. Mercer study findings support the ERCOT Variable Compensation Plan structure. Mercer results indicate that over 80% of employers in their data base have variable pay programs for management and executives at the same or greater average target percentages as contained in the ERCOT Variable Compensation Plan.

Alternatives:

1. Approve a Variable Compensation Plan and associated goals for 2006, as recommended by the H.R. & Governance Committee or as modified by the Board.
2. Do not have a Variable Compensation Plan for 2006.

Conclusion/Recommendation:

The H.R. & Governance Committee will make its final recommendation regarding the 2006 Variable Compensation Plan during the January 17, 2006 Board meeting.



MEMO

Attachment A

RESOLUTION OF THE BOARD OF DIRECTORS OF ELECTRIC RELIABILITY COUNCIL OF TEXAS, INC.

January 17, 2006

WHEREAS, the Board of Directors (“the Board”) of the Electric Reliability Council of Texas, Inc. (the “Company” or “ERCOT”) deems it desirable and in the best interests of the Company that there be a Variable Compensation Plan for certain ERCOT employees; and

WHEREAS, in February 2005 the Board approved a Variable Compensation Plan for ERCOT officers, directors and managers for 2005, subject to the findings of the Mercer compensation study and confirmation that the Variable Compensation Plan would not be inconsistent with the Mercer study’s findings; and

WHEREAS, in December 2005, the Board reviewed and approved the possible percentage awards in the 2005 Variable Compensation Plan, after determining that they were consistent with the Mercer study’s findings; and

WHEREAS, the 2006 Variable Compensation Plan is an improved version of the previously-approved 2005 plan; and

WHEREAS, the results of the Mercer study indicate that over 80% of employers in the Mercer study’s data base have variable pay programs for management and executives at the same or greater average target percentages as contained in the 2006 ERCOT Variable Compensation Plan; and

WHEREAS, adoption of the 2006 Variable Compensation Plan would allow recognition of ERCOT employees who expend considerable effort and initiative to achieve ERCOT’s corporate goals, would help ensure ERCOT’s ability to attract and retain key talent, and would provide meaningful incentives for excellence in job performance by ERCOT employees.

NOW, THEREFORE, BE IT RESOLVED, that the Board hereby approves the 2006 Variable Compensation Plan and associated goals, as recommended by the H.R. & Governance Committee during the January 17, 2006 Board meeting.