
THIRD READING

Bill No: SB 1174
Author: Valladares (R)
Introduced: 2/18/26
Vote: 21

SENATE TRANSPORTATION COMMITTEE: 12-0, 4/7/26

AYES: Cortese, Strickland, Archuleta, Arreguín, Blakespear, Gonzalez, Grayson, Menjivar, Richardson, Seyarto, Valladares, Wiener

NO VOTE RECORDED: Dahle

SENATE JUDICIARY COMMITTEE: 13-0, 4/21/26

AYES: Umberg, Niello, Allen, Ashby, Caballero, Durazo, Laird, Reyes, Stern, Valladares, Wahab, Weber Pierson, Wiener

SENATE APPROPRIATIONS COMMITTEE: 7-0, 5/14/26

AYES: Cervantes, Seyarto, Cabaldon, Dahle, Grayson, Richardson, Wahab

SUBJECT: Public contracts: Department of Transportation: bid preferences: employee stock ownership plans

SOURCE: California Employee Ownership Coalition

DIGEST: This bill requires the State Department of Transportation (Caltrans) to provide certain bid preferences to a contractor with an employee stock ownership plan (ESOP) that bids on a state-funded construction contract, as specified.

ANALYSIS:

Existing law:

- 1) Establishes Caltrans and provides the Department with various powers and duties, including but not limited to, planning, designing, constructing, operating, and maintaining the State's highway system, as specified.

- 2) Authorizes Caltrans to enter into any contracts required for the performance of its duties, as provided.
- 3) Establishes bid preferences in public contracting for certain types of bidders, including, but not limited to, small business and microbusiness bidders.

This bill:

- 1) Requires Caltrans, on or after January 1, 2028, to provide certain bid preferences to a contractor with an ESOP that bids on a state-funded construction project, as specified.
- 2) Provides various definitions as they pertain to the provisions specified in this bill.
- 3) Specifically, requires Caltrans to provide a bid preference to qualified contractors for state-funded construction contracts, as follows:
 - a) Two percent to a qualified contractor with 30 to 49 percent of the entity owned by its ESOP.
 - b) Three percent to a qualified contractor with 50 to 99 percent of the entity owned by its ESOP.
 - c) Four percent to a qualified contractor with 100 percent of the entity owned by its ESOP.
 - d) An additional one percent for qualified contractors that include employees covered by a collective bargaining agreement or master labor agreement.
- 4) Specifies that the bid preference shall not be awarded to a noncompliant bidder and shall not be used to achieve any applicable minimum requirements.
- 5) Provides that it is unlawful for a person or contractor to willfully or knowingly carry out a number of actions pertaining to fraud, providing false statements, and / or impeding an investigation of qualifications as an ESOP contractor, as specified.
- 6) Imposes a variety of civil penalty fines for a person or contractor who is found in violation of the abovementioned actions, as specified.

- 7) In addition to civil penalty fines, a person or contractor who is found in violation of the abovementioned actions is required to be suspended from bidding or participating as either a contractor, subcontractor, or supplier, in any contract or project for Caltrans for a period between one month to one year, as specified.
- 8) Prohibits Caltrans from entering a contract with a person or contractor suspended for one of the abovementioned violations during the period of suspension, as specified.

Comments

- 1) *Purpose of this bill.* According to the author, “California law establishes several programs that provide preferences to several classes of businesses on public works construction. Those programs, however, are fundamentally flawed. They only assess the owners of those businesses which, in some cases, could only be one person. SB 1174 proposes a more equitable wealth distribution compared to other construction procurement preferences for construction contracting. One way to do that, which the legislature has recognized through the passage of AB 2849 (Bonta) and SB 1407 (Becker) both from 2022, is the promotion of employee-owned businesses. Government Code Section 12100.31(c) perfectly explains the benefits of those entities:

“Employees becoming owners would create opportunities for wealth-building and community stability. It would also help California create a more inclusive, equitable, and stable economy, supported by the studies of employee-owned businesses and their success and resiliency during the Great Recession and the COVID-19 pandemic.

“The most efficient way to achieve California’s policy objective, that is, to diversify ownership to a broader population, is to incentivize shared ownership through employee stock ownership plans (ESOPs). Rather than requiring each qualified individual to start up their own enterprise, this strategy would allow existing owners to extend ownership rights to employees via grants of stock through ESOP accounts, a process separate from the employee’s compensation. Given the current demographic breakdown of the California workforce on public infrastructure projects as documented by Caltrans in the 2024 Disparity Study, these Plans would directly distribute ownership to the intended populations on a much broader and more inclusive scale than existing policies. According to the study, 65.8% of California construction workers during the

period of 2018 to 2022 were people of color. Modelled after California's Small Business Enterprise and Disabled Veterans Business Enterprise programs, SB 1174, as proposed to be amended, establishes a scaled bid preference for construction companies that operate an ESOP program. This will build wealth for construction workers.”

- 2) *Employee stock ownership plan.* Ultimately, an ESOP is a retirement plan, in some ways similar to and governed by the same laws and regulations as a 401k plan, which provides a company's workforce with an ownership interest in the company. To establish an ESOP, a firm forms a trust that purchases the shares of a company from the owner and allocates the shares to employees as part of their compensation. ESOP shares are part of an employee's remuneration for work performed. Shares are allocated to employees and may be held in an ESOP trust until the employee retires or leaves the company. Once the employee retires or leaves the company, the shares are then either bought back by the company for redistribution or voided.

Most private U.S. companies operating as an ESOP are structured as S Corporations. S Corporations are corporations that elect to pass corporate income, losses, deductions, and credits through to their shareholders for federal tax purposes. Shareholders of S corporations report the flow-through of income and losses on their personal tax returns and are assessed tax at their individual income tax rates. According to the IRS, to qualify for S corporation status, the corporation must meet a number of requirements, including being a domestic corporation and have no more than 100 shareholders.

- 3) *Caltrans' contracting.* Caltrans has in place utilization goals and bid preferences for certified Disadvantaged Business Enterprises (DBE), Small Businesses (SB), and Disabled Veteran Business Enterprise (DVBE) when soliciting state contracts. Certified Small Businesses and DVBE can receive a 5% bid preference on applicable state solicitations. Additionally, Caltrans has established utilization goals of 25% for SBs, 5% for DVBEs, and 22.2% for DBEs.

The contractor certification process is managed by the Department of General Services (DGS). For example, in order to obtain certification as a small business for public works contracts, a company must meet the following requirements:

- Be independently owned and operated;

- Not dominant in field of operation;
- Principal office located in California;
- Owners, Officers, Members/Managers, Partners must be domiciled in California;
- Average annual gross receipts of forty-three million dollars (\$43,000,000) or less over the previous three (3) tax years, as biennially adjusted in accordance with Government Code section 14837, subdivision (d)(3). If the business or its affiliate(s) has been in existence for less than three (3) tax years, then the GAR will be based upon the number of years in existence; and,
- A business with 200 or fewer employees (including affiliates).

The provisions specified in this bill attempt to align ESOP companies with a similar bid preference structure afforded to SBs and DVBEs. The author points to ESOP construction companies as businesses that provide more equitable wealth distribution for its employees in comparison to its DBE, SB, DVBE counterparts that are currently eligible for bid preferences. As a result, the author and sponsors of this bill claim that by offering similar bid preferences for ESOP companies, these companies will be incentivized to grow and in turn, provide greater financial opportunities for its shareholder employees. On the other hand, it's important to note that providing a 2%-5% bid preference for ESOP construction companies may lead to increase project costs for Caltrans. However, at this time, as the total number of ESOP construction companies that may participate if this measure were to go into effect is unknown, an approximation of the fiscal impact is unclear.

- 4) *Federal Regulations*. It's important to note that on October 3, 2025, the United States Department of Transportation (U.S. DOT) issued an Interim Final Rule (IFR), which took immediate effect revising / modifying DBE eligibility for state transportation programs. The IFR removes race- and sex-based presumptions from the definition of "socially and economically disadvantaged individual" as it pertains to DBE eligibility. Instead, majority owner(s) must now demonstrate on a case-by-case basis that the individual meets the criteria described in federal regulations (i.e. 49 CFR Section 26.671) to qualify as a DBE. Caltrans has informed current DBE eligible businesses, per federal law,

that they must reapply for DBE eligibility with Caltrans and be reevaluated under the updated federal criteria. The author asserts that under the updated federal requirements, many businesses may be subject to losing their DBE status and ESOPs may serve as a viable alternative.

FISCAL EFFECT: Appropriation: No Fiscal Com.: Yes Local: No

According to the Senate Appropriations Committee:

- Unknown one-time and ongoing costs to Caltrans, likely in the hundreds of thousands of dollars annually, to update internal contracting guidance and processes and the Contract Administration & Tracking System II, and to conduct ongoing compliance monitoring activities on state-funded construction contracts. (State Highway Account)
- Unknown potentially significant increased state contracting costs, to the extent awarding contracts to ESOP bidders reduces competition in the bid pool and results in higher contracting costs (Various transportation special funds, federal funds). Actual increases in project costs will vary and depend on, among other things, the number of eligible ESOP contractors, frequency of use, and the cost of the contracts awarded. Staff notes that this bill would cover all state-funded construction contracts for programs administered by Caltrans.

SUPPORT: (Verified 5/14/26)

California Employee Ownership Coalition (Sponsor)

Ambrose advisors

Bapko Metal

C. Wells Pipeline Materials INC.

Caltrol, INC.

Couts Heating and Cooling

Employee-owned S Corporations of America

Eureka Capital Partners, LLC

Ggg Demolition, INC.

Griffith Company

Marina Landscape, INC.

Mcguire and Hester

Murray Company

Pavement Coatings Co.

Pavement Recycling Systems

Prs Holdings, INC

Prs Logistics

Riverside Construction Company, INC.
The Esop Association
1,355 Individuals

OPPOSITION: (Verified 5/14/26)

None received

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