

SENATE JUDICIARY COMMITTEE
Senator Thomas Umberg, Chair
2025-2026 Regular Session

SB 1174 (Valladares)
Version: February 18, 2026
Hearing Date: April 21, 2026
Fiscal: Yes
Urgency: No
AM

SUBJECT

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

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.

EXECUTIVE SUMMARY

The author and sponsor of the bill argue that existing preferences for certain types of businesses in state contracting are based on who the owner is instead of how the employees are compensated, such as the disabled veteran enterprise program. This bill would provide for a preference in bidding on CalTrans contracts for a contractor with an ESOP, which is an employee-owned company where employees own part or all shares in a business. The author and sponsor argue that this bill could act as an incentive for construction businesses to convert to ESOPs. The bill's provisions in this Committee's jurisdiction are the civil penalties and enforcement provisions. The bill is sponsored by the California Employee Ownership Coalition and supported by several business entities. No timely opposition was received by the Committee. The bill passed the Senate Transportation Committee on a vote of 12 to 0.

PROPOSED CHANGES TO THE LAW

Existing law:

- 1) Establishes CalTrans with various powers and duties, including but not limited to, planning, designing, constructing, operating, and maintaining the State's highway system, as specified. (Gov. Code § 14001 et seq.)

- 2) Establishes bid preferences in public contracting for certain types of bidders, including, but not limited to, small business, microbusiness, and disabled veteran business enterprise bidders. (Gov. Code § 14835 et seq; Mil. & Vet. Code § 999 et seq.)
- 3) Makes certain legislative findings and declarations of the Legislature under the California Employee Ownership Act, including that 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. (Gov. Code § 12100.31.)

This bill:

- 1) Defines the following terms for purposes of the bill.
 - a) “Contractor” means any person or entity who submits a bid and performs work on a state-funded construction contract.
 - b) “Department” means the Department of Transportation.
 - c) “Employee stock ownership plan” or “ESOP” has the same definition as that term is defined in paragraph (7) of subsection (e) of Section 4975 of the Internal Revenue Code, as that provision read on January 1, 2022.
 - d) “ESOP contractor” means a contractor that presents the following documentation at the time of bid:
 - i. A valid and favorable ESOP determination letter from the Internal Revenue Service.
 - ii. Its most recently filed Internal Revenue Service Form 5500. The department may request any additional schedules associated with the form.
 - iii. An independent review that establishes the percentage of the ESOP contractor that is owned by its ESOP. The independent review shall be performed by an independent accounting firm and shall cover, at minimum, all of the following:
 1. Certification that the review was performed in accordance with standards established by the American Institute of Certified Public Accountants.
 2. Certification that the statements are the representations of management.
 3. Certification that the review consisted of inquiries and analytical procedures that are lesser in scope than those of an audit.
 4. Certification that the accountant is not aware of any material modifications that need to be made to the statements for

them to be in conformity with generally accepted accounting principles.

- 2) Requires CalTrans when it prepares a solicitation for a state-funded construction contract to provide a bid preference to an ESOP contractor.
- 3) Requires the bid preference to be calculated as provided below.
 - a) If 30 to 49 percent, inclusive, of the ESOP contractor is owned by its ESOP, one of the following may apply:
 - i. in solicitations where an award is to be made to the lowest responsible bidder meeting specifications, the preference to the ESOP contractor shall be 2 percent of the lowest responsible bidder meeting specifications; or
 - ii. in solicitations where an award is to be made to the highest scored bidder based on evaluation factors in addition to price, the preference to the ESOP contractor shall be 2 percent of the highest responsible bidder's total score.
 - b) If 50 to 99 percent, inclusive, of the ESOP contractor is owned by its ESOP, one of the following may apply:
 - i. in solicitations where an award is to be made to the lowest responsible bidder meeting specifications, the preference to the ESOP contractor shall be 3 percent of the lowest responsible bidder meeting specifications; or
 - ii. in solicitations where an award is to be made to the highest scored bidder based on evaluation factors in addition to price, the preference to the ESOP contractor shall be 3 percent of the highest responsible bidder's total score.
 - c) If 100 percent of the ESOP contractor is owned by its ESOP, one of the following may apply:
 - i. in solicitations where an award is to be made to the lowest responsible bidder meeting specifications, the preference to the ESOP contractor shall be 4 percent of the lowest responsible bidder meeting specifications; or
 - ii. in solicitations where an award is to be made to the highest scored bidder based on evaluation factors in addition to price, the preference to the ESOP contractor shall be 4 percent of the highest responsible bidder's total score.
 - d) An additional 1 percent to the bid preferences under is to be provided to an ESOP contractor that includes employees covered by a collective bargaining agreement or master labor agreement.
- 4) Requires the bid preference amount in solicitations where an award is to be made to the lowest responsible bidder to be computed by assessing the sum of the percentages above to the ESOP contractor's lowest responsive bid.

- a) The bid preference amount in solicitations where an award is to be made to the highest scored bidder based on evaluation factors in addition to price is to be computed by assessing the sum of the percentages above on the ESOP contractor's highest scored bid. The bid preference shall then be subtracted from the bid. This amount shall be used for bid evaluation purposes.
- 5) Prohibits bid preferences under this bill from being awarded to a noncompliant bidder and it cannot be used to achieve any applicable minimum requirements.
- 6) Makes it unlawful for a person or contractor to do any of the below listed acts.
 - a) Knowingly and with intent to defraud, fraudulently obtain, retain, attempt to obtain or retain, or aid another in fraudulently obtaining or retaining or attempting to obtain or retain, acceptance as an ESOP contractor.
 - b) Willfully and knowingly make a false statement with the intent to defraud, whether by affidavit, report, or other representation, to a state official or employee for the purpose of influencing the acceptance as an ESOP contractor.
 - c) Willfully and knowingly obstruct, impede, or attempt to obstruct or impede, any state official or employee who is investigating the qualifications of a person or contractor that has requested acceptance as an ESOP contractor.
 - d) Knowingly and with intent to defraud, fraudulently obtain, attempt to obtain, or aid another person or contractor in fraudulently obtaining or attempting to obtain, public moneys to which the person is not entitled under this chapter.
 - e) Establish, or cooperate in the establishment of, or exercise control over, a contractor found to have violated any of the provisions in (a) through (d).
- 7) Makes a person who violates any provision of 6)(a) through (d) liable for a civil penalty not to exceed \$5,000 for the first violation, and a civil penalty not to exceed \$20,000 for each additional or subsequent violation.
 - a) A person who violates 6)d) is liable for a civil penalty not to exceed \$50,000 for the first violation and \$200,000 for each additional or subsequent violation. A person or contractor that fails to satisfy this penalty is prohibited from further contracting with CalTrans until the penalties are satisfied.
- 8) Provides that a person or contractor that violates 6) is, in addition to the penalties provided for in 7), to be suspended from bidding on or participating as either a contractor, subcontractor, or supplier, in any contract or project for CalTrans for a period of not less than 30 days nor more than one year. However, for an

additional or subsequent violation, the period of suspension is to be extended for a period of up to three years.

- 9) Requires CalTrans to report an alleged violation to the Attorney General, who is required to determine whether to bring a civil action against any person or contractor for a violation of these provisions.
- 10) Prohibits CalTrans from entering into a contract with a person or contractor suspended for a violation of these provisions during the period of suspension. CalTrans is prohibited from awarding a contract to any contractor using the services of a person or contractor suspended for violating these provisions during the period of the suspension.
- 11) Requires CalTrans to verify that the contractor to whom a contract is being awarded, or a person or contractor being used by that contractor, is not under suspension for violating these provisions.
- 12) Makes these provisions operative on January 1, 2028.

COMMENTS

1. Stated need for the bill

The author writes:

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.¹ 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. This bill seeks to enact an ESOP preference in CalTrans contracts

An employee-owned company is one where employees own part or all of the shares in a business. While the forms of employee ownership may be different (such as stock grants, worker cooperatives, and stock options), the goal is the same: to promote employee ownership in a business. According to the National Center For Employee Ownership, construction is the third most popular industry for ESOP ownership in the U.S. at 16 percent, after manufacturing (21 percent) and professional services (19 percent).² The author and sponsor argue that this bill could act as an incentive for construction businesses to convert to ESOPs, which could lead to diversity of ownership and stronger economic outcomes for employees. They state that this bill furthers the goals of the California Employee Ownership Act, noting that the Legislature stated:

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. (Gov. Code § 12100.31(c).)

The bid preference provisions of this bill are modeled after the ones under the Small Business Enterprise and Disabled Veterans Business Enterprise programs. (Gov. Code § 14835 et seq; Mil. & Vet. Code § 999 et seq.) The civil penalty provisions are modeled off the penalty provisions under the Small Business Enterprise program, though the amounts of the civil penalties in this bill differ from the Small Business Enterprise program. (Gov. Code § 14842.5.) In order to be liable for a civil penalty, the bill requires knowing and willful conduct by a person or contractor and only authorizes the Attorney General to bring an enforcement action.

¹ Cal. Dept. of Trans., *Disparity Study* at p. 4, available at <https://dot.ca.gov/programs/civil-rights/disparity-study>.

² NCEO, *ESOP Breakdowns by Industry 2026 Update*, available at <https://www.esop.org/infographics/esops-by-industry-sector.php>.

3. Stakeholder statements

The California Employee Ownership Coalition, the sponsor of the bill, writes in support stating:

[...] Current law provides for a variety of bid preferences and participation goals for certain types of businesses in public works contracts. They include the Small Business Enterprise (SBE), Disabled Veteran Business Enterprise (DVBE) and Disadvantaged Business Enterprise (DBE) programs. However, current law does not recognize employee-owned companies, despite their demonstrated benefits to workers and communities.

SB 1174 proposes a new type of bid preference that targets companies that operate employee stock ownership plans (ESOPs). Rather than an “independently owned and operated” business, or one owned by investors, companies that operate ESOPs are owned by their employees. This is a unique and expanding business model that gives workers the opportunity to share ownership in their employer.

SB 1174 is a modest step to encourage the development and expansion of ESOPs in California. The bill creates a bid preference, up to maximum of five percent, to ESOP companies that bid on Caltrans construction projects that are 100% state funded. The bid preference is scaled based on the level of ESOP ownership.

The legislature should work to expand and encourage worker ownership because they provide wealth and economic security for workers. In fact, ESOPs in California have distributed an estimated \$11.2 billion in value to their employee-owners. These distributions represent meaningful wealth building outcomes for tens of thousands of California workers. [...]

SUPPORT

California Employee Ownership Coalition (sponsor)

AmbroseAdvisors

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

OPPOSITION

None received

RELATED LEGISLATION

Pending Legislation: None known.

Prior Legislation:

SB 713 (Valladares, 2025) would have required the Director of General Services to issue an ESOP contractor certificate to a qualified contractor that presents a valid and favorable ESOP determination letter from the Internal Revenue Service, as provided. SB 713 died in the Senate Appropriations Committee.

SB 1407 (Becker, Ch. 733, Stats. 2022) established the California Employee Ownership Program, within Office of Small Business Administration.

AB 2849 (Bonta, Ch. 808, Stats. 2022) established a panel o conduct a study regarding the creation of an Association of Cooperative Labor Contractors for the purpose of facilitating the growth of democratically run high-road cooperative labor contractors, as provided.

SB 553 (Wilk, 2019) would have required an entity awarding a contract pursuant to the State Contract Act to provide a 3 percent bid preference to a qualified ESOP bidder, as defined. SB 553 failed passage in the Senate Governmental Organization Committee.

PRIOR VOTES

Senate Transportation Committee (Ayes 12, Noes 0)
