PART 6: STATE REVENUES AND DEVOLUTION

Authors

Jeff Davis
Senior Fellow and Editor, Eno Transportation Weekly
Eno Center for Transportation

Rebecca Higgins
Vice President of Policy
Eno Center for Transportation

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Part 6: State Revenues and Devolution

The Federal-aid highway system today is federally-assisted and state-administered; similarly, transit agencies receive federal funding, and the local agencies select and deliver projects, and operate the assets supported by those funds. With federal assistance comes a bevy of federal requirements, notably compliance with regulations that affect procurement, domestic content, design and engineering specifications, location choices, environmental mitigation, and other outcomes. The federal program structure also sets constraints for state and local agencies. For instance, the total amount of each state's apportionments for highway programs versus transit is set by law, as are program levels within each mode. These laws determine the amounts available for various project types (although at this point there is a fair amount of flexibility to transfer funding between programs and modes).

History of the Federal Programs

The original 1956 highway law more than tripled annual funding levels for the Federal-aid highway program and provided that, after the construction of the new, 41,000-mile system of divided, limited-access Interstate highways was completed, the Highway Trust Fund would be abolished, and Federal-aid funding and related taxes be reduced back to their pre-1956 levels. Whether or not this outcome was the actual intent of the authors of the 1956 law, they at least wanted to ensure that future Congresses would have to debate the issue of whether or not to extend a super-sized Federal-Aid Highway Program, post-Interstate.

Congress has consistently extended the authorization of the Highway Trust Fund starting in 1970, but there have also consistently been voices arguing to devolve the federal collection and distribution of funding for transportation. Devolution proposals would repeal (or more often reduce) the federal HTF revenues measures and prompt states to replace that federal funding with alternative state revenue measures. Devolving the funding would enable states to also avoid the regulatory compliance costs and legal constraints imposed by the federal programs.

In the 1980s, the U.S. Advisory Commission on Intergovernmental Relations (USACIR) critically examined the potential to devolve the highway and transit programs. With 97 percent of Interstate system already complete and the majority of costs for the uncompleted portions associated with projects that lacked national significance per CBO, USACIR recommended devolution of the highway and transit programs.[1] Many of the findings of the USACIR report still appear relevant. "Simultaneous devolution of a federal responsibility to states and localities along with the relinquishment of a federal revenue base to finance that responsibility" would help to stabilize the financing of highways according to the report. Moreover, "with state and

local governments freed from federal requirements, some of which are unsuitable and expensive, turnbacks offer the possibility of more flexible, more efficient, and more responsive financing of those roads that are of predominantly state or local concern. Investment in highways could be matched more closely to travel demand and to the benefits received by the communities served by those roads."[2]

Throughout the years, Members of Congress have proposed devolution in stand-alone bills and as amendments to surface transportation laws. Such proposals have typically taken one of two forms. One model of devolution is based on the recommendations of USACIR: reduce federal excise taxes, allow states to opt to raise those taxes instead, and limit federal activity to core federal functions (such as roads on federally-owned lands and, possibly, maintaining key standards on the Interstates). The Transportation Empowerment Act of 1996, introduced by Representative John Kasich (R-OH) and Senator Connie Mack (R-FL), was the first legislative proposal of this form.[3] The second form of devolution is structured as an opt-out option for states paired with the rebating of HTF contributions to states that choose to opt-out. This idea was first introduced by Senator Kay Bailey Hutchinson (R-TX) in the Highway Fairness and Reform Act of 2009.[4]

In the short-term, devolution would not be an immediate no-cost solution to Highway Trust Fund shortfalls. As noted in Part 3, there is a buildup of outstanding obligations from the HTF for which the federal government is already legally responsible.[i] Between the $86 billion of obligated balances and the $44 billion in unobligated spending that was previously authorized, the USDOT authority would likely face the need to defray a total of $130 billion of unpaid bills at some point in the future. The current HTF balance of $74 billion would cover a portion of this, leaving $54 billion in additional future revenue needed to cover USDOT's legal obligations. In other words, Congress could devolve and zero out the current programs but would need to extend current HTF taxes for another eighteen months, post-devolution, in order to raise the requisite funds. Since most states would need to increase their own tax revenues immediately, this could result in a period of double taxation which could be difficult for elected officials to explain and justify. Alternatively, a devolution plan could provide yet another transfer from general revenues in order to pay off validly incurred federal obligations from the pre-devolution days.

Serious consideration of devolution would also require Congress to determine which functions require a federal role, whether there is a continued need for federal

[i] Specifically, as of August 2025, USDOT had a total of $86 billion in outstanding HTF obligations of funds made available by the IIJA and previous acts ($66.7 billion for the highway account and $17.4 billion for the mass transit account and approximately another billion each from National Highway Traffic Safety Administration (NHTSA) and the Federal Motor Carrier Safety Administration (FMCSA)).

standards, and how to fund NHTSA and FMCSA, which both receive funding from the Highway Trust Fund.

Despite these questions and obstacles, there may be real benefits of a new conversation on devolution as a means of improving the relationship between transportation improvements and the communities they serve. Federal funds support a range of activities that are not inherently federal in nature. While they still predominantly fund large-scale capital improvements on the National Highway System, many of the community projects may be more appropriately funded at the state and local level. Moreover, the federal program priorities may push states toward expansion projects versus maintenance work.

It is also difficult for national standards to adjust to different geographic conditions and land-use patterns. Inflexible federal design standards have led to roads with overly large rights of way, increasing land acquisition and construction costs and creating unique challenges in dense environments. As the USACIR report noted, "the design standards in federal law or regulations… can force the construction of a road that is more costly because it is built to a higher level than is needed or justifiable in terms of budget priorities."[5]

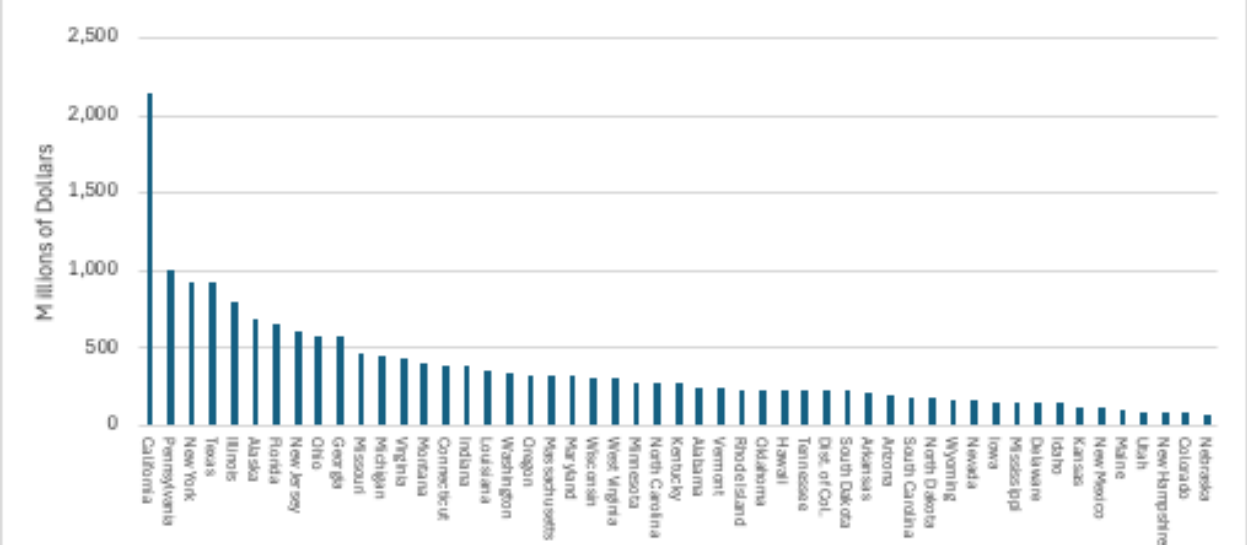
Relieved of costs for compliance with Davis-Bacon, the Brooks Act, Buy America, and other engineering, design, and contracting requirements, states may see their transportation funding go further on each project. Importantly though, devolution would only relieve compliance from requirements that are tied to the USDOT funding action; other federal laws and regulations would continue to apply to projects, such as the Endangered Species Act, the Migratory Bird Treaty Act, the Clean Air Act, the Clean Water Act, and the Rivers and Harbors Act.

Most importantly, any reduction in compliance costs is unlikely to make up the difference between the current levels of revenues versus spending. Collectively across all states, the amount of new highway formula funding received by states in fiscal 2023 exceeded their tax payments into the HTF highway account by $18.7 billion. To the extent that states and transit agencies want to continue to spend approximately the amount that they receive in federal apportionments, devolution alone will not solve the issue of funding shortfalls. State and local governments would have to either increase state and local taxes by an amount larger than the reduction in federal taxes that residents paid, or choose to reduce their transportation spending.

As an added complication, the relationship between state apportionments and their contributions to the Highway Trust Fund varies widely. For FY2023, the State of Alaska received 8.73 times more in highway apportionments than they paid to the highway account, the District of Columbia received 12.46 times more, and Vermont received 4.67 times their payment. At the "low" end, Texas received just 121 percent

of their highway account payment, and Colorado received only 112 percent. On a dollar basis the "overpayment" to states beyond their contribution to the highway account ranged from $2.1 billion in California and $1.0 billion in Pennsylvania, downwards to $71 million in Nebraska. In other words, the amount that a state would need to raise to replace the full amount of their individual apportionment would also vary widely. Under devolution, some states might choose to spend less on transit than they contribute to the HTF mass transit account, but state transit apportionments exceed contributions to the transit account by even greater percentages. States may also face challenges in cutting transit spending—only five states reported directing no state or local highway user revenues toward mass transit in 2023.

Figure 11: FY 2023 Federal Highway Formula Apportionments in Excess of that State's FY 2023 HTF-HA Tax Contributions



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State Revenue Options

Under devolution, new State taxes would need to exceed federal rates to fully replace federal funding, but on the other hand, State and local governments agencies seeking to replace federal funds would face some advantages in raising those revenues. There is a wider range of revenue options that are feasible and sometimes more politically palatable for State and local governments despite being impracticable, cost prohibitive, unpopular, or unconstitutional at the Federal level. State revenues broadly fit into three categories: Indirect user fees, direct user fees, and monetization.

Indirect user fees

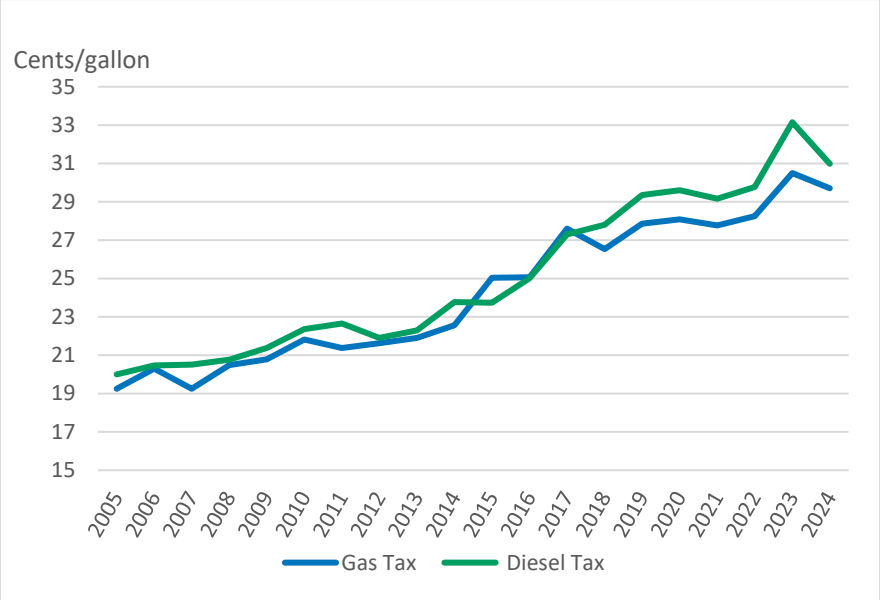
Indirect user fees use proxies to approximate the level of use of transportation assets. While these proxies may not always accurately gauge use of the asset, indirect user fees typically have the benefit of fairly low administrative costs. Motor fuel taxes and registration fees are both indirect user fees that together represent the majority of state transportation revenues.

Motor Fuel Taxes

Every state today levies a tax on both gasoline and diesel for on-roadway uses. These taxes are most often levied as a per gallon tax, while others are structured as sales taxes, and typically taxes are collected at the point of sale. (This is different from the federal excise tax that is collected at the rack and therefore technically a tax on wholesale fuel distributors rather than consumers.) While prohibited in many states, some states such as Nevada and Hawaii also allow localities to collect fuel taxes.

State fuel taxes today range from a high of 70.9 cents per gallon in California, to a low of 8 cents per gallon in Alaska, with an average of approximately 30 cents per gallon across all states. While Congress has not increased the rate of Federal motor fuel taxes that fund that Highway Trust Fund since 1993, most states have done so. In the 15 years from 2008 through 2023, the gasoline tax rate stayed flat or was reduced in just 13 states, and in only 11 states for diesel taxes. The remaining states and the District of Columbia increased their gasoline tax rate by an average of 50%, and their diesel tax rate by 53%.

Figure 12: Average State Fuel Tax Rate

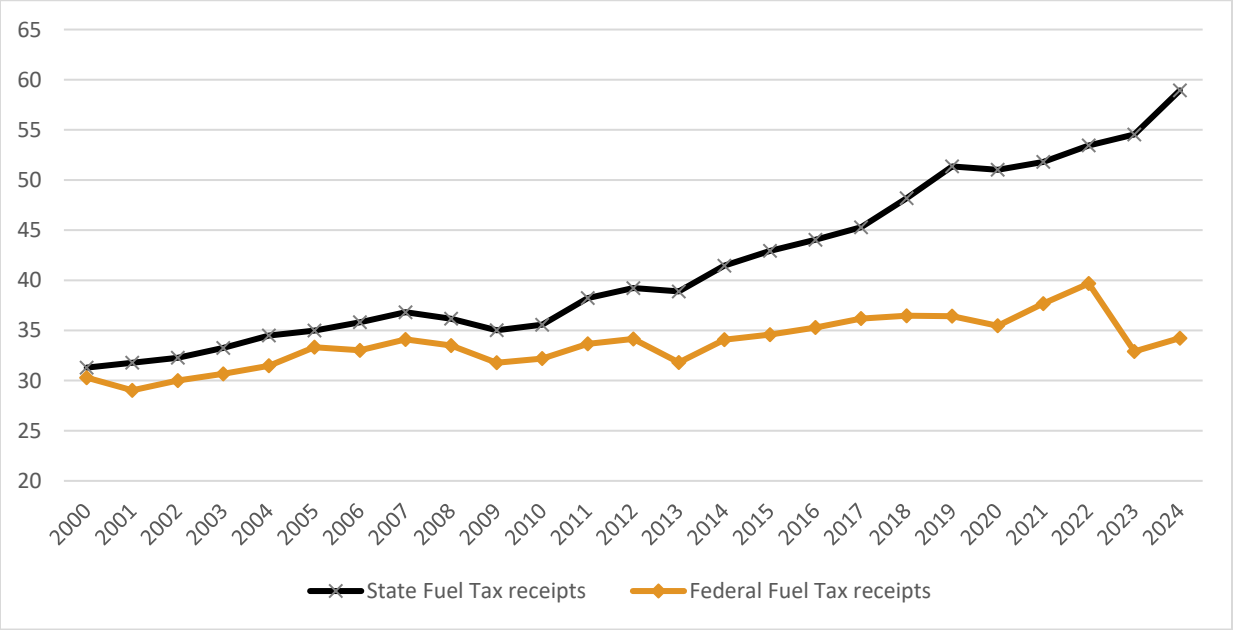


Source: FHWA Highway statistics Table MF-201

This greater willingness of states to increase motor fuel taxes is apparent in the data on total fuel tax receipts at the state versus federal level, as shown in the table below. In the year 2000, state and federal motor fuel tax revenues were approximately equivalent, but since then states motor fuel tax receipts increased by 74% while in the same period Federal motor fuel taxes receipts grew by just 9%.

Figure 13: State v Federal Fuel Tax Receipts

Billions of dollars



Source: FHWA Highway Statistics Tables MF-1 and FE-210

Despite the increases in state gas tax rates, this revenue is declining as a percentage of overall transportation budgets, which speaks to the range of other viable revenue options available to states.[ii] While Federal motor fuel taxes represent about 91 percent of the revenues deposited into the HTF, gas tax revenue contributes just 36% of state transportation revenue.

- Title, Registration, and Licensing Fees

As part of their vehicle titling and registration requirements, state transportation agencies or departments of motor vehicles (DMV) typically charge fees to the vehicle owner. This may include title fees, which are typically charged just once at the point of purchase, as well as registration fees or license plate fees, which are often charged annually. The fee structures and amounts vary widely between states and the revenues from these fees are not necessarily dedicated to transportation spending in

[ii] Based on fiscal year 2024 data from the National Association of State Budget Officers, gas tax revenue has declined as a percentage of state transportation revenue from 41.1% in 2018 to 35.9% in 2024.

all states. However, unlike the Federal government, which has no annual interaction with vehicle owners, State DMVs have an existing collection mechanism that could easily be built upon with little additional collections costs.

States use revenues from vehicle taxes, registrations, and licensing fees for both transportation uses and non-transportation uses. FHWA data on the revenues from motor vehicle registrations and taxes that are used as transportation spending accounted for $36.4 billion in 2023.[6] This category of spending has grown in the last several decades both in nominal amounts and as a percentage of highway user revenues that are collected. In 2000, the $15.5 billion collected for registration fees and vehicle taxes represented 32 percent of highway-user revenue, but in 2023 the category accounts for 38 percent of highway user revenues. In fact in 20 states, the revenues from these motor vehicle and motor carrier taxes exceed the revenues from motor fuel taxes.

- Electric and Hybrid Fees

With the growing number of electric and hybrid vehicles on the roadways contributing less or not at all to state motor fuel tax revenues for transportation, many states have opted to impose additional fees on electric and hybrid vehicles. According to data from the National Conference of State Legislatures, 40 states plus the District of Columbia have fees on EVs, typically in addition to the traditional motor vehicle registration fee. Some of these are structured as flat fees and some are tied to gross vehicle weight categories. Fees range from $50 per year in South Dakota, Hawaii, and Colorado, to $200 or more in 12 states, with an average of approximately $150 per year. Hybrid vehicles, though they represent a much larger share of vehicles, face additional registration fees in 34 states and the majority of those fees are $100 or less, with an average of $75/year.[7]

Direct User Fees

Direct user fees for roadways offer the significant benefit of creating a direct relationship between use of an asset and payment for that use however the costs of tracking that usage and collecting associated fees tend to be high. Tolling is the direct user fee that is used most widely; VMT fees and congestion fees have been piloted or implemented in more limited locations in the U.S.

- Tolling

Despite being predominantly prohibited on federally funded roads since the creation of the Highway Trust Fund, state and local collection of tolls on roads, bridges, tunnels resulted in approximately $22 billion in revenue in 2023.[8] The prohibition on tolling has little basis in federalism, and the number of exemptions have grown to allow tolling in most cases for new, reconstructed or replaced roads, bridges, and tunnels. Paired with the previously grandfathered toll roads, most major road projects at this point could be financed with a combination of toll and public private

partnerships or bonds. Devolution and removal of the tolling prohibition would enable the imposition of tolls on existing roads without reconstructing them first.

There are examples of toll roads where traffic volumes were inadequate to cover the costs of project construction. However this would not be an issue for tolls imposed on existing roadways, unconnected with any reconstruction work, as could happen if the prohibition were removed to fully allow tolling.

One challenge for tolling that would remain an impediment is the inefficient cost of collection for tolling compared to fuel tax collection. A 2007 study from the Transportation Research Board estimated that toll collection costs range from 16.5% to 92.6% of the amount collected, while also acknowledging significant data gaps.[9] The expanded use of electronic transponders has reduced collection costs but a Congressional Research Service study in 2017 indicated that the costs still range from 8% to 13% of revenues collected.[10]

- VMT Fees

As noted in Section 4, Vehicle Miles Traveled (VMT) fees have been considered an area of potential promise for transportation revenues, and numerous states have studied and piloted this revenue option, with support from the Surface Transportation System Funding Alternatives Program established in the FAST Act. VMT fees at the state level are not without challenges. Pilot programs evaluating implementation of VMT fees at the state level have found impediments in the costs of administering VMT fees and the need for coordination and collection mechanisms to address cross-state travel. According to the Government Accountability Office, State DOT officials noted that costs include start-up costs, operating costs, and the cost of developing and implementing enforcement mechanisms for mileage fee systems.[11] On the other hand, the challenges may be easier to over at the state level compared to a federal VMT. Many states have pre-existing systems for conducting inspections and collecting registration fees that can help to reduce the costs of collecting VMT fees.

Four states currently operate VMT fee programs: Oregon, Utah, Virginia, and Hawaii. Although all four programs are currently voluntary, with participants allowed opt to pay fixed fees instead, Hawaii plans to make its program mandatory beginning in 2028 for all EVs and for all passenger vehicles in 2033.[12] Hawaii has not yet set the fee amount or structure for the post-2033 VMT, but estimates that they would achieve revenue neutrality with existing fuel tax collections through a VMT fee of about 0.8 cents per mile. In the states currently operating fees, the price per mile ranges from 0.8 cents to two cents per mile.

- Congestion Pricing

Congestion pricing charges drivers for driving in specified networks during specified times. This can take the form of a fee that corresponds to the number of miles driven

in that network or can be imposed as a cordon price, e.g. a flat fee to enter the priced network. The first real implementation of congestion pricing in the U.S. has used the cordon price approach rather than a VMT approach. In New York City, the newly launched Central Business District Tolling Program produced an average of $56 million per month in revenue over the first nine months of implementation.[13]

Implementation of congestion pricing in Manhattan benefits from the density of vehicles entering and exiting the central business district and the geography that limits the number of entrance and exit points; these factors make congestion pricing more cost-efficient than it might be in many places. Congestion pricing also requires significant capital investment into tolling infrastructure and has operational and enforcement costs. In New York, MTA allocated more than $427 million to plan and build the congestion pricing infrastructure and entered a contract for $556 million over 6 years for a toll operator to install, operate, and maintain the infrastructure.[14]

Monetizing Assets

A final category of state revenues includes a range of activities that seek to capture the value of existing assets or planned improvements.

- ### Value Capture and TIFs

State and local treasuries can use value capture techniques to monetize the value produced by a transportation investment. Through this technique, the increases in land values and business activity that usually follow transportation improvements can help defray the costs of those investments more directly. Value capture can be achieved through tax increment financing (TIF), through which an increment of additional property or other tax is levied on properties within a special assessment district, the revenues of which are used to finance eligible projects. Other approaches include imposition of developer fees and business improvement districts, or transportation user fees assessed on residents and businesses based on estimates of trips they generate.

- ### Right of Way Activity: Concessions, EV Charging, and Truck Parking

Although States own fairly extensive right-of-way assets, federal law prohibits states from pursuing commercial activity at their rest areas and other assets that would otherwise be a potential source of revenue. Reversing the statutory ban would enable States to receive concession revenues for providing commercial services, e.g. fuel and charging, food, and even lodging at Interstate rest areas.

The commercialization of rest areas have significant revenue potential. For instance in Delaware, a welcome center constructed as a public private partnership guarantees a contractual minimum annual revenue of $1.6 million to the State's Transportation Trust Fund, and actual revenues from concessions produced $2.4 million in FY24.[15] In contrast, in states that lack the ability to commercialize rest

areas, the maintenance is a net expense, which has led to closure of some state rest areas.

In addition to revenue potential, commercializing rest areas offers solutions to several policy challenges states now face. For one, improved truck driver compliance with Hours of Service regulations as a result of Electronic Logging Devices has exacerbated shortages of truck parking. While the shortage of truck parking constitutes a safety concern, and State DOTs have the authority to construct free parking for truck drivers, the commercial activity ban limits the financial viability of the public investment. Similarly, removing the ban on commercial activity would improve the ability of States to fill gaps in the EV charging network.

Additional State Revenues

States also fund transportation with revenues not associated with transportation usage or investments, including sales and income taxes. Many States also use tax-exempt bonds to pay for transportation investments. Imposing new state revenues could provide states with an opportunity to issue new bonds against the future state revenues. Note, if states were to make up for the elimination of federal surface transportation funding by issuing more tax-exempt bonds, there would be an impact to the U.S. Treasury losing tax revenue.

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[2] *ibid*

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