Repayment threshold increases for student debt

The income threshold at which student loan repayments begin rose on 6 April 2018.

English and Welsh students who started their courses after 31 August 2012 can now earn £25,000 a year – up from £21,000 – before they have to start repaying their student loans. The increase could provide a saving of £360 a year, with repayment rates at 9%.

Although the change was heralded as good news, that is not the whole story:

- Automatic enrolment pension contributions nearly tripled at the same time. For those earning £29,000 or more, this increase more than wipes out the savings from the repayment threshold increase.
- Interest rates for student loans have not changed. Before graduation, interest remains at RPI + 3% (currently 6.1%, and 6.3% from September 2018). After graduation interest is charged at RPI for those earning up to £25,000, rising on a sliding scale up to RPI + 3% for those earning £45,000 or more.
- As with any loan, lower repayment levels mean a longer payment period. Although student loans are capped at 30 years, after which the debt is written off.
- The Institute for Fiscal Studies estimates that the higher threshold will cost the taxpayer £2.3 billion a year, and that the government will end up writing off about 45% of total student debt.

A basic rate taxpaying graduate who is auto-enrolled in a workplace pension scheme faces an effective marginal 'tax' rate of 43.4% – more than higher rate tax – for every £1 earned above £25,000:

Income tax	20%
National insurance	12%
Auto-enrolment pension contribution (net)	2.4%
Student loan repayment	9%
TOTAL	**43.4%**

Once the higher rate tax threshold is reached, the effective marginal rate becomes 51%. The savings from lower national insurance contributions, and earnings over the auto-enrolment threshold, are more than lost on extra income tax.

If you have children or grandchildren going to university, these figures are a reminder that it could be wise to start planning university funding. However, it is perhaps better to think of graduation funding, as it may not make sense to pay off the student loan early.

Tax laws can change. The Financial Conduct Authority does not regulate tax advice.