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Bolster your retirement savings by reducing your monthly tax burden

If you earn a monthly salary of R100 000 and you were given a legal and above-board option that would result in a tax saving of R1.8 million over 20 years, would you take it?

Niel Fourie, public policy actuary at the Actuarial Society of South Africa (ASSA), has a solution that can help you achieve exactly that, whilst at the same time significantly bolstering your retirement savings. But there is a caveat: you have to sacrifice a portion of your monthly take home pay.

The good news is, says Fourie, that this solution will work for any salaried taxpayer prepared to sacrifice a portion of their take home pay.

To illustrate this, Fourie crunched the numbers for monthly salaries of R25 000, R50 000 and R100 000.

“Obviously, the higher your pay scale, the more impressive the numbers,” says Fourie.

Take a salary of R100 000 a month. If you are currently contributing 10%, or R10 000, of this salary to a retirement fund, your monthly tax is R28 814. Assuming there are no other deductions, your take home pay is R61 186.

If you had to double your monthly contribution to a retirement fund to R20 000, your tax payable would drop by R4 100 to R24 714 and your take home package to R55 286, a reduction of R5 900. Fourie explains that effectively the Government is now sponsoring R4 100 towards your retirement savings, by reducing your tax rate as an incentive to save more for your retirement.

This tax saving would amount to R49 200 in the first 12 months and to a whopping R1.8 million over 20 years assuming a 6% salary increase every year and tax brackets adjusting accordingly.

Fourie explains that instead of sacrificing this money to taxes, you have effectively grown your retirement savings by at least this amount or more, depending on where you invested your money.

You earn R50 000

If you are currently contributing 10%, or R5 000, to a retirement fund, your monthly tax is R10 683 and your take home pay is R34 317.

If you had to double your monthly contribution to a retirement fund to R10 000, your tax payable would drop by R1 800 and your take home package to R31 117, a reduction of R3 200. In this case Government is sponsoring the additional R1 800 towards your retirement savings.

Over 12 months, your tax saving would amount to R21 600 and over 20 years to R794 568.77.

You earn R 25 000

If you are currently contributing 10%, or R2 500 every month to a retirement fund, your monthly tax is R3 372 and your take home pay is R19 128.

If you had to double your monthly contribution to a retirement fund to R5 000, your tax payable would drop by R650 and your take home package to R17 278, a reduction of R1 850. In this case Government is sponsoring the additional R650 towards your retirement savings.

Over 12 months, your tax saving would amount to R7 800 and over 20 years to R286 927.61.

Sacrifice a little, gain a lot

Fourie says by giving up a portion of your take-home pay, you end up with significant tax savings, which, if invested wisely, could grow into a sizeable nest egg.

"Even though you will be taxed when you start drawing an income in retirement it will most likely be at a lower marginal rate. It is also clear that the more you earn the more compelling the argument to save in a pension fund or a retirement annuity."

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