Three things to know before borrowing retirement account savings

If you're in a situation where you need extra cash now, you may be peeking at all your accounts to see what you can tap. While your retirement savings may seem like a good place to start, here are three important factors to consider before taking money from this account:

1. It's not free money – it's a loan.

When you tap retirement plan savings, you are taking a loan from your account, one you are required to repay. So, before you initiate that loan, be sure you can afford to take the immediate hit to your paycheck and cash flow.

2. Borrowed money is no longer working as hard for you.

Sure, the cash you take out is helping you with some short-term needs. However, at the same time, you lose the long-term growth potential that your money could've had within your retirement account. We're talking about compounding interest, potential dividends, and participation in any growth in the markets – an opportunity lost. You have to weigh whether you can afford the potential long term hit to your savings.

3. Repayment speeds up if you leave your job.

Keep this in mind: The loan repayment period you agree to is only valid as long as you're working with your current employer. Once you leave your employer – by choice or by termination – you must repay the loan in full by your tax filing deadline for that year (including extensions). What happens if you don't? The IRS will treat that loan as a taxable distribution, hitting you with a tax bill on the outstanding amount – plus a 10 percent early-withdrawal penalty. So, be sure you know where you stand with your current employer before you agree to that loan.

Here's the bottom line: Remember these three things before borrowing from your retirement account. Your money is working hardest for you in that account – and borrowing from it comes with some potentially costly strings.

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