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Retirement Plan Loans:

To Borrow or Not to Borrow?

Although you may have the ability to borrow money from your retirement plan in the form of a loan, please proceed with caution! If you borrow from your retirement account, you may end up causing harm to your financial futures.

Below are a few of the drawbacks to taking a loan from your retirement plan:

- **Double-Taxation:**
Unlike retirement plan contributions, repayments for loans are made on an “after-tax” basis. That means that you use dollars that have already been taxed for your loan payments. Then, you pay tax again on your distributions at retirement. Thus, you will pay taxes twice on your loan amount.
- **Loss of Saving**
Most workers that borrow from their retirement plan cannot afford to pay back the loan as well as continue to save in the plan. Thus, they end up only paying back the principal and interest for the loan, and not saving for their future.
- **Loss of Compounding Return**
The dollars that you borrow earn nothing for you. Most people who borrow money reduce their savings amounts and upon employment termination can’t afford to pay back the loan. These factors contribute to the loss of time and compounding return on savings.
- **Cost of Interest Payments**
Although the interest that you will pay on the loan will be paid back to yourself, the amount you borrow will not earn you anything. The dollars you use for the interest are already your dollars. It’s like taking money from one pocket and putting it into another. You already have the money!
- **Repayment Upon Employment Termination**
If you terminate employment the outstanding balance of your loan becomes due immediately. If you can’t afford to pay back the outstanding balance, it then becomes taxed and penalized as a pre-retirement distribution (assuming you are under age 59 1/2). Therefore you pay federal and state income tax. Generally, workers that borrow money are unable to pay back any outstanding balance upon employment termination. In addition, they have the tax consequence to pay at tax return time!

If you have any questions regarding plan loans or your plan’s loan provisions, please contact your benefits department or plan consultant-Brad Warner/Tom Padilla 610-742-6314.