

## **IRS Announces December 2017 Applicable Federal Rates and 7520 Rates**

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The Internal Revenue Service (IRS) publishes a monthly update to the applicable federal rates (AFRs) and 7520 rates.

Planning professionals and their clients should take note of fluctuations in these rates and be mindful of planning opportunities that come with rate changes.

The AFR is calculated by the IRS under Section 1274(d) of the Internal Revenue Code (the Code) and is used for many purposes. One of its most common applications is to establish the minimum interest rate that can be charged on an intra-family loan without income or gift tax consequences. These “safe harbor rates” are dependent upon two factors: (i) the term of the loan and (ii) the frequency of compounding of interest.

For these purposes:

- Demand notes and notes with a term of three years or less are considered short-term obligations,
- Notes with a term of more than three years but less than nine years are considered mid-term obligations, and
- Notes with a term of more than nine years are considered long-term obligations.

The 2017 AFR rates are as follows:

The 7520 rates are used to calculate the present value of an annuity, an interest for life or for a term of years, or a remainder or a reversionary interest. They are calculated by the IRS under Code Section 7520 (hence, the name 7520 rates) and are always 120% of the AFR for mid-term obligations with semi-annual compounding. The 7520 rates for 2017 are as follows:

Rates are typically published by the 20th day of each month and provide planning opportunities for certain estate planning vehicles which are interest rate sensitive. For example:

- Lower rates are generally preferable for intra-family loans, grantor retained annuity trusts (GRATs), installment sales to grantor trusts and charitable lead annuity trusts (CLATs).
- Higher rates are generally preferable for qualified personal residence trusts (QPRTs) and charitable remainder annuity trusts (CRATs).

As rates continue to change, advisors and clients should maintain an open dialogue so that clients can take advantage of any planning opportunities tied to increasing or decreasing rates.

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