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TO: Clients and Friends of the Firm

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RE: Taxation of Individuals

I. Tax Jurisdiction

On January 1, 2004, the Law "On Personal Income Tax" (the PIT Law) came into effect. Notwithstanding the number of notable changes to the previous personal income tax rules, the law inherits certain key principles established by preceding acts of legislation, among which is tax jurisdiction.

Individuals, who are tax residents in Ukraine, are subject to personal income taxation on their worldwide income. Non-resident individuals are subject to taxation only on income from Ukrainian sources.

II. Taxation of Resident Individuals

A. Tax Residency

A tax resident of Ukraine is an individual, who has permanent residence in Ukraine. If an individual has a permanent residence in more than one country, he or she will be qualified as Ukrainian tax resident in case he or she has closer personal or economic ties (e.g. center of vital interests) in Ukraine.

If it is impossible to determine the country in which the individual has his center of vital interests or if the individual does not have a permanent residence in any country, the individual will be considered a Ukrainian tax resident if present in Ukraine for at least 183 days of the tax period (including days of arrival and departure). Furthermore, if tax residency is impossible to determine based on the above provisions, additional factors which may be applied to determine residency may be used, such as he or she is a legal Ukrainian citizen, has family permanently residing in Ukraine or is registered as a subject of entrepreneurial activity in Ukraine.

B. Tax Rates

The personal income tax rate is currently 15 percent as of January 1, 2007 (an increase from 13 percent). Individuals must also make contributions to the Pension Fund (up to 2%), the temporary disability fund (0.5-1%) and the unemployment fund (0.5%).

In addition, from January 1, 2004 there is a five percent income tax on interest income received on deposits and deposit certificates, from certificates of real estate operations, and from construction financing funds. Furthermore, income derived from gambling, winnings, etc. will be taxed at a rate equal to double the flat rate.

III. Taxable Income

Resident individuals are taxable on their worldwide income, i.e., on income "received" from both domestic and foreign sources. Income is taxable irrespective of whether it is received in cash or in-kind.

If a resident individual receives benefits in-kind, the amount of taxable income is determined on the basis of the fair market value (normal price) of the property, services or other benefits received.

Exemptions from Taxable Income - The following benefits received by a resident individual are specifically excluded from personal income taxation:

- State social insurance and state welfare payments, housing subsidies, and other payments and compensations payable from the state budget, the Pension Fund and social security funds;
- Income from state bonds issued by the Ministry of Finance and state lottery winnings;
- State Pension and social security insurance payments;
- Alimony;
- Gifts made by spouses from their part of joint property as well as gifts made by parents to children and vice versa (with certain limitations);
- Dividends payable in shares (stocks, etc.) issued by a resident entity, if such issuance does not change the proportion of shares in the charter fund of such resident entity;
- The value of state-owned apartments (buildings) received by individuals on a no-charge basis or on a discount basis.

The PIT Law contains a list of items specifically included in the gross income of an individual. These include, among others, gifts, insurance payments and premiums, rental income, fringe benefits (including the cost of received rent, property, food, assistance of home servants, expense

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Thank you.