



US\$200,000,000

8.625 per cent. Puttable Loan Participation Notes due 2011
issued by, but without recourse to, Bayerische Hypo- und Vereinsbank AG,
for the sole purpose of funding a US\$200,000,000 loan to

The City of Kyiv

acting through

the Kyiv City Council

Issue Price: 100 per cent.

Bayerische Hypo- und Vereinsbank AG (the “Bank” or the “Issuer”) is issuing the US\$200,000,000 8.625 per cent. Puttable Loan Participation Notes due 2011 (the “Notes”) for the purpose of financing a seven-year loan (the “Loan”) to The City of Kyiv (the “City” or “Kyiv”) acting through the Kyiv City Council (the “Borrower”), pursuant to a loan agreement dated 15 July 2004 (the “Loan Agreement”) between the Borrower and the Bank as lender. The Notes will be issued on or about 22 July 2004 and constituted by a Trust Deed dated on or about 22 July 2004 (the “Trust Deed”) between the Bank and Deutsche Trustee Company Limited (the “Trustee”). **NOTEHOLDERS WILL HAVE A RIGHT (THE “PUT OPTION”) TO REQUIRE THE ISSUER TO REDEEM THEIR NOTES AT PAR ON 15 JULY 2007. SEE “TERMS AND CONDITIONS OF THE NOTES – REDEMPTION AT THE OPTION OF NOTEHOLDERS.”**

SEE “RISK FACTORS” FOR A DISCUSSION OF CERTAIN FACTORS TO BE CONSIDERED IN CONNECTION WITH AN INVESTMENT IN THE NOTES.

In each case where amounts of principal, interest and additional amounts (if any) are stated to be payable in respect of the Notes, the obligation of the Bank to make any such payment shall constitute an obligation only to pay to the Noteholders, on each date upon which such amounts of principal, interest and additional amounts (if any) are due in respect of the Notes, all principal, interest and additional amounts (if any) actually received by or for the account of the Bank pursuant to the Loan Agreement. The Bank will have no other financial obligation under the Notes.

Save as otherwise expressly provided herein and in the Trust Deed, no proprietary or other direct interest in the Bank’s rights under or in respect of the Loan Agreement or the Loan exists for the benefit of the Noteholders. Subject to the terms of the Trust Deed, no Noteholder will have any entitlement to enforce any of the provisions in the Loan Agreement or have direct recourse to the Borrower except through action by the Trustee under the Security Interests, as defined in the Terms and Conditions of the Notes. Noteholders will be deemed to have accepted and agreed that they will be relying solely on the credit and financial standing of the City in respect of the servicing of the Notes.

Application has been made to list the Notes on the Luxembourg Stock Exchange.

The Notes and the Loan have not been, and will not be, registered under the United States Securities Act of 1933, as amended (the “Securities Act”) or with any securities regulatory authority of any State or other jurisdiction of the United States. The Notes may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. The Notes are being offered and sold outside the United States to non-U.S. persons in reliance on Regulation S (“Regulation S”) under the Securities Act (the “Regulation S Notes”) and within the United States to qualified institutional buyers (“QIBs”), as defined in Rule 144A (“Rule 144A”) under the Securities Act, in reliance on the exemption from registration under the Securities Act provided by Rule 144A (the “Rule 144A Notes”). Prospective purchasers are hereby notified that sellers of the Notes may be relying on the exemption from the provisions of Section 5 of the Securities Act provided by Rule 144A.

The Notes have not been approved or disapproved by the U.S. Securities and Exchange Commission, any State securities commission in the United States or any other U.S. regulatory authority nor have any of the foregoing authorities passed upon or endorsed the merits of the Notes or the accuracy or adequacy of this Offering Circular. Any representation to the contrary is a criminal offence in the United States.

Deutsche Bank Securities
Commercial Bank Khreschatyk

Parex Bank

Morgan Stanley
HVB Corporates & Markets

The Bank has not authorised any offer of Notes to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995, as amended (the “POS Regulations”). Notes may not lawfully be offered or sold to persons in the United Kingdom except in circumstances which do not result in an offer to the public in the United Kingdom within the meaning of the POS Regulations or otherwise in compliance with all applicable provisions of the POS Regulations.

The City accepts responsibility for the accuracy and completeness of the information contained in this Offering Circular, other than as provided herein. To the best of the City’s knowledge and belief (and the City has taken all reasonable care to ensure that such is the case), the information set forth in the Offering Circular is true and accurate in all material respects and is not misleading in any material respect; the opinions, predictions and intentions expressed in this Offering Circular are honestly held; and this Offering Circular does not omit to state any material fact necessary to make such information, opinions, predictions or intentions not misleading in any material respect. The Bank accepts responsibility for information in respect of itself.

Information under the heading “Ukraine” has been extracted from the offering circular dated 2 March 2004 for the issuance of Ukraine sovereign debt securities, which was prepared by the Cabinet of Ministers of Ukraine, represented by the Ministry of Finance, for and on behalf of Ukraine, and was not prepared in connection with the preparation of this Offering Circular. The City has not independently verified this information, and it is therefore subject to uncertainty as to its completeness and reliability. The City only accepts responsibility for the correct extraction and reproduction of the information under such heading.

None of the managers named under “Subscription and Sale” (the “Managers”), the Trustee or, except as specifically stated otherwise herein, the Bank makes any representation or warranty, express or implied, as to the accuracy or completeness of the information in this document. Each person receiving this document acknowledges that such person has not relied on the Managers, the Trustee or, except as specifically stated otherwise herein, the Bank or any person affiliated with the Managers, the Trustee or the Bank, in connection with its investigation of the accuracy of such information or its investment decision. Each person contemplating making an investment in the Notes must make its own investigations and analysis of the creditworthiness of the City and its own determination of the suitability of any other factors that may be relevant to it in connection with such investment.

No person is authorised to provide any information or to make any representation not contained in this document. Any such representation or information should not be relied upon as having been authorised by the City, the Bank, the Trustee or the Managers.

Neither the delivery of this document nor the offering, sale or delivery of any Note shall in any circumstances create any implication that there has been no adverse change, or any event reasonably likely to involve an adverse change, in the condition (financial or otherwise) of the City or the Bank since the date of this document.

The distribution of this document and the offering, sale and delivery of Notes in certain jurisdictions may be restricted by law. Persons into whose possession this document comes are required by the Managers to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers, sales and deliveries of Notes and on distribution of this document and other offering material relating to the Notes, see “Subscription and Sale”.

In this document, all references to “hryvnia” and “UAH” are to the lawful currency for the time being of Ukraine, all references to “dollars”, “U.S. dollars”, “USD” and “US\$” are to the lawful currency for the time being of the United States of America and all references to “EURO”, “Euro”, “euros” or “€” are to the currency introduced at the start of the third stage of European economic and monetary union pursuant to the Treaty establishing the European Community, as amended.

Translations of amounts from hryvnia to dollars are solely for the convenience of the reader and are made at various exchange rates. No representation is made that the hryvnia or dollar amounts referred to herein could have been converted into dollars or hryvnia, as the case may be, at any particular exchange rate or at all. The National Bank of Ukraine’s hryvnia/dollar exchange rate as reported on 15 July 2004 was UAH 5.32 to the dollar.

The Notes are not guaranteed by, and do not constitute the obligation of, the country of Ukraine (“Ukraine” or the “State”), either directly or acting through the Ministry of Finance of Ukraine, nor does Ukraine have any responsibility to facilitate enforcement in the event of a default on the Notes. The information about Ukraine under the caption “Ukraine” and contained elsewhere in this Offering Circular is accordingly provided solely for informational purposes.

The Notes will be in registered form. The Notes may be held and transferred and will be offered and sold in the principal amount of US\$2,000 and integral multiples of US\$1,000 in excess thereof, except that Rule 144A Notes will not be held, transferred, offered or sold in amounts less than US\$100,000 and integral multiples of US\$1,000 in excess thereof. The Regulation S Notes will be evidenced by a global note certificate (the "Regulation S Global Note Certificate"), which will be registered in the name of BT Globenet Nominees Limited as a nominee for, and deposited with a common depository for Euroclear Bank S.A./N.V. as operator of the Euroclear System ("Euroclear") and Clearstream Banking, société anonyme ("Clearstream, Luxembourg") on or about 22 July 2004. The Rule 144A Notes will be evidenced by a global note certificate (the "Rule 144A Global Note Certificate" and, together with the Regulation S Global Note Certificate, the "Global Note Certificates"), which will be registered in the name of Cede & Co. as nominee of, and deposited with a custodian for, The Depository Trust Company ("DTC"). Ownership interests in the Global Note Certificates will be shown on, and transfers thereof will be effected only through, records maintained by DTC, Euroclear and Clearstream, Luxembourg and their respective participants. Individual note certificates ("Individual Note Certificates") evidencing holdings of Notes will only be available in certain limited circumstances. See "Form of Notes and Transfer Restrictions".

NOTICE TO NEW HAMPSHIRE RESIDENTS

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENSE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES ("RSA") WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER RSA 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

STABILISATION

IN CONNECTION WITH THIS ISSUE, DEUTSCHE BANK SECURITIES INC. (THE "STABILISING MANAGER"), OR ANY PERSON ACTING FOR THE STABILISING MANAGER, MAY OVER-ALLOT OR EFFECT TRANSACTIONS WITH A VIEW TO SUPPORTING THE MARKET PRICE OF THE NOTES AT A LEVEL HIGHER THAN WHICH MIGHT OTHERWISE PREVAIL FOR A LIMITED PERIOD. HOWEVER, THERE MAY BE NO OBLIGATION ON THE STABILISING MANAGER (OR ANY AGENT OF THE STABILISING MANAGER) TO DO THIS. SUCH STABILISING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME AND MUST BE BROUGHT TO AN END AFTER A LIMITED PERIOD. SUCH STABILISING SHALL BE IN COMPLIANCE WITH ALL APPLICABLE LAWS, REGULATIONS AND RULES.

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PRESENTATION OF FINANCIAL AND OTHER INFORMATION

Financial Information

Prior to the dissolution of the Soviet Union in 1991, the collection of data and production of official statistical information with respect to the economy of the City was geared to the needs of central planning. Since that time, the means employed in collecting data and methodologies used in the production of statistics have evolved significantly from year to year. Statistical information reported herein has been derived from official publications of, and information supplied by, the Main Financial Office of the Kyiv City State Administration (the “Main Financial Office”) and other departments and committees of the City, as well as by the State Committee of Statistics of Ukraine. See “The City of Kyiv – Overview of Municipal Administration”.

Accounting Principles

The City maintains its books and records in hryvnia and prepares its budget in accordance with the resolutions on the City Budget for the relevant year adopted by the Kyiv City Council (the “City Council”) and pursuant to the procedures prescribed by the Budget Code of Ukraine, dated 21 June 2001 (the “Budget Code”), which came into force on 24 July 2001, and certain internal directives adopted by the City. The main feature of these accounting principles is that revenues are recognised in the period in which they are collected by the City and expenditures (including capital expenditures) are recognised when paid by the City. There is no system of accrual of revenue or expenditure amounts.

The financial information relating to the City presented in this Offering Circular is derived from the City’s records maintained by each of the relevant City departments and compiled by the Main Financial Office. The City Council’s Commission on Budget and Socio-economic Development (the “City Budget Commission”) monitors the implementation of the City Budget. The City Budget Commission carries out regular reviews of the Kyiv City State Administration, including in relation to its compliance with financial and budgetary legislation. See “City Budget and Financial Information – City Budgetary System – Budget Implementation”.

As a result of the introduction of the Budget Code, a number of changes have been made to the budgetary and accounting policies adopted by the City from 25 September 2001. Among other things, the Budget code (i) set out the distinction between general and special purpose funds, (ii) prohibited the creation of off-budget funds and (iii) introduced the concept of ‘budget deficit’ and regulated the procedure for borrowings by local authorities. See “City Budget and Financial Information – City Budgetary System”. The budgetary and accounting principles applicable to the City continue to evolve with an increasing emphasis being placed on the level of detail to which the City Budget is prepared and implemented and control over the flow and use of Budget funds. This process is expected to continue.

Financial Information for 1999, 2000, 2001, 2002 and 2003

The financial information set forth in this Offering Circular for the years ended 31 December 1999, 2000, 2001, 2002 and 2003 is extracted or derived from the City Council resolutions approving the City Budgets for 1999, 2000, 2001, 2002 and 2003, respectively. See “City Budget and Financial Information – City Budgetary System – Budget Process”.

Financial Information for 2004

The City’s budget for 2004 was approved by City Council Resolution No. 267/1142 of 18 December 2003 (the “2004 City Budget Resolution”). On 18 March 2004, amendments to the 2004 City Budget Resolution, set out in City Council Resolution No. 82/1292, were approved by the City Council. On 15 April 2004, by its Resolution No. 149/1359 on Amendments to Resolution No. 267/1142 of the City Council on the 2004 City Budget of 18 December 2003, the City Council introduced amendments to the 2004 City Budget Resolution. These amendments primarily relate to an increase in the amount of permitted external debt of the City to up to US\$350 million. It is likely that certain further amendments will be made to the 2004 City Budget later in the year. References in this Offering Circular to the “2004 City Budget” or to budgeted financial information for the City for 2004 are to the City’s financial information as budgeted for 2004 on a consolidated basis with the financial information of City districts after taking into account all amendments to the 2004 City Budget Resolution to date.

Restatement of Financial Information

Results of the implementation of the annual budget are ordinarily approved by the City Council in the year following that budget year. Budget results are subject to technical adjustment during the budget year and the year following that budget year and the final figures reflecting the results of the implementation of the annual budget are therefore not normally available before the City Council approves the previous year's budget results, which ordinarily occurs within seven months after the end of a given budget year. Budget information may not be changed after the City Council has approved the results of the previous year's budget.

Inflation

Financial information in this document relating to the City's revenues and expenditures has not been adjusted for the effects of inflation and is presented on the basis of those hryvnia values which applied at the time of receipt of revenues or payment of expenditures.

The following table sets forth certain consumer price index and producer price index information for the City and Ukraine, year on year, for year-end 1999 to 2003:

	1999		2000		2001	
	Kyiv	Ukraine	Kyiv	Ukraine	Kyiv	Ukraine
Consumer Price Index	16.4	19.2	30.0	25.8	7.0	6.1
Producer Price Index	12.7	15.7	18.9	20.8	1.0	0.9
			2002		2003	
			Kyiv	Ukraine	Kyiv	Ukraine
Consumer Price Index			3.6	(0.6)	8.1	8.2
Producer Price Index			(0.7)	5.7	11.2	11.1

Sources: State Committee of Statistics, 2002 Ukraine Statistical Year-Book and 2002 Kyiv Statistical Year-Book

According to the State Committee of Statistics, Ukraine's Consumer Price Index for the period from January to May 2004 was 2.9 per cent.

Unless otherwise stated, references in this document to "inflation" in the City in any period refer to the average annual or average annualised percentage change in the City's Consumer Price Index, as appropriate.

Rounding Adjustments

Data included in this document has been subject to rounding adjustments. Accordingly, figures that are totals may not be the arithmetical sum of their components.

Exchange Rates

Since late 1994, the National Bank of Ukraine (the "NBU") has allowed the currency to float freely. The currency of Ukraine, the hryvnia, was introduced in 1996. In April 1997, the authorities introduced a "currency band" for the hryvnia allowing it to float within the rate range of UAH 1.7-1.9 = US\$1.00. Under this policy, the UAH/US\$ exchange rate was allowed to float the stated minimum and maximum amounts, which the NBU pledged to defend through market intervention. In order to achieve stabilisation in Ukraine's currency and financial markets, which were severely affected in 1998 by the emerging markets financial crisis, the NBU adopted a series of anti-crisis measures. These measures were aimed at limiting foreign currency exchange transactions and included extending the currency band in effect at that time to UAH 2.5 - 3.5 = US\$1.00. The NBU subsequently established a new band, effective until the end of 1999, of UAH 3.40 - 4.60 = US\$1.00. The new currency trading band helped to stabilise currency demand and, in line with the programme agreed with the IMF, the NBU had withdrawn most of the currency exchange restrictions previously imposed as a temporary measure.

In 2001, the average hryvnia/US dollar exchange rate increased by 1.3 per cent. due to a favourable trade balance and policies adopted by the NBU. Purchases of foreign exchange in the inter-bank market throughout 2001 and 2002 helped to prevent a substantial nominal appreciation of the

hryvnia. In 2002, the average hryvnia/US dollar exchange rate increased by 0.08 per cent. due to a favourable balance of payments and policies adopted by the NBU. The NBU continues to follow a floating exchange rate policy, intervening only to smoothen sharp downward fluctuations of the exchange rate. The NBU also has a number of other monetary tools that are, or can be, used to support the hryvnia. These include obligatory sales of 50 per cent. of hard currency earnings by exporters, licensing and a maximum 90 day period between the prepayment of imported goods and their delivery to the customs territory as well as reserve requirements and outright sales of US dollars. The following table sets out the average and period end hryvnia/US dollar exchange rates reported by the NBU:

	<u>Average</u>	<u>Period End</u>
1999	4.13	5.22
2000	5.44	5.43
2001	5.37	5.30
2002	5.32	5.33
2003	5.33	5.33
2004 (to 31 May 2004).....	5.33	5.33

Source: NBU

The NBU's hryvnia/dollar exchange rate as reported on 15 July 2004 was UAH 5.32 to the dollar.

SUMMARY OF THE OFFERING

The following is a summary of certain information contained elsewhere in this document. Reference is made to, and this Summary is qualified in its entirety by, the more detailed information contained elsewhere in this document.

Issuer:	Bayerische Hypo- und Vereinsbank AG
Borrower:	The City of Kyiv acting through the Kyiv City Council
Joint Lead Managers:	Deutsche Bank Securities Inc. Morgan Stanley & Co. International Limited
Managers:	Bayerische Hypo- und Vereinsbank AG, Open Joint Stock Company Commercial Bank “Khreschatyk”, Parex Bank
Issue Amount:	US\$200,000,000
Issue Price:	100 per cent. of the principal amount of the Notes
Issue Date:	22 July 2004
Maturity Date:	15 July 2011
Trustee:	Deutsche Trustee Company Limited
Registrar:	Deutsche Bank Trust Company Americas
Paying Agents:	Deutsche Bank Luxembourg S.A. and Deutsche Bank Trust Company Americas
Principal Paying Agent:	Deutsche Bank AG London
Interest:	The Notes will bear interest from 22 July 2004 at a rate of 8.625 per cent. per annum payable semi-annually in arrears on 15 January and 15 July in each year except that the first payment of interest shall be made on 15 January 2005 in respect of the period from (and including) the Issue Date to (but excluding) 15 January 2005.
Status:	The Notes will constitute the obligations of the Issuer to apply an amount equal to the gross proceeds of the issue of the Notes solely for the purpose of financing a 7-year loan (the “Loan”) to the Borrower pursuant to the terms of a loan agreement made between the Issuer as lender (in such capacity, the “Lender”) and the Borrower and dated 15 July 2004 (the “Loan Agreement”). The Issuer will pay the holders of the Notes solely all amounts equivalent to those (if any) received from the Borrower under the Loan Agreement less amounts in respect of certain Reserved Rights (as defined in the Terms and Conditions of the Notes).
Form:	<p>The Notes will be issued in registered form. The Notes will be in denominations of US\$2,000 each and integral multiples of US\$1,000 in excess thereof, except that Rule 144A Notes will not be held, transferred, offered or sold in amounts less than \$100,000 and integral multiples of US\$1,000 in excess thereof. The Regulation S Notes and the Rule 144A Notes will be represented by a Regulation S Global Note Certificate and a Rule 144A Global Note Certificate, respectively.</p> <p>The Global Note Certificates will be exchangeable for Notes in individual form in the limited circumstances specified in the Global Note Certificate.</p>
Initial Delivery of the Notes:	On or before the Issue Date, the Rule 144A Global Note Certificate will be deposited with a custodian for DTC, and the Regulation S Global Certificate will be deposited with a common depository for Euroclear and Clearstream, Luxembourg. The Rule 144A Notes

will be registered in the name of a nominee of DTC, and the Regulation S Notes will be registered in the name of a common nominee for Euroclear and Clearstream, Luxembourg.

Early Redemption:..... The Notes may be redeemed at the option of the Issuer in whole, but not in part, at any time, upon giving notice to the Noteholders, at the principal amount thereof together with accrued and unpaid interest to the date of redemption and any additional amounts in respect thereof, upon receiving notice that the Borrower has prepaid the Loan for tax reasons or in the event that it becomes unlawful for the Lender to fund the advance or allow to remain outstanding the Loan under the Loan Agreement as more fully described in Clause 10 of the Loan Agreement. See also Condition 5 (*Redemption and Purchase*) in “Terms and Conditions of the Notes”.

Put Option..... The Issuer shall, at the option of the Holder of any Note, redeem such Note on 15 July 2007 at a price equal to 100 per cent. of its principal amount together with interest accrued to such date, plus additional amounts, if any. In that event, the Borrower will be required to prepay the Loan together with accrued interest and any additional amounts in the amount that the Issuer is required to pay the Holders of Notes who have exercised such option.

Issuer’s Covenant: As long as any of the Notes remain outstanding, the Issuer will not, without the prior written consent of the Trustee, agree to any amendments to or any modification or waiver of, or authorise any breach or proposed breach of, the terms of the Loan Agreement, except as otherwise expressly provided in the Trust Deed or the Loan Agreement.

Negative Pledge and other Covenants: The Loan Agreement contains a negative pledge in relation to the creation of Security Interests (other than Permitted Security Interests) (each as defined in the Loan Agreement) over the Indebtedness (as defined in the Loan Agreement) of the Borrower as set out in the Loan Agreement.

Events of Default/Relevant Event:..... In the case of an Event of Default (as defined in the Loan Agreement) or a Relevant Event (as defined in the Terms and Conditions of the Notes), the Trustee may, subject as provided in the Trust Deed, (1) require the Lender to declare all amounts payable under the Loan Agreement by the Borrower to be due and payable (in the case of an Event of Default) or (2) enforce the security created in the Trust Deed in favour of the Noteholders (in the case of a Relevant Event).

Upon repayment of the Loan following an Event of Default, the Notes will be redeemed or repaid at the principal amount thereof, together with interest accrued to the date fixed for redemption and any additional amounts due, and thereupon shall cease to be outstanding.

Rating: The Notes have been rated B by Standard & Poor’s Rating Services. The Borrower has been rated B by Standard & Poor’s Rating Services and B2 by Moody’s Investors Service, Inc.

A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation.

Withholding Tax: All payments of principal and interest in respect of the Notes will be made free and clear of and without deduction or withholding for or on account of any taxes, duties, assessments, fees or other governmental charges of the United Kingdom or Ukraine save as

required by law. If any such withholding or deduction is so required, the Issuer shall (subject to certain exceptions) pay such additional amounts as will result in the receipt by the Noteholders of such amounts as would have been received by them had no such withholding or deduction been required. The sum payable by the Borrower under the Loan will be required (subject to certain exceptions) to be increased to the extent necessary to ensure that the Issuer receives a net sum of sufficient amount to enable it to pay such additional amounts. The sole obligation of the Issuer in this respect will be to pay to the Noteholders sums equivalent to the sums received from the Borrower. See Condition 7 (*Taxation*) in “Terms and Conditions of the Notes”.

Listing:..... Application has been made to list the Notes on the Luxembourg Stock Exchange. The Notes issued and sold in reliance on Rule 144A are eligible for trading on the PORTAL[®] Market, a subsidiary of The Nasdaq Stock Market, Inc.

Selling Restrictions:..... The Notes have not been and will not be registered under the Securities Act and, subject to certain exceptions, may not be offered or sold within the United States. The Notes may be sold in the United Kingdom only in compliance with applicable laws. The Notes have not been registered in Ukraine and may not be offered or sold within Ukraine. The offer and sale of the Notes may also be restricted in other jurisdictions. See “Subscription and Sale”.

Governing Law:..... The Notes will be governed by English law.

Risk Factors:..... For a discussion of certain risks that should be considered by prospective purchasers of the Notes, see “Risk Factors”.

ERISA Considerations: The Notes may be regarded for ERISA purposes as equity interests in a separate entity whose sole asset is the Loan. The Notes may only be acquired by a benefit plan investor that is subject to ERISA or section 4975 of the U.S. Internal Revenue Code if an applicable U.S. Department of Labor Prohibited Transaction exemption applies. Each purchaser and/or holder of Notes and each transferee thereof will make or will be deemed to have made certain representations in this regard. Potential purchasers should read the sections entitled “Certain ERISA and Other Considerations” and “Form of Notes and Transfer Restrictions”.

RISK FACTORS

Prospective investors should carefully review this entire Offering Circular, and in particular the information set forth below, before making a decision to invest in the Notes.

Risks Associated with Ukraine

General

An investment in a newly independent country with an economy in transition, such as Ukraine, is subject to substantially greater risks than an investment in a country with a more developed economy and a more mature political and legal system. Although some progress has been made since independence in 1991 in reforming Ukraine's economy and political and judicial systems, to a large extent Ukraine still lacks the necessary legal infrastructure and regulatory framework that is essential to support market institutions, the effective transition to a market economy and broad-based social and economic reforms. As a consequence, an investment in Ukraine carries risks that are not typically associated with investing in more mature markets. These risks may be compounded by incomplete, unreliable or unavailable economic and statistical data on Ukraine, including certain of the information provided in this Offering Circular. See “– Official economic data in this Offering Circular may not be reliable” below.

Ukraine's political and economic environment may destabilise, causing the economy to deteriorate and affecting the City's ability to repay the Loan.

Ukraine has, over recent years, undergone substantial political transformation from a constituent republic in a federal socialist state to the early stages of an independent sovereign democracy. In parallel with this transformation, Ukraine is slowly transitioning from a centrally planned economy to a market economy. However, this process is far from complete. Historically, a lack of political consensus in the Ukrainian Parliament has made it difficult for the Ukrainian government to sustain a stable coalition of parliamentarians to secure the necessary support to implement a variety of policies intended to foster liberalisation, privatisation and financial stability.

Structural weaknesses in the economy remain that are likely to restrain economic growth and impose substantial fiscal pressures on the Ukrainian government over the coming years. Although Ukraine has experienced a number of positive macroeconomic trends over the recent years such as gross domestic product (“GDP”) growth of 9.2 per cent., 5.2 per cent. and an estimated 8.5 per cent. in 2001, 2002 and 2003, respectively, an increase in its current account surplus from US\$1.4 billion in 2001 to US\$3.2 billion in 2002 (and from US\$2.2 billion in the first nine months of 2002 to US\$2.5 billion in the first nine months of 2003), a steady increase in its foreign exchange reserves since 1998 (most recently, from US\$3.1 billion at the end of 2001 to US\$4.4 billion at the end of 2002 and to US\$6.9 billion as at the end of 2003) and inflation levels (as measured by the Consumer Price Index (“CPI”)) of 6.1 per cent. in 2001 and 8.2 per cent. in 2003, and deflation of 0.6 per cent. in 2002, all of these positive trends may not be sustainable over the longer term and may be reversed unless Ukraine undertakes certain important structural reforms in the near future while continuing to exercise monetary policies that have contributed to the reduced inflationary levels. The most critical structural reforms that need to be implemented include (i) comprehensive reforms of Ukrainian tax legislation with a view to broadening the tax base by eliminating exemptions and bringing a substantial portion of the shadow economy into the reporting economy, (ii) the reform of the energy sector through the introduction of uniform market based energy prices and improvement in collection rates (and, consequently, the elimination of the persistent deficits in that sector) and (iii) the reform of social benefits and pensions. These structural reforms will be difficult to implement in view of the Presidential elections to take place in October 2004 and the small majority that the current coalition Government enjoys in the Parliament. Continued reform will also depend in part on Presidential support. President Leonid Kuchma has served two terms in office and on 25 December 2003 the Ukrainian Constitutional Court ruled that President Kuchma is not barred by the Constitution from running for a third consecutive term in office. However, President Kuchma has indicated that he is not planning to run again in the presidential election scheduled to take place in October 2004. It is not certain whether and in what way the necessary reforms will be supported by President Kuchma's successor or any other future President. There can be no assurance that the political initiatives necessary to achieve these or any other reforms described elsewhere in this Offering Circular will continue, will not be reversed or will achieve their intended aims.

Regional relationships upon which Ukraine depends for its economic growth may deteriorate and affect the City's ability to repay the Loan.

Ukraine's economy depends heavily on its trade flows with Russia and the rest of the Commonwealth of Independent States, largely because Ukraine imports a large proportion of its energy requirements, especially from Russia (with whom the country runs large trade deficits). In addition, a large share of Ukraine's services receipts comprise transit charges for oil, gas and ammonia from Russia. As a result, Ukraine considers its relations with Russia to be of strategic importance. If bilateral trade relations were to deteriorate or if Russia stopped transiting a large portion of its oil and gas through Ukraine, this could materially and adversely affect Ukraine's balance of payments and foreign currency reserves, and could indirectly affect the City's financial condition and thus its ability to repay the Loan.

Ukraine's developing legal system is subject to risks and uncertainties, which may have an adverse effect on the City's ability to repay the Loan.

Since independence in 1991, as Ukraine has been developing from a planned to a market based economy, the Ukrainian legal system has also been developing to support this market based economy. Ukraine's legal system is however in transition and is therefore subject to greater risks and uncertainties than a more mature legal system. In particular, risks associated with the Ukrainian legal system include, but are not limited to:

- provisions in the laws and regulations that are ambiguously worded or lack specificity and thereby raise difficulties when implemented or interpreted;
- inconsistencies between and among the constitution of Ukraine, laws, presidential decrees, and Ukrainian governmental, ministerial and local orders, decisions, resolutions and other acts;
- the lack of judicial and administrative guidance on the interpretation of Ukrainian legislation, including the complicated mechanism of exercising constitutional jurisdiction by the Constitutional Court of Ukraine;
- the relative inexperience of judges and courts in interpreting Ukrainian legislation and the general inconsistency in their interpretation of Ukrainian legislation in the same or similar cases;
- corruption within the judiciary; and
- a high degree of discretion on the part of governmental authorities, which could result in arbitrary actions.

Furthermore, several fundamental Ukrainian laws either have only recently become effective or are still pending hearing or adoption by the Ukrainian Parliament. For example, with effect from 1 January 2004, Ukraine adopted a new civil code, a new economic code, new mortgage finance laws and a new law on personal income tax. The recent origin of much of Ukrainian legislation, the lack of consensus about the scope, content and pace of economic and political reform and the rapid evolution of the Ukrainian legal system in ways that may not always coincide with market developments place the enforceability and underlying constitutionality of laws in doubt, and result in ambiguities, inconsistencies and anomalies. In addition, Ukrainian legislation often contemplates implementing regulations. Often such implementing regulations have either not yet been promulgated, leaving substantial gaps in the regulatory infrastructure, or have been promulgated with substantial deviation from the principal rules and conditions imposed by the respective legislation, which results in a lack of clarity and growing conflicts with regulatory authorities.

These and other factors that impact on Ukraine's legal system make an investment in these Notes subject to greater risks and uncertainties than an investment in a country with a more mature legal system.

There are uncertainties relating to Ukraine's judicial system, which may make legal recourse and enforcement against the City difficult or impossible.

The independence of the judicial system and its immunity from economic and political influences in Ukraine remain largely untested. Although the Constitutional Court of Ukraine is the only body authorised to exercise constitutional jurisdiction and has mostly proven its impartiality of judgment, the system of constitutional jurisdiction itself remains too complicated to ensure smooth and effective removal of discrepancies between the Constitution of Ukraine and applicable Ukrainian legislation on the one hand and among various laws of Ukraine on the other hand.

The system of general and specialised courts is understaffed and underfunded. Judges and courts are generally inexperienced in the area of business and corporate law. Judicial precedents generally have no binding effect on subsequent decisions. Not all Ukrainian legislation is readily available to the

public or organised in a manner that facilitates understanding. Court decisions are not open to public access and, therefore, may not serve as guidelines in interpreting applicable Ukrainian legislation to the public at large. Moreover, courts themselves are not bound by earlier decisions taken under the same or similar circumstances, which results in the inconsistent application of Ukrainian legislation to resolve the same or similar disputes. The Ukrainian judicial system became more complicated and hierarchic as a result of the recently introduced judicial reform. The expected result of the judicial reform is that the Ukrainian judicial system will become even slower than before.

Enforcement of court orders and judgments can in practice be very difficult in Ukraine. The State Execution Service, a body independent of the Ukrainian courts, is responsible for the enforcement of court orders and judgments in Ukraine. Often, enforcement procedures are very time-consuming and may fail for a variety of reasons, including the defendant lacking sufficient bank account funds, the complexity of auction procedures for the sale of the defendant's property or the defendant undergoing bankruptcy proceedings. In addition, the State Execution Service has limited authority to enforce court orders and judgments quickly and effectively. Ukrainian enforcement agencies are bound by the method of execution envisaged by the relevant court order or judgment and may not independently change such method even if it proves to be inefficient or unrealisable. Furthermore, notwithstanding successful execution of a court order or a judgment, a higher court could reverse the court order or judgment and require that the relevant funds or property be restored to the defendant. Moreover, in practice the procedures employed by the State Execution Service do not always comply with applicable legal requirements, resulting in delays to or failures in enforcement of court orders and judgments.

These uncertainties also extend to certain rights, including investor rights. In Ukraine, there is no established history of investor rights or responsibility to investors and in certain cases the courts may not enforce these rights. In the event courts take a consistent approach in protecting rights of investors granted under applicable Ukrainian legislation, the government and/or the legislature of Ukraine may attempt legislatively to overrule any such court decisions by backdating such legislative changes to a certain date in the past.

These and other factors that impact on Ukraine's judicial system make an investment in the Notes subject to greater risk and uncertainty than an investment in a municipality in a country with a more developed judicial system.

The City's financial information is unaudited and may therefore not accurately reveal its true financial condition.

Although the implementation of the City Budget is subject to internal control and monitoring and the Kyiv City State Administration is subject to certain internal checking procedures, and while the financial accounts of the City related to the use of budget funds in a given budget year are subject to audit by an independent audit firm, the financial information with regard to the City of Kyiv presented in this Offering Circular has not been audited or reviewed by independent auditors in accordance with international auditing standards and as a result may not accurately reveal the City's true financial condition.

Official economic data in this Offering Circular may not be reliable.

Although a range of government ministries and City departments, along with the NBU, the State Committee of Statistics and the Main Financial Office, produce statistics on Ukraine and its economy and the City and its economy, there can be no assurance that these statistics are as accurate or as reliable as those compiled in more developed countries. Prospective investors should be aware that figures relating to Ukraine's GDP and the City's Gross City Product ("GCP") and many other aggregate figures cited in this Offering Circular may be subject to some degree of uncertainty and may not be fully in accordance with international standards. Furthermore, standards of accuracy of statistical data may vary from ministry to ministry and department to department and from period to period due to the application of different methodologies. In this Offering Circular, data is presented as provided by the relevant ministry or department to which the data is attributed and no attempt has been made to reconcile such data to the data compiled by other ministries or departments or by other organisations. The existence of a sizeable unofficial or shadow economy may also impact on the accuracy and reliability of statistical information.

Risks Associated with the City

The division of tax revenues with the State may not favour the City, thereby making it difficult for the City to repay the Loan.

The division of tax revenues between the budget of Ukraine (the “State Budget”) and the budget of the City (the “City Budget”) is governed by Ukrainian law. In recent years, the State Budget’s share of tax revenues has increased and that of the City Budget has decreased. This trend is likely (although not certain) to continue. The increasing share taken by the State of the tax revenues collected in the City may have an adverse effect on the City’s financial condition, which in turn may reduce the City’s capacity to meet its spending commitments and may adversely affect the ability of the City to comply with its obligations under the Loan Agreement. Monies in the state treasury of Ukraine (the “State Treasury”) would not likely be available to the City’s creditors including the Bank with respect to the Loan Agreement. See “City Budget and Financial Information – City Budgetary System – Budgetary Relations between the State and Local Governments” and “City Budget and Financial Information – Budget Revenues – Tax Revenues”.

The new flat-rate income tax in Ukraine may have a material adverse effect on the City’s revenues and thus on its ability to repay its debts, including the Loan.

On 22 May 2003, Parliament approved the Law of Ukraine “On Tax on Individuals’ Income” (the “Personal Income Tax Law”), which has reformed personal income tax by introducing a flat rate tax of 13 per cent. with effect from 1 January 2004 (to be increased to 15 per cent. from 1 January 2007). The previous income tax rate scale ranged from 10 to 40 per cent. This law entered into effect on 1 January 2004. The City expects to experience budget revenue losses as a result of the introduction of this new flat-rate tax because it has resulted in the pool of income tax revenues to be divided between the City and the State being smaller than under the income tax rates in effect before 1 January 2004. It is expected that Kyiv will lose more tax revenues than poorer regions of Ukraine will due to the loss of higher-end tax bracket revenues.

The City anticipates that the potential decrease in revenues of the City Budget resulting from the flat-rate income tax will be offset by certain factors. For example, the Budget Code provides that the granting by the State of any tax privileges that decrease the revenues of local budgets should be accompanied by compensation to the local budgets for the loss of revenues. The City will be compensated by the State for any budget losses incurred as a result of the flat-rate income tax in accordance with the procedure for compensation of local budgets approved by the Cabinet of Ministers of Ukraine. In addition, the City expects that tax evasion will be reduced as a consequence of lower tax rates. However, there can be no assurance that these or other factors will sufficiently offset the reduction in revenue resulting from the flat-rate income tax or that such tax will not otherwise have a material adverse effect on the City’s financial condition. See “City Budget and Financial Information – Budget Revenues – Tax Revenues”.

Non-payment of financial obligations to the City may have a material adverse effect on the City’s ability to repay its indebtedness.

The Ukrainian financial system suffers from chronic and endemic problems relating to the non-payment of financial obligations. At any one time, the City, like most other local governments in Ukraine, is owed considerable amounts of unpaid taxes. As at 31 December 2003, there was an aggregate of UAH 40.3 million of tax revenues outstanding and unpaid to the City as compared with UAH 33.8 million as at 31 December 2002 and UAH 44.9 million at 31 December 2001. The largest component of these amounts is land taxes in arrears in an amount of UAH 23.5 million as at 31 December 2003. Non- payment of taxes owed to the City may have a material adverse effect on the City’s cash flow and, consequently, on the ability of the Bank to comply with its obligations under the Notes. See “City Budget and Financial Information – Budget Revenues”.

Actual 2004 city budget results may differ from 2004 city budget information contained herein.

The 2004 City Budget Resolution was enacted prior to the commencement of the 2004 budget year. See “Presentation of Financial and Other Information”. The results of implementation of the 2004 City Budget will be approved by the City following the 2004 budget year. Historically, the City’s planned revenues and expenditures have differed materially from the results of implementation of a given City Budget. Accordingly, there can be no assurance that the results of implementation of the 2004 City Budget will not differ materially from the information relating to the 2004 City Budget contained herein.

Kyiv's economy is significantly more controlled by the City than Western cities' economies are by their municipal governments.

The City is responsible for a greater part of the local economy than is the case for municipal governments in most Western cities. The City also has a far more significant role and responsibility vis-à-vis healthcare, education and social services than many Western (including American) cities have. This could lead to pressure on the financial resources which would otherwise be used to service the Loan.

The City's infrastructure requires substantial investment, and if this is not provided, the City's economic development could be hampered.

The City's infrastructure, including transportation, sewage, bridges and roads are inadequate and outdated and require substantial investment. Should they not receive such investment, the City's economic development could be hampered, which could have a material adverse effect on the City's financial condition.

The City's death rate exceeds its birth rate which may mean a future erosion of the City's tax base and thus of its ability to repay its indebtedness.

The population of Ukraine is declining, and the City's own birth rates and death rates reflect a similar trend, albeit the rate of decline in the City is less than the national rate. This may result in a declining tax base for the City and thus a decline in its revenues. This could result in a weakening of the City's financial condition and could ultimately have an adverse effect on its ability to repay its debts.

Risks Associated with the Notes

Civil liabilities of the City may not be enforceable and the Bank may therefore not be able to successfully pursue claims under the Loan Agreement.

Certain assets of the City are not available to satisfy the claims of creditors, including any claims by the Bank under the Loan Agreement. In particular, the Land Code of Ukraine, as adopted on 25 October 2001, provides that certain types of land, such as public parks, cemeteries, land covered with forest, land under roads, land covered with water and certain other types of land may not be alienated by a municipality. In addition, there is uncertainty under Ukrainian law as to whether, in the event of any enforcement following a default by the City, other categories of the City's assets (other than the City's budget funds which have been allocated for the purpose of paying debt) would be available for purposes of such enforcement, and there is a related risk that a creditor might only be able to enforce against such allocated budget funds and not against the City's other assets. See "City Budget and Financial Information – Indebtedness of the City of Kyiv".

Enforcement against the City's budget funds is subject to the procedures provided by budget legislation, as interpreted by the courts and as applied by the State Treasury. In particular, Article 25 of the Budget Code may be interpreted as providing generally for the obligation of the State Treasury to transfer money from an account of the City to the Bank as part of an enforcement procedure on the basis of a decision of a Ukrainian court (including to enforce the decision of a foreign court or an arbitration). However, enforcement may be refused or impeded because the relevant payment is not envisaged or is not given the requisite priority in the City's budget for the relevant year, or due to the absence of specific implementation mechanisms and established practices applied by the State Treasury. Furthermore, the extent to which budget laws in future years may limit enforcement is unknown at this time. In addition, certain assets of the City (such as schools and hospitals) have been transferred to the City districts and are legally owned by the districts. While the City may require the districts to transfer such assets back to it, certain actions would need to be taken by the City in order to make those assets available to creditors. Accordingly, in the event of any enforcement following a default by the City, there can be no assurance that the Bank will be able to recover fully amounts due to it under the Loan Agreement.

There is also a risk that, notwithstanding the waiver of sovereign immunity by the City, a claimant will not be able to enforce a court judgment against certain assets of the City (including the imposition of any arrest order or attachment or seizure of such assets and their subsequent sale) without the City having specifically consented to such enforcement at the time when the enforcement is sought.

In the event that a Noteholder obtains a final judgment for a sum of money rendered by a court in any jurisdiction other than Ukraine, enforceability in Ukraine of such final judgment will be

recognised by a court of Ukraine as a basis upon which to approve enforcement of a judgment against the City or its assets, properties, or revenues in Ukraine, provided that there exists an international treaty between Ukraine and the country where the foreign judgment was rendered concerning the recognition and enforcement of judgments in civil cases and, unless such international treaty otherwise provides, provided that the relevant requirements set forth in the Law of Ukraine “On Recognition and Enforcement in Ukraine of Foreign Court Judgments”, as adopted on 29 November 2001, and any other relevant law, decree or regulation of Ukraine are met. No such international treaty exists between Ukraine and the United Kingdom or the Federal Republic of Germany concerning the recognition and enforcement of judgments in civil cases. Accordingly, it is unlikely that a court of Ukraine would recognise or enforce a judgment from such a country without re-examination of the issues. A court of Ukraine may refuse or limit enforcement of a foreign judgment, *inter alia*, on public policy grounds and may seek to decline jurisdiction over a dispute arising out of an agreement governed by foreign law.

The City has agreed that, in relation to any claim by the Bank (or, following the transfer of its rights under the Loan Agreement pursuant to the Trust Deed, by the Trustee) in respect of any dispute or difference of whatever nature howsoever arising under, out of or in connection with the Loan Agreement, such claimant may elect, by notice in writing to the City, to settle such claims by arbitration in accordance with the Rules of Arbitration of the International Chamber of Commerce (the “Rules”) as at present in force by a panel of three arbitrators appointed in accordance with the Rules. The seat of arbitration shall be London, England. The procedural law of arbitration shall be English law. Ukraine is a party to the United Nations (New York) Convention on the Recognition and Enforcement of Foreign Arbitral Awards dated 10 June 1958 (the “Convention”). An arbitral award in a country which is a party to the Convention should be recognised and enforced by the courts of Ukraine without re-examination of the issues, subject to certain qualifications, such as that a court of Ukraine may refuse or limit enforcement of such award on public policy grounds.

Payments on the Notes are limited to payments received by the Bank under the Loan Agreement.

The Bank is only obliged to make payments under the Notes to the Noteholders in an amount equivalent to sums of principal, interest and/or additional amounts (if any) actually received by or for the account of the Bank pursuant to the Loan Agreement (less any amount in respect of the Reserved Rights). Consequently, if the Borrower fails fully to meet its obligations under the Loan Agreement, the Noteholders will receive less than the scheduled amount of principal or interest on the relevant due date.

Noteholders have no direct recourse to the Borrower.

Except as otherwise expressly provided in the Terms and Conditions and in the Trust Deed, no proprietary or other direct interest in the Bank’s rights under or in respect of the Loan Agreement or the Loan exists for the benefit of the Noteholders. Subject to the terms of the Trust Deed, no Noteholder will have any entitlement to enforce any of the provisions in the Loan Agreement or have direct recourse to the Borrower except through action by the Trustee under the Security Interests. Neither the Bank nor the Trustee pursuant to the assignment of the Transferred Rights (as defined in the Terms and Conditions of the Notes) shall be required to take proceedings to enforce payment under the Loan Agreement unless it has been indemnified and/or secured by the Noteholders to its satisfaction against all liabilities, proceedings, claims and demands to which it may thereby become liable and all costs charges and expenses which may be incurred by it in connection therewith.

In addition, under the Terms and Conditions of the Notes, Noteholders will be deemed to have accepted that:

- neither the Bank nor the Trustee makes any representation or warranty in respect of, and shall at no time have any responsibility for, or (save as otherwise expressly provided in the Trust Deed and paragraph (vi) of Condition 1 of the Terms and Conditions of the Notes) liability or obligation in respect of, the performance and observance by the Borrower of its obligations under the Loan Agreement or the recoverability of any sum of principal, interest, Additional Amounts or Tax Indemnity Amounts or other amounts, if any, due or to become due from the Borrower under the Loan Agreement;
- neither the Bank nor the Trustee shall at any time have any responsibility for, or obligation or liability in respect of, the condition (financial, operational or otherwise), creditworthiness, affairs, status, nature or prospects of the Borrower;

- neither the Bank nor the Trustee shall at any time be liable for any misrepresentation or breach of warranty or any act, default or omission of the Borrower under or in respect of the Loan Agreement;
- neither the Bank nor the Trustee shall at any time have any responsibility for, or liability or obligation in respect of, the performance and observance by the Registrar, any Transfer Agent or any Paying Agent of their respective obligations under the Agency Agreement (each of the foregoing capitalised terms as defined in the Terms and Conditions of the Notes);
- the financial servicing and performance of the terms of the Notes depend solely and exclusively upon performance by the Borrower of its obligations under the Loan Agreement, its covenant to pay under the Loan Agreement and its credit and financial standing. The Borrower has represented and warranted to the Bank in the Loan Agreement that the Loan Agreement constitutes legal, valid and binding obligations of the Borrower. The representations and warranties given by the Borrower in Clause 11 (Representations and Warranties of the Borrower) of the Loan Agreement are given by the Borrower to the Bank for the sole benefit of the Bank and neither the Trustee nor any Noteholder shall have any remedies or rights against the Borrower that the Bank may have with respect to such representations or warranties, other than any right the Trustee may have pursuant to the assignment of the Transferred Rights;
- the Bank (and, pursuant to the assignment of the Transferred Rights, the Trustee) will rely on self-certification by the Borrower as a means of monitoring whether the Borrower is complying with its obligations under the Loan Agreement and shall not otherwise be responsible for investigating any aspect of the Borrower's performance in relation thereto and, subject as further provided in the Trust Deed, the Trustee will not be liable for any failure to make the usual or any investigations which might be made by a security holder in relation to the property which is the subject of the Security Interests and held by way of security for the Notes, and shall not be bound to enquire into or be liable for any defect or failure in the right or title of the Bank to the security property, whether such defect or failure was known to the Trustee or might have been discovered upon examination or enquiry or whether capable of remedy or not, nor will it have any liability for the enforceability of the security created by the Security Interests, whether as a result of any failure, omission or defect in registering or filing or otherwise protecting or perfecting such security, and the Trustee will have no responsibility for the value of such security; and
- if the Borrower is required by law to make any withholding or deduction for or on account of tax from any payment under the Loan Agreement or if the Bank is required by law to make any withholding or deduction for or on account of tax from any payment in respect of the Notes, the sole obligation of the Bank will be to pay to the Noteholders sums equivalent to the sums actually received from the Borrower pursuant to the Loan Agreement in respect of such payment, including, if applicable, Additional Amounts or Tax Indemnity Amounts in respect of the tax required to be so withheld or deducted; the Bank shall not be obliged to take any actions or measures as regards such deductions or withholdings other than those set out in Clause 8 (Taxes) and Clause 10.4 (Mitigation) of the Loan Agreement.

The Bank's obligations will be discharged once the Borrower has made its required payments, even if the Bank has not passed such payments on to the Noteholders.

Payments of principal and/or interest made by the Borrower under the Loan Agreement to, or to the order of, the Trustee or the Principal Paying Agent will satisfy pro tanto the obligations of the Bank in respect of the Notes and consequently Noteholders will have no further recourse against the Bank or the Borrower after any such payment is made.

Ukrainian currency control regulations may prevent the City from repaying the Loan to the Bank.

The NBU is empowered to define the policy and regulate currency operations in Ukraine, as well as establish any restrictions on currency operations and repatriation.

Ukrainian currency control regulations and practice may be subject to continual change, with the NBU exercising considerable autonomy in interpretation and practice. While at present, the Loan is only subject to registration with the NBU and no licence is required to be obtained from the NBU in order to make payments of principal and interest under the Loan, there can be no guarantee that such law and practice will remain unchanged during the term of the Loan. In addition, certain categories of payments by the City from Ukraine to recipients outside of Ukraine, other than payments of principal and interest under the Loan Agreement and payments that are deemed to

constitute fees for works or services rendered to the City by a non-resident, may require an individual licence of the NBU. In practice, similar payments are often made without such a licence and, to the best of the City's knowledge, the NBU does not challenge this practice. However, there can be no assurance that such practice, and the related position of the NBU, will remain unchanged during the term of the Loan. If an individual licence of the NBU is required for the City to make any such payments, the City will promptly apply for such a licence. However, if the NBU refuses to issue such a licence, there can be no assurance that the City will be able to make payments on the Loan.

While the Loan Agreement will be registered with the NBU prior to the closing of the issue of the Notes, payments under the Loan to any entity other than the Bank would require either an amended loan registration certificate or an additional licence from the NBU. The City believes that the NBU would be inclined to view enforcement of security by the Trustee as a mere assignment of the Bank's claims by the Bank to the Trustee, and would be in a position to amend the loan registration certificate based on receipt of documentary evidence that such assignment has occurred. However, given that there is no established procedure for such an amendment, it is not clear what documents would satisfy such a requirement. In addition, there can be no assurance that the NBU would not require an additional licence in order for the City to make payments to the Trustee, nor that the City would receive a licence if one were required. If the City does not receive such a licence, if required, there can be no assurance that the City will be able to make payments on the Loan.

The NBU recently issued a regulation pursuant to which the state agency monitoring external markets shall review fees for services rendered by a non-resident under an agreement (or a series of agreements for the rendering of similar services) the value of which, as set forth in the agreement (or series of agreements), is in excess of an equivalent of €50,000 ("service payments to non-residents"). Unless a cross-border transaction relating to a non-resident's services is licensed by the NBU or is otherwise subject to an exemption, any such payment can be made only on the basis of a written conclusion of the relevant state agency that the value of the services set forth in the agreement (or series of agreements) is not excessive. If the relevant state agency, for any reason, refuses to carry out a review of such fees, any such payment can be made only on the basis of a specific permission of the NBU. If the relevant state agency determines that the fees are excessive, or refuses to carry out a review of the fees, and if the NBU does not issue a permission, the fees cannot be paid (unless such decision of the state agency or the NBU has been overruled by a court order). The applicable regulations exempt from this requirement payments made in accordance with the terms of a loan registration certificate issued by the NBU in respect of the relevant loan agreement. However, it is unclear whether such exemption should be deemed to apply only to the payment of interest on the loan, which would be specified in the loan registration certificate, or, in addition, to the payment of fees or commissions, which would not be specified in such loan registration certificate. Accordingly, there is a risk that any payment of fees or commissions by the City to the Bank pursuant to, or in connection with, the Loan Agreement may be deemed to constitute "service payments to non-residents" and be subject to review by the relevant state agency pursuant to the NBU regulation described above. There can be no assurance that in such event the relevant state agency will not determine that the fees are excessive, or refuse to carry out a review of the fees, or that the NBU will (if requested) issue a special permission, in which case (absent a court decision overruling such decision) it may not be possible to pay such fees and commissions.

Proceeds available to Noteholders under security given pursuant to the Trust Deed might be reduced under the German Insolvency Code.

Under the German Insolvency Code, receivables assigned for security purposes may be subject to deductions. Clause 4 of the Trust Deed provides for, *inter alia*, an English law charge in favour of the Trustee for the benefit of Noteholders over certain receivables of the Bank under the Loan Agreement. Section 166(2) of the German Insolvency Code provides that receivables assigned for security purposes may, after the commencement of insolvency proceedings, not be enforced by the assignee but by the insolvency administrator which will be entitled to deduct from the gross enforcement proceeds a lump-sum of 9 per cent. of the gross enforcement proceeds consisting of 4 per cent. as cost of determination and 5 per cent. as costs for realisation. However, the 5 per cent. component may be increased or decreased by any substantial amount by which the actual costs of realisation exceed or fall below 5 per cent. of the enforcement proceeds. Value added tax will be deducted to the extent payable by the insolvent estate in connection with the realisation. Should the Bank become unable to make payments with respect to the Notes, the proceeds that are available for distribution to Noteholders under the security created pursuant to Clause 4 of the Trust Deed might therefore be reduced by 9 per cent. as increased or decreased and by an amount reflecting the actual

costs of realisation and value added tax, since it cannot be excluded that a German court would hold that an English law charge should be subject to Section 166(2) of the German Insolvency Code.

The same may apply if the secured property is capable of being enforced by the Trustee but the Trustee does not enforce the security interests within the time limit specified by the insolvency court. Where the insolvency administrator waives his right of realisation in favour of the Trustee, the Trustee is nevertheless obliged to transfer to the estate 4 per cent. of the gross enforcement proceeds as costs of determination, as well as the amount of any value added tax, if applicable.

Interest payments under the Loan may not qualify for the reduced rate of withholding tax under the applicable double taxation treaty.

In general, payments of interest on borrowed funds by a Ukrainian entity to a non-resident person are subject to Ukrainian withholding tax at the rate of 15 per cent., absent reduction or exemption pursuant to the terms of an applicable tax treaty. Based on professional advice it has received, the City believes that, under the terms of the double taxation treaty between Ukraine and the Federal Republic of Germany (the “Double Taxation Treaty”), payments of interest on the Loan are currently subject to a 2 per cent. withholding tax on the gross amount of such interest payments, provided that certain conditions set forth in the Double Taxation Treaty and under applicable Ukrainian legislation are duly satisfied. Under the Loan Agreement, the City will be required to gross up payments in respect of such withholding tax at a rate of up to 2 per cent. However, there can be no assurance that such reduced rate of withholding tax under the Double Taxation Treaty is or will continue to be available.

Specifically, in order for the reduced rate of withholding under the Double Taxation Treaty to be applicable, the Bank must be the beneficial owner of the interest payments being received in Germany. While the City believes the Bank will be treated as the beneficial owner of the income in question, the notion of beneficial ownership is not well defined, either in Ukrainian or in international tax law. As a consequence, different interpretations are possible and the position could be taken that the Bank should not be viewed as the beneficial owner of the interest payments being received in Germany. However, the City believes that it is unlikely that the Ukrainian authorities will adopt this view. See “Taxation – Ukrainian Tax Considerations – Withholding Tax on Interest Payments and Principal Repayments Under the Loan”.

The City may, in certain circumstance, be required to gross up amounts payable under the Loan, but such gross-up clause may be unenforceable under Ukrainian law and this could lead to a default under the Loan Agreement.

To the extent that any payments (including payments of interest) under the Loan Agreement are subject to any withholding tax (other than in respect of applicable withholding tax at a rate of up to 2 per cent.), as a result of which the Bank would reduce payments under the Notes in the amount of such withholding tax, the City may, in certain circumstances specified in the Loan Agreement and subject to certain exceptions relating to the maintenance by the Bank of its residence in a qualifying jurisdiction, become obliged to pay such Additional Amounts (as defined in the Loan Agreement) as may be necessary so that the net payments received by the Bank will not be less than the amount the Bank would have received in the absence of such withholding tax.

In addition, in certain cases, interest payments on the Notes by the Bank to Noteholders who are German tax residents may be subject to German withholding tax, which would reduce the amounts received by such Noteholders under the Notes. In such cases, the Bank will not pay any Additional Amounts unless it has received such funds from the City. Furthermore, interest payments on the Notes by the Bank to Noteholders who are not German tax residents may be subject to German withholding tax if the Notes are issued in definitive form and interest is paid directly to such Noteholders. Based on professional advice the City has received, the City believes that payments in respect of the Notes will only be subject to deduction or withholding for or on account of German or Ukrainian taxes as described in “Taxation – Ukrainian Tax Considerations – Withholding Tax on Interest Payments and Principal Repayments under the Loan”.

While there is doubt as to whether the tax gross-up clause contained in the Loan Agreement is enforceable under Ukrainian law, a failure by the City to pay additional amounts, where applicable, would constitute an event of default under the Loan Agreement. If, as a result of changes in the Double Taxation Treaty or certain other laws, the City would become obliged to pay Additional Amounts (other than additional amounts payable in respect of applicable Ukrainian withholding tax at a rate of up to 2 per cent.), under certain circumstances the City may prepay the Loan at its principal amount, together with accrued but unpaid interest, and Additional Amounts, if any, and Tax

Indemnity Amounts, if any, and thereupon (subject to receipt of the relevant funds from the City) all outstanding Notes will be prepaid by the Bank.

If the Trustee enforces the Security under the Trust Deed, payments under the Loan Agreement may lose the benefit of the applicable double taxation treaty and may become subject to Ukrainian withholding tax.

In the event that the Trustee enforces the security under the Trust Deed, the Trustee will be entitled to payments of principal and interest under the Loan Agreement. Consequently, payments under the Loan Agreement may then cease to have the benefit of the Double Taxation Treaty and consequently may become subject to Ukrainian withholding tax. Except in respect of applicable withholding tax at a rate of up to 2 per cent., the City will not be required to gross up payments under the Loan Agreement in such circumstances and consequently Noteholders will receive payments net of any such withholding tax and will have no right to require their Notes to be prepaid

If the Bank ceases to be resident in a qualifying jurisdiction for purposes of the Loan Agreement, payments of interest under the Loan Agreement will be subject to Ukrainian withholding tax.

Payments of interest under the Loan Agreement will be subject to Ukrainian withholding tax at the rate of 15 per cent. if the Bank or any successor or assign of the Bank ceases to be resident in a Qualifying Jurisdiction (as defined in Clause 1 of the Loan Agreement), or if the Bank or any successor or assign of the Bank takes any action that would render the Double Taxation Treaty inapplicable. Where this is the case, except in respect of applicable withholding tax at a rate of up to 2 per cent., the City will only be required to gross up payments in the event that the Bank or any successor or assign of the Bank ceases to be resident in a Qualifying Jurisdiction by reason of a change of law, or if the Double Taxation Treaty is amended or repudiated, after the date of the Loan Agreement. Consequently, should the Bank cease to be resident in a Qualifying Jurisdiction in any other circumstances, the City will have no obligation to gross up and no right to prepay the Loan. As a result, Noteholders will receive payments under the Notes net of such withholding and will have no right to require their Notes to be prepaid.

The lack of clarity under Ukrainian legislation may mean that the City is not duly authorised to take out the loan from the Bank.

The City believes that, prior to the Issue Date, it will have obtained all authorisations required under Ukrainian legislation to obtain the Loan and to enter into, and to perform its obligations under, the Loan Agreement and the other agreements related thereto. However, the Loan represents only the second municipal loan obtained under the procedure for the making of a municipal borrowing pursuant to the Regulations on the Carrying Out of Borrowings to Local Budgets, approved by Regulation of the Cabinet of Ministers of Ukraine No. 207 dated 24th February 2003 ("Regulation 207"). Certain requirements of Regulation 207 lack clarity, and (notwithstanding the municipal loan obtained pursuant to this procedure in 2003), there is no established practice for their implementation. In particular, it is not certain whether the Loan would be deemed sufficiently authorised by a resolution of the City Council approving the principal terms of all of the external borrowings of the City for the 2004 budget year. Such a resolution has been passed by the City in relation to the Loan and the Ministry of Finance has issued an official explanation to the City that such a resolution of the City Council approving the principal terms of all of the external borrowings of the City for the 2004 budget year need not contain a specific authorisation of the terms of the relevant loan agreement. However, there remains some doubt as to whether a separate resolution of the City containing a more specific approval of the terms of the Loan Agreement and the related agreements is required. Were there to be an adverse interpretation of Regulation 207 in this regard, the validity of the Loan Agreement may be subject to challenge as a matter of Ukrainian law.

There is no existing market for the Notes.

While application has been made to list the Notes on the Luxembourg Stock Exchange, there can be no assurance that an active trading market for the Notes will develop or, if one does develop, that it will be maintained. If an active trading market for the Notes does not develop or is not maintained, the market price and liquidity of the Notes may be adversely affected.

The market for securities of Ukrainian issuers is volatile.

The market for securities issued, directly or otherwise, by Ukrainian issuers is influenced by economic and market conditions in Ukraine and, to varying degrees, market conditions in the Russian Federation and other Eastern European countries and elsewhere. Access by Ukrainian issuers to international financial markets has been significantly limited since the emerging market financial crisis

of August 1998. There can be no assurance that similar events will not recur and cause market volatility or significant illiquidity and/or adversely affect the price of the Notes.

In the event that some Noteholders elect to exercise their put option, non-electing Noteholders may be adversely affected by a reduced liquidity of their Notes.

Under the Terms and Conditions of the Notes, Noteholders will have a right (the “Put Option”) to require the Issuer to redeem their Notes at par on 15 July 2007. In the event that the Put Option is exercised by only some of the Noteholders, any Noteholders who fail to exercise the Put Option will hold Notes whose liquidity will be reduced as a result of the decreased amount of Notes outstanding. See “Terms and Conditions of the Notes – Redemption at the option of Noteholders”.

In the event that some or all of the Noteholders elect to exercise their put option, the City may not have the funds necessary to finance the redemption of Notes required by the Terms and Conditions of the Notes and the Loan Agreement.

Under the Terms and Conditions of the Notes, Noteholders will have a right (the “Put Option”) to require the Issuer to redeem their Notes at par on 15 July 2007. However, in the event that the Put Option is exercised by some or all of the Noteholders, it is possible that the City will not have sufficient funds to make the required prepayments of the Loan to enable the Issuer to redeem the Notes in accordance with the Loan Agreement. See “Terms and Conditions of the Notes – Redemption at the option of Noteholders” and “Terms of the Loan Agreement – Prepayment – Prepayment in the event of the exercise of any Put Option”.

A negative change in Ukraine’s or the City’s credit rating could adversely affect the price of the Notes.

Ukraine sovereign bonds are rated “B (stable outlook)” by Standard & Poor’s Rating Service, a division of The McGraw Hill Companies, Inc., and “B2 (stable outlook)” by Moody’s Investors Service, Inc. A security rating is not a recommendation to buy, sell or hold securities and may be subject to revision or withdrawal at any time by the assigning rating organization. The City has received a rating of “B (stable outlook)” from Standard & Poor’s Rating Service and “B2 (stable outlook)” from Moody’s Investors Service, Inc. Any negative change in Ukraine’s or the City’s own credit rating could materially adversely affect the market price of the Notes.

DESCRIPTION OF THE TRANSACTION AND THE SECURITY

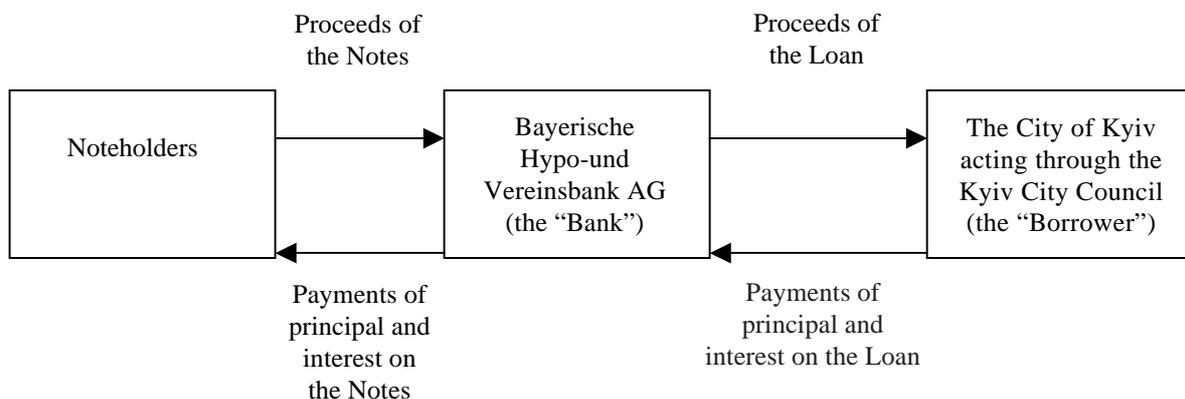
The transaction will be structured as a loan to the City by the Bank.

The Bank will issue the Notes, which will be limited recourse loan participation notes, for the sole purpose of funding the Loan to the City. The Notes will have the benefit of, and be constituted by, the Trust Deed. As provided in the Trust Deed, the Bank will (a) charge and pledge by way of security to the Trustee its rights to principal, interest and other amounts under the Loan Agreement (other than Reserved Rights (as defined in the Trust Deed); (b) charge and pledge by way of security to the Trustee sums held on deposit in an account with Deutsche Bank AG London, account number 0313943, in the name of the Bank together with the debt represented thereby (the "Account") pursuant to the Trust Deed; and (c) transfer its administrative rights under the Loan Agreement to the Trustee, for the benefit of the Noteholders. The Borrower will be obliged to make payments under the Loan to the Account in accordance with the terms of the Loan Agreement. The Bank will agree in the Trust Deed not to agree to any amendments to or any modification or waiver of, or authorise any breach or proposed breach of, the terms of the Loan Agreement unless the Trustee has given its prior written consent or except as otherwise expressly provided in the Trust Deed and Loan Agreement. The Bank will further agree to act at all times in accordance with any instructions of the Trustee from time to time with respect to the Loan Agreement, save as otherwise provided in the Trust Deed. Any amendments, modifications, waivers or authorisations made with the Trustee's consent shall be notified to the Noteholders in accordance with Condition 14 of the Terms and Conditions of the Notes and shall be binding on the Noteholders. The Bank will also agree in the Agency Agreement to require the Borrower to make all payments under the Loan Agreement to the Account. Formal notice of the security interests created by the Trust Deed will be given to the Borrower, Deutsche Bank AG London and Deutsche Bank Luxembourg S.A., who will each be required to acknowledge the same.

In the event that the Trustee enforces the security interests granted to it, the Trustee will assume certain rights and obligations towards the Noteholders as more fully set out in the Trust Deed.

This offering is made on a limited recourse basis, and the Bank will not have any obligations to the Noteholders save for the obligation to account to the Noteholders in respect of the payments of principal and interest under the Loan if, and only to the extent, received from the Borrower and retained, less amounts in respect of Reserved Rights (as defined in "Terms and Conditions of the Notes") that the Bank is entitled to retain from any amounts actually received.

Application has been made to list the Notes on the Luxembourg Stock Exchange.



USE OF PROCEEDS

The proceeds from the offering of the Notes, being US\$200,000,000, will be used by the Bank for the sole purpose of financing the Loan. The net proceeds of the Loan available to the City, after deducting discounts, fees and expenses incurred in connection with the offering, will be approximately US\$198.7 million. The City will apply the net proceeds of the Loan towards the satisfaction of the City's budgetary expenditure objectives, particularly through capital investments in the areas of transportation infrastructure and public utilities. In particular, the City expects to use the majority of the proceeds on the construction of the new Podilskiy bridge over the Dnipro River. Part of the proceeds will also be used to construct a new waste recycling plant and to build a special cardiology unit. See "City Budget and Financial Information – Budget Expenditures – Construction".

TERMS AND CONDITIONS OF THE NOTES

The following is the text of the Terms and Conditions of the Notes, which will be endorsed on each Note in definitive form. The terms and conditions applicable to any Note in global form will differ from those terms and conditions which would apply to the Note were it in definitive form to the extent described under "Summary of Provisions Relating to the Notes while in Global form" below.

The US\$200,000,000 8.625 per cent. Puttable Loan Participation Notes due 2011 (the "Notes", which expression includes any further notes issued pursuant to Condition 13 (*Further Issues*) and forming a single series therewith) of Bayerische Hypo- und Vereinsbank AG (the "Issuer") are constituted by, are subject to, and have the benefit of, a trust deed dated 22 July 2004 (as amended or supplemented from time to time, the "Trust Deed") between the Issuer and Deutsche Trustee Company Limited as trustee (the "Trustee", which expression includes all persons for the time being trustee or trustees appointed under the Trust Deed) and are the subject of an agency agreement dated 22 July 2004 (as amended or supplemented from time to time, the "Agency Agreement") between the Issuer, Deutsche Bank Trust Company Americas as registrar (the "Registrar", which expression includes any successor registrar appointed from time to time in connection with the Notes), Deutsche Bank AG London as principal paying agent (the "Principal Paying Agent", which expression includes any successor principal paying agent appointed from time to time in connection with the Notes), the transfer agents named therein (the "Transfer Agents", which expression includes any successor or additional transfer agents appointed from time to time in connection with the Notes), the paying agents named therein (together with the Principal Paying Agent, the "Paying Agents", which expression includes any successor or additional paying agents appointed from time to time in connection with the Notes) and the Trustee. References herein to the "Agents" are to the Registrar, the Principal Paying Agent, the Transfer Agents and the Paying Agents and any reference to an "Agent" is to any one of them. Certain provisions of these Conditions are summaries of the Trust Deed and the Agency Agreement and subject to their detailed provisions. The Noteholders (as defined below) are entitled to the benefit of, bound by, and are deemed to have notice of, all the provisions of the Trust Deed and are deemed to have notice of those provisions of the Agency Agreement applicable to them. Copies of the Trust Deed and the Agency Agreement are available for inspection during normal business hours at the registered office for the time being of the Trustee, being at the date hereof Winchester House, 1 Great Winchester Street, London EC2N 2DB and at the Specified Offices (as defined in the Agency Agreement) of each of the Agents, the initial Specified Offices of which are set out below.

The Issuer authorised the creation, issue and sale of the Notes for the sole purpose of financing the US\$200,000,000 loan (the "Loan") to Kyiv City Council (the "Borrower"). The Issuer and the Borrower have recorded the terms of the Loan in an agreement dated 15 July 2004 between the Issuer, as lender, and the borrower (as amended and supplemented from time to time, the "Loan Agreement").

In each case where amounts of principal, interest and additional amounts, if any, due pursuant to Condition 6 (*Payments*) and Condition 7 (*Taxation*) are stated herein or in the Trust Deed to be payable in respect of the Notes, the obligation of the Issuer to make any such payment shall constitute an obligation only to pay to the Noteholders (as defined in Condition 2(a)), on each date upon which such amounts of principal, interest and additional amounts, if any, are due in respect of the Notes, to the extent of the sums of principal, interest, Additional Amounts and Tax Indemnity Amounts (each as defined in the Loan Agreement), if any, actually received by or for the account of the Issuer pursuant to the Loan Agreement, less any amounts in respect of the Reserved Rights (as defined below). Noteholders must therefore rely solely and exclusively upon the covenant to pay under the Loan Agreement and the credit and financial standing of the Borrower. Noteholders shall have no recourse (direct or indirect) to any other assets of the Issuer.

As security for the Issuer's payment obligations under the Trust Deed and in respect of the Notes, the Issuer has:

- (A) charged by way of security to the Trustee all of the Issuer's rights, interests and benefits in and to (i) principal, interest and other amounts now or hereafter paid and payable by the Borrower to the Issuer as lender under the Loan Agreement and (ii) all amounts now or hereafter paid or payable by the Borrower to the Issuer under or in respect of any claim, award or judgment relating to the Loan Agreement (in each case other than its right to amounts in respect of any rights, interests and benefits of the Issuer under the following clauses of the Loan Agreement: Clause 7.3 second sentence thereof (*Costs of Prepayment*); Clause 8.3(a) (*Tax Indemnity*); Clause 10 (*Changes in Circumstances*); Clause 11 (*Representations and Warranties of the Borrower*);

Clause 16 (*Default Interest and Indemnity*); Clause 20 (*Fees, Costs and Expenses*); (to the extent that the Issuer's claim is in respect of one of the aforementioned clauses of the Loan Agreement) Clause 8.2 (*Payments*), Clause 18.2 (*Currency Indemnity*) and Clause 19.3 (*No Set Off*) (such rights are referred to herein as the "Reserved Rights");

- (B) charged by way of security to the Trustee all of the Issuer's rights, interests and benefits in and to all sums held on deposit from time to time, in the Collection Account (as defined in the Loan Agreement) with the Principal Paying Agent (as defined below), together with the debt represented thereby (except to the extent such debt relates to Reserved Rights) pursuant to the Trust Deed (this sub-clause (B), together with sub-clause (A) other than the Reserved Rights, the "Charged Property"); and
- (C) assigned absolutely by way of security to the Trustee all of the Issuer's rights, interests and benefits whatsoever, both present and future, whether proprietary, contractual or otherwise under or arising out of or evidenced by the Loan Agreement (including, without limitation, the right to declare the Loan immediately due and payable and to take proceedings to enforce the obligations of the Borrower thereunder) other than the Charged Property and the Reserved Rights and amounts payable by the Borrower in relation to the Charged Property and the Reserved Rights (the "Transferred Rights"),

together, the "Security Interests".

In certain circumstances, the Trustee can (subject to it being indemnified and/or secured to its satisfaction) be required by Noteholders holding at least one-quarter of the principal amount of the Notes outstanding or by an Extraordinary Resolution (as defined in the Trust Deed) of the Noteholders to exercise certain of its powers under the Trust Deed (including those arising in connection with the Security Interests).

1. Form, Denomination and Status

- (a) *Form and denomination*: The Notes are in registered form, without interest coupons attached, in the denominations of US\$2,000 and integral multiples of US\$1,000 in excess thereof except that Notes issued to "qualified institutional buyers" (as defined in, and in accordance with, Rule 144A under the U.S. Securities Act of 1933, as amended (the "Securities Act")) will be issued, and may be transferred, only in an amount not less than US\$100,000 and integral multiples of US\$1,000 in excess thereof (each, an "Authorised Holding").
- (b) *Status*: The sole purpose of the issue of the Notes is to provide the funds for the Issuer to finance the Loan. The Notes constitute the obligation of the Issuer to apply an amount equal to the principal amount of the Notes solely for financing the Loan and to account to the Noteholders for an amount equivalent to sums of principal, interest, Additional Amounts and Tax Indemnity Amounts, if any, actually received by or for the account of the Issuer pursuant to the Loan Agreement (less any amounts in respect of Reserved Rights), the right to receive which is, *inter alia*, being charged by way of security to the Trustee by virtue of the Security Interests as security for the Issuer's payment obligations under the Trust Deed and in respect of the Notes.

Payments in respect of the Notes to the extent of the sums actually received by or for the account of the Issuer by way of principal, interest, Additional Amounts or Tax Indemnity Amounts, if any, pursuant to the Loan Agreement (less any amounts in respect of the Reserved Rights) will be made *pro rata* among all Noteholders (subject to Condition 7 (*Taxation*)), on the dates on which such payments are due in respect of the Notes subject to the conditions attaching to, and in the currency of, such payments under the Loan Agreement. The Issuer shall not be liable to make any payment in respect of the Notes other than as expressly provided herein and in the Trust Deed. The Issuer shall be under no obligation to exercise in favour of the Noteholders any rights of set-off or of banker's lien or to combine accounts or counterclaim that may arise out of other transactions between the Issuer and the Borrower.

Noteholders are deemed to have accepted that:

- (i) neither the Issuer nor the Trustee makes any representation or warranty in respect of, and shall at no time have any responsibility for, or (save as otherwise expressly provided in the Trust Deed and paragraph (vi) below) liability, or obligation in respect of the performance and observance by the Borrower of its obligations under the Loan Agreement or the

recoverability of any sum of principal, interest, Additional Amounts or Tax Indemnity Amounts or other amounts, if any, due or to become due from the Borrower under the Loan Agreement;

- (ii) neither the Issuer nor the Trustee shall at any time have any responsibility for, or obligation or liability in respect of, the condition (financial, operational or otherwise), creditworthiness, affairs, status, nature or prospects of the Borrower;
- (iii) neither the Issuer nor the Trustee shall at any time have any responsibility for, or obligation or liability in respect of, any misrepresentation or breach of warranty or any act, default or omission of the Borrower under or in respect of the Loan Agreement;
- (iv) neither the Issuer nor the Trustee shall at any time have any responsibility for, or liability or obligation in respect of, the performance and observance by the Registrar, the Principal Paying Agent, any Transfer Agent or any Paying Agent of their respective obligations under the Agency Agreement;
- (v) the financial servicing and performance of the terms of the Notes depend solely and exclusively upon performance by the Borrower of its obligations under the Loan Agreement, its covenant to pay under the Loan Agreement and its credit and financial standing. The Borrower has represented and warranted to the Issuer in the Loan Agreement that the Loan Agreement constitutes legal, valid and binding obligations of the Borrower. The representations and warranties given by the Borrower in Clause 11 (*Representations and Warranties of the Borrower*) of the Loan Agreement are given by the Borrower to the Issuer for the sole benefit of the Issuer and neither the Trustee nor any Noteholder shall have any remedies or rights against the Borrower that the Issuer may have with respect to such representations or warranties, other than any right the Trustee may have pursuant to the assignment of the Transferred Rights;
- (vi) the Issuer (and, pursuant to the assignment of the Transferred Rights, the Trustee) will rely on self-certification by the Borrower and certification by third parties as a means of monitoring whether the Borrower is complying with its obligations under the Loan Agreement and shall not otherwise be responsible for investigating any aspect of the Borrower's performance in relation thereto and, subject as further provided in the Trust Deed, the Trustee will not be liable for any failure to make the usual or any investigations which might be made by a security holder in relation to the property which is the subject of the Security Interests and held by way of security for the Notes, and shall not be bound to enquire into or be liable for any defect or failure in the right or title of the Issuer to the secured property represented by the Security Interests whether such defect or failure was known to the Trustee or might have been discovered upon examination or enquiry or whether capable of remedy or not, nor will it have any liability for the enforceability of the security created by the Security Interests whether as a result of any failure, omission or defect in registering or filing or otherwise protecting or perfecting such security and the Trustee will have no responsibility for the value of such security; and
- (vii) if the Borrower is required by law to make any withholding or deduction for or on account of tax from any payment under the Loan Agreement or if the Issuer is required by law to make any withholding or deduction for or on account of tax from any payment in respect of the Notes, the sole obligation of the Issuer will be to pay the Noteholders sums equivalent to the sums actually received from the Borrower pursuant to the Loan Agreement in respect of such payment, including, if applicable, Additional Amounts or Tax Indemnity Amounts in respect of the tax required to be so withheld or deducted; the Issuer shall not be obliged to take any actions or measures as regards such deductions or withholdings other than those set in Clause 8 (*Taxes*) and Clause 10.4 (*Mitigation*) of the Loan Agreement.

Save as otherwise expressly provided herein and in the Trust Deed, no proprietary or other direct interest in the Issuer's rights under or in respect of the Loan Agreement or the Loan exists for the benefit of the Noteholders. Subject to the terms of the Trust Deed, no Noteholder will have any entitlement to enforce any of the provisions in the Loan Agreement or have direct recourse to the Borrower except through action by the Trustee under the Security Interests. Neither the Issuer nor the Trustee pursuant to the Transferred Rights shall be required to take proceedings to enforce payment under the Loan Agreement unless it has been indemnified and/or

secured by the Noteholders to its satisfaction against all liabilities, proceedings, claims and demands to which it may thereby become liable and all costs, charges and expenses which may be incurred by it in connection therewith.

As provided in the Trust Deed, the obligations of the Issuer are solely to make payments of amounts in aggregate equal to principal, interest, Additional Amounts, Tax Indemnity Amounts or other amounts, if any, actually received by or for the account of the Issuer pursuant to the Loan Agreement (less any amounts in respect of Reserved Rights), the right to which is being charged by way of security to the Trustee as aforesaid. Noteholders must therefore rely solely and exclusively upon the covenant to pay under the Loan Agreement and the credit and financial standing of the Borrower.

The obligations of the Issuer to make payments as stated in the previous paragraph constitute direct and general obligations of the Issuer which will at all times rank *pari passu* and rateably without any preference among themselves.

Payments made by the Borrower under the Loan Agreement to, or to the order of, the Trustee or (before such time that the Issuer has been required by the Trustee, pursuant to the terms of the Trust Deed, to pay to or to the order of the Trustee) the Principal Paying Agent will satisfy *pro tanto* the obligations of the Issuer in respect of the Notes.

2. Register, Title and Transfers

- (a) *Register:* The Registrar will maintain outside the United Kingdom a register (the “Register”) in respect of the Notes in accordance with the provisions of the Agency Agreement. In these Conditions, the “Holder” of a Note means the person in whose name such Note is for the time being registered in the Register (or, in the case of a joint holding, the first named thereof) and “Noteholder” shall be construed accordingly. A certificate (each, a “Note Certificate”) will be issued to each Noteholder in respect of its registered holding. Each Note Certificate will be numbered serially with an identifying number which will be recorded in the Register.

The Rule 144A Global Note Certificate will be deposited with a custodian for, and title to the Notes issued in respect of the Rule 144A Global Note Certificate will be registered in the name of, a nominee of DTC. The Regulation S Global Note Certificate will be deposited with a common depositary for Euroclear and Clearstream, Luxembourg and the title to the Notes issued in respect of the Regulation S Global Note Certificate will be registered in the name of a nominee of such common depositary.

- (b) *Title:* The Holder of each Note shall (except as otherwise required by law) be treated as the absolute owner of such Note for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any other interest therein, any writing on the Note Certificate relating thereto (other than the endorsed form of transfer) or any notice of any previous loss or theft of such Note Certificate) and no person shall be liable for so treating such Holder. No person shall have any right to enforce any term or condition of the Notes or the Trust Deed under the Contracts (Rights of Third Parties) Act 1999.
- (c) *Transfers:* Subject to Condition 2(f) (*Closed periods*) and Condition 2(g) (*Regulations concerning transfers and registration*) below, a Note may be transferred upon surrender of the relevant Note Certificate, with the endorsed form of transfer duly completed (including any certificates as to compliance with restrictions on transfer included therein), at the Specified Office of the Registrar or any Transfer Agent, together with such evidence as the Registrar or (as the case may be) such Transfer Agent may reasonably require to prove the title of the transferor and the authority of the individuals who have executed the form of transfer; *provided, however, that* a Note may not be transferred unless the principal amount of Notes transferred and (where not all of the Notes held by a Holder are being transferred) the principal amount of the balance of Notes not transferred are Authorised Holdings. Where not all the Notes represented by the surrendered Note Certificate are the subject of the transfer, a new Note Certificate in respect of the balance of the Notes will be issued to the transferor.
- (d) *Registration and delivery of Note Certificates:* Within five business days of the surrender of a Note Certificate in accordance with Condition 2(c) (*Transfers*) above, the Registrar will register the transfer in question and deliver a new Note Certificate of a like principal amount to the Notes transferred to each relevant Holder at its Specified Office or (as the case may be) the Specified Office of any Transfer Agent or (at the request and risk of any such relevant Holder) by uninsured first class mail (airmail if overseas) to the address specified for the purpose by such

relevant Holder. In this paragraph, “business day” means a day on which commercial banks are open for general business (including dealings in foreign currencies) in the city where the Registrar or (as the case may be) the relevant Transfer Agent has its Specified Office.

- (e) *No charge*: The transfer of a Note will be effected without charge by or on behalf of the Issuer, the Registrar or any Transfer Agent but against such indemnity as the Registrar or (as the case may be) such Transfer Agent may require in respect of any tax or other duty of whatsoever nature which may be levied or imposed in connection with such transfer.
- (f) *Closed periods*: Noteholders may not require transfers to be registered during the period of 15 days ending on the due date for any payment of principal or interest in respect of the Notes.
- (g) *Regulations concerning transfers and registration*: All transfers of Notes and entries on the Register are subject to the detailed regulations concerning the transfer of Notes scheduled to the Agency Agreement. The regulations may be changed by the Issuer with the prior written approval of the Trustee, the Registrar and the Borrower. A copy of the current regulations will be mailed (free of charge) by the Registrar and/or any Transfer Agent to any Noteholder who requests in writing a copy of such regulations. So long as any of the Notes are listed on the Luxembourg Stock Exchange, a copy of the current regulations will be publicly available at the specified offices of the Transfer Agent and the Paying Agent in Luxembourg.

3. Issuer’s Covenant

As provided in the Trust Deed, so long as any of the Notes remain outstanding (as defined in the Trust Deed), the Issuer will not, without the prior written consent of the Trustee or an Extraordinary Resolution or Written Resolution (as defined in the Trust Deed), agree to any amendments to or any modification or waiver of, or authorise any breach or proposed breach of, the terms of the Loan Agreement and will act at all times in accordance with any instructions of the Trustee from time to time with respect to the Loan Agreement, except as otherwise expressly provided in the Trust Deed and the Loan Agreement. Any such amendment, modification, waiver or authorisation made with the consent of the Trustee shall be binding on the Noteholders and any such amendment or modification shall be notified by the Issuer to the Noteholders in accordance with Condition 14 (*Notices*).

4. Interest

- (a) *Accrual of Interest*: The Notes bear interest from 22 July 2004 (the “Issue Date”) at the rate of 8.625 per cent. per annum, (the “Rate of Interest”) payable semi-annually in arrear on 15 January and 15 July in each year (each, an “Interest Payment Date”, the first such date being 15 January 2005), except that the first payment of interest shall be made in respect of the period from (and including) the Issue Date to (but excluding) such first Interest Payment Date, all subject as provided in Condition 6 (*Payments*). Each period from (and including) the Issue Date or any Interest Payment Date to (but excluding) the next (or first) Interest Payment Date is herein called an “Interest Period”.

Each Note will cease to bear interest from the due date for redemption unless, upon due presentation, payment of principal is improperly withheld or refused, in which case it will continue to accrue interest at such rate (both before and after judgment) until whichever is the earlier of (a) the day on which all sums due in respect of such Note up to that day are received by or on behalf of the relevant Noteholder and (b) the day which is seven days after the Principal Paying Agent or the Trustee has notified the Noteholders that it has received all sums due in respect of the Notes up to such seventh day (except to the extent that there is any subsequent default in payment).

The amount of interest payable in respect of a Note for the first Interest Period shall be calculated by applying the Rate of Interest to the principal amount of such Note, multiplying the product by the quotient of the number of days in the first Interest Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days consisting of 12 months of 30 days each and, in the case of an incomplete month, the actual number of days elapsed) and rounding the resulting figure to the nearest cent (half a cent being numbered upwards). The amount of interest payable in respect of a Note for any Interest Period other than the first Interest Period shall be calculated by applying the Rate of Interest to the principal amount of such Note, dividing the product by two and rounding the resulting figure to the nearest cent (half a cent being rounded upwards). Where interest is required to be calculated in respect of a

period other than an Interest Period, it shall be calculated on the basis of a year of 360 days consisting of 12 months of 30 days each and, in the case of an incomplete month, the actual number of days elapsed.

- (b) *Default Interest under the Loan Agreement:* In the event that, and to the extent that, the Issuer actually receives any amounts in respect of interest on unpaid sums from the Borrower pursuant to Clause 16 (*Default Interest and Indemnity*) of the Loan Agreement (other than amounts so received forming part of the Reserved Rights), the Issuer shall account to the Noteholders for an amount equivalent to the amounts in respect of interest on unpaid sums actually so received. Any payments made by the Issuer under this Condition 4(b) will be made on the next following business day (as defined in Condition 6(d)) after the day on which the Issuer receives such amounts from the Borrower and, save as provided in this Condition 4(b), subject as provided in Condition 6 (*Payments*).

5. Redemption and Purchase

- (a) *Scheduled redemption:* Unless previously prepaid pursuant to Clause 7 (*Prepayment*) of the Loan Agreement or repaid in accordance with Clause 10.3 (*Illegality*) of the Loan Agreement, the Borrower will be required to repay the Loan on its due date as provided in the Loan Agreement and, subject to such repayment, all the Notes will be redeemed at their principal amount on 15 July 2011, subject as provided in Condition 6 (*Payments*).
- (b) *Redemption by the Issuer:* The Notes shall be redeemed by the Issuer in whole, but not in part, at any time, on giving not less than 25 days' nor more than 60 days' notice to the Noteholders (which notice shall be irrevocable and shall specify a date for redemption, being the same date as that set forth in the notice of prepayment referred to in Condition 5(b)(i) or (ii) below) in accordance with Condition 14 (*Notices*) at the principal amount thereof, together with interest accrued and unpaid to the date fixed for redemption and any additional amounts in respect thereof pursuant to Condition 7 (*Taxation*), if, immediately before giving such notice, the Issuer satisfies the Trustee that:
- (i) the Issuer has received a notice of prepayment from the Borrower pursuant to Clause 7.1 (*Prepayment for Tax Reasons*) of the Loan Agreement; or
 - (ii) the Issuer has delivered a notice to the Borrower, the contents of which require the Borrower to repay the Loan, in accordance with the provisions of Clause 10.3 (*Illegality*) of the Loan Agreement.

The Issuer shall deliver to the Trustee a certificate signed by two officers of the Issuer stating that the Issuer is entitled to effect such redemption in accordance with this Condition 5(b). A copy of the Borrower's notice of prepayment or details of the circumstances contemplated by Clause 10.3 (*Illegality*) of the Loan Agreement and the date fixed for redemption shall be set forth in the notice.

The Trustee shall be entitled to accept any notice or certificate delivered by the Issuer in accordance with this Condition 5(b) as sufficient evidence of the satisfaction of the applicable circumstances in which event they shall be conclusive and binding on the Noteholders.

Upon the expiry of any such notice given by the Issuer to the Noteholders as is referred to in this Condition 5(b), the Issuer shall be bound to redeem the Notes in accordance with this Condition 5, subject as provided in Condition 6 (*Payments*).

- (c) *Redemption at the option of Noteholders:*

- (i) The Issuer shall, at the option of the Holder of any Note, redeem such Note on 15 July 2007 (the "Put Settlement Date") at a price equal to 100 per cent. of its principal amount together with interest accrued to such date, plus additional amounts, if any. In order to exercise the option contained in this Condition 5(c) (the "Put Option"), the Holder of a Note must, not less than 95 nor more than 125 days before the Put Settlement Date, deposit the Note Certificate relating to such Note with any Paying Agent together with a duly completed put option notice (a "Put Option Notice") in the form obtainable from any Paying Agent. No Note Certificate, once deposited with a duly completed Put Option Notice in accordance with this Condition 5(c), may be withdrawn; *provided, however*, that if, prior to the Put Settlement Date, the Notes evidenced by any Note Certificate so deposited become immediately due and payable or, upon due presentation of any Note Certificate on the Put Settlement Date, payment of the redemption moneys is improperly

withheld or refused, such Note Certificate shall, without prejudice to the exercise of the Put Option, be returned to the Holder by uninsured first class mail (airmail if overseas) at the address specified by such Holder in the relevant Put Option Notice.

- (ii) At least 90 days prior to the Put Settlement Date, the Issuer will deliver a notice (the “Put Option Aggregate Payment Notice”) to the Trustee and the Borrower (with a copy to the Principal Paying Agent) in accordance with Condition 14 (*Notices*) setting out the aggregate payment (including the computation thereof) required to be made by the Issuer on the Put Settlement Date for all Notes in respect of which a Put Option has been properly exercised.
- (iii) Subject to and in accordance with Clause 7.2 (*Prepayment in the event of the exercise of any Put Option*) of the Loan Agreement, the Borrower will prepay the loan (together with all accrued and unpaid interest and any other amounts outstanding thereunder) in an amount equal to the aggregate payment for all Notes in respect of which a Put Option has been exercised, as set forth in the Put Option Aggregate Payment Notice delivered pursuant to Condition 5(c)(ii). On the Put Settlement Date, the Issuer will, to the extent permitted by law and subject to such prepayment, redeem in accordance with Condition 5(c)(i) all Notes in respect of which a Put Option has been properly exercised.
- (d) *No other redemption:* Except where the Loan is accelerated pursuant to Clause 15.8 (*Rights of Lender Upon Occurrence of an Event of Default*) of the Loan Agreement, the Issuer shall not be entitled to redeem the Notes prior to that due date otherwise than as provided in Condition 5(b) (*Redemption by the Issuer*) and Condition 5(c) (*Redemption at the option of Noteholders*) above.
- (e) *Purchase:* The Issuer or any of its subsidiaries or the Borrower may at any time purchase Notes in the open market or otherwise and at any price. Such Notes may be held or resold (provided that any such resale is outside the United States as defined in Regulation S under the U.S. Securities Act of 1933 (the “Securities Act”)) or surrendered by the purchaser to the Issuer for cancellation.

Notes held by the Issuer and its subsidiaries will continue to carry the right to attend and vote at meetings of Noteholders and will be taken into account in determining how many Notes are outstanding for the purposes of these Conditions and the provisions of the Trust Deed. However, Notes held by the Borrower will cease to carry such rights and will not be taken into account, inter alia, for the purposes of Conditions 11 (Meetings of Noteholders; Modification and Waiver; Substitution) and 12 (Enforcement).

- (f) *Cancellation:* All Notes redeemed or purchased and surrendered for cancellation by the Issuer shall be cancelled and all Notes purchased by the Borrower and surrendered to the Issuer pursuant to Clause 7.5 (*Purchase of Instruments Issued to the Agreed Funding Source*) of the Loan Agreement, together with an authorisation addressed to the Registrar by the Borrower, shall be cancelled.

6. Payments

- (a) *Principal:* Payments of principal shall be made by U.S. dollar cheque drawn on, or, upon application by a Holder of a Note to the Specified Office of the Principal Paying Agent not later than the fifteenth day before the due date for any such payment, by transfer to a U.S. dollar account maintained by the payee with, a bank in New York City, and shall only be made upon surrender (or, in the case of part payment only, endorsement) of the relevant Note Certificates at the Specified Office of any Paying Agent.
- (b) *Interest:* Payments of interest shall be made by U.S. dollar cheque drawn on, or upon application by a Holder of a Note to the Specified Office of the Principal Paying Agent not later than the fifteenth day before the due date for any such payment, by transfer to a U.S. dollar account maintained by the payee with, a bank in New York City and (in the case of interest payable on redemption), and shall only be made upon surrender (or, in the case of part payment only, endorsement) of the relevant Note Certificates at the Specified Office of any Paying Agent.
- (c) *Payments subject to fiscal laws:* All payments in respect of the Notes are subject in all cases to any applicable fiscal or other laws and regulations in the place of payment, but without prejudice to the provisions of Condition 7 (*Taxation*). No commissions or expenses shall be charged to the Noteholders in respect of such payments.

- (d) *Payments on business days:* Where payment is to be made by transfer to a U.S. dollar account, payment instructions (for value the due date, or, if the due date is not a business day, for value the next succeeding business day) will be initiated and, where payment is to be made by U.S. dollar cheque, the cheque will be mailed (i) (in the case of payments of principal and interest payable on redemption) on the later of the due date for payment and the day on which the relevant Note Certificate is surrendered (or, in the case of part payment only, endorsed) at the Specified Office of a Paying Agent and (ii) (in the case of payments of interest payable other than on redemption) on the due date for payment. The holder of a Note shall not be entitled to any interest or other payment in respect of any delay in payment resulting from (A) the due date for a payment not being a business day or (B) a cheque mailed in accordance with this Condition 6 (*Payments*) arriving after the due date for payment or being lost in the mail. In this paragraph, “business day” means any day on which banks are open for general business (including dealings in foreign currencies) in New York City, London, Kyiv and, in the case of surrender (or, in the case of part payment only, endorsement) of a Note Certificate, in the place in which the Note Certificate is surrendered (or, as the case may be, endorsed).
- (e) *Partial payments:* If a Paying Agent makes a partial payment in respect of any Note, the Issuer shall procure that the amount and date of such payment are noted on the Register and, in the case of partial payment upon presentation of a Note Certificate, that a statement indicating the amount and the date of such payment is endorsed on the relevant Note Certificate.
- (f) *Record date:* Each payment in respect of a Note will be made to the person shown as the Holder in the Register at the opening of business in the place of the Registrar’s Specified Office on the fifteenth day before the due date for such payment (the “Record Date”). Where payment in respect of a Note is to be made by cheque, the cheque will be mailed to the address shown as the address of the Holder in the Register at the opening of business on the relevant Record Date.
- (g) *Payment to the Collection Account:* Save as the Trustee may otherwise direct at any time after the security created pursuant to the Trust Deed becomes enforceable, the Issuer will pursuant to the provisions of Clause 7.1 of the Agency Agreement require the Borrower to make all payments of principal, interest, Additional Amounts, Tax Indemnity Amounts or other amounts, if any, to be made pursuant to the Loan Agreement, less any amounts in respect of the Reserved Rights, to the Collection Account.
- (h) *Payment obligations limited:* Notwithstanding any other provisions to the contrary, the obligations of the Issuer to make payments under Condition 5 (*Redemption and Purchase*) and Condition 6 (*Payments*) shall constitute an obligation only to pay to the Noteholders on such date upon which a payment is due in respect of the Notes, to the extent of sums of principal, interest, Additional Amounts, Tax Indemnity Amounts or other amounts, if any, actually received by or for the account of the Issuer pursuant to the Loan Agreement, less any amount in respect of the Reserved Rights.

7. Taxation

All payments by the Issuer in respect of the Notes shall be made free and clear of and without deduction or withholding for or on account of any present or future taxes, duties, assessments, fees or other governmental charges (“Taxes”) imposed or levied by or on behalf of the Federal Republic of Germany, Ukraine, any jurisdiction from or through which a payment is made, or any political subdivision or taxing authority thereof or therein in each of the preceding jurisdictions (each, a “Taxing Jurisdiction”), unless such withholding or deduction is required by law. In that event, the Issuer shall, subject as provided below, pay such additional amounts (“additional amounts”) as will result in the receipt by the Noteholders after such withholding or deduction of such amounts as would have been received by them if no such withholding or deduction had been made or required to be made. The foregoing obligation to pay additional amounts, however, will not apply to any:

- (i) Taxes that would not have been imposed but for the existence of any present or former connection between such Noteholder and the relevant Taxing Jurisdiction other than the mere receipt of such payment or the ownership or holding of such Note;
- (ii) Taxes that would not have been imposed but for the presentation by the Noteholder for payment on a date more than 30 days after a Relevant Date (as defined below);
- (iii) Taxes required to be deducted or withheld by any Paying Agent from a payment on a Note, if such payment can be made without deduction or withholding by any other Paying Agent;

- (iv) Taxes that would not have been imposed but for the failure of the Noteholder to comply with the Issuer's written request addressed to the Noteholder at least 60 days prior to the relevant payment to provide information with respect to any reasonable certification, documentation, information or other reporting requirement concerning the nationality, residence, identity or connection with the Taxing Jurisdiction of the holder of such Note;
- (v) Taxes imposed on a payment to an individual and required to be made pursuant to European Union Directive on the Taxation of Savings Income in the form of Interest Payments (Directive 2003/48/EC) or any other European Union Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive; and
- (vi) Taxes imposed or levied by or on behalf of the Federal Republic of Germany or any political subdivision of a taxing authority thereof and withheld by the Issuer in its capacity as Disbursing Agent (as defined in "Taxation-German Tax Considerations") or upon interest payments made upon the physical presentation of the Notes or coupons, if any; and
- (vii) except in respect of applicable Ukrainian withholding tax at a rate of up to 2 per cent., Taxes imposed in connection with and on account of a Relevant Event.

Notwithstanding the foregoing provisions, the Issuer shall only make payments of additional amounts to the Noteholders pursuant to this Condition 7 (*Taxation*) to the extent and at such time as it shall have actually received an equivalent amount for such purposes from the Borrower under the Loan Agreement by way of Additional Amounts or Tax Indemnity Amounts or otherwise.

To the extent that the Issuer receives a lesser sum from the Borrower under the Loan Agreement, the Issuer shall account to each Noteholder entitled to receive such additional amount pursuant to this Condition 7 (*Taxation*) for an additional amount equivalent to a *pro rata* portion of such sum (if any) as is actually received by, or for the account of, the Issuer pursuant to the provisions of the Loan Agreement on the date of, in the currency of, and subject to any conditions attaching to such payment to the Issuer.

In these Conditions, "Relevant Date" means whichever is the later of (a) the date on which the payment in question first becomes due and (b) if the full amount payable has not been received in London by the Principal Paying Agent or the Trustee on or prior to such due date, the date on which (the full amount having been so received) notice to that effect has been given to the Noteholders.

Any reference in these Conditions to principal or interest shall be deemed to include, without duplication, any additional amounts in respect of principal or interest (as the case may be) which may be payable under this Condition 7 (*Taxation*) or any undertaking given in addition to or in substitution of this Condition 7 (*Taxation*) pursuant to the Trust Deed or the Loan Agreement.

If the Issuer or the Borrower becomes subject at any time to any taxing jurisdiction other than the Federal Republic of Germany or Ukraine, as the case may be, references in these Conditions to the Federal Republic of Germany and/or Ukraine shall be construed as references to the Federal Republic of Germany and/or Ukraine and/or such other jurisdiction.

8. Prescription

Claims for principal and interest on redemption shall become void unless the relevant Note Certificates are surrendered for payment within ten years, and claims for interest due other than on redemption shall become void unless made within five years, of the appropriate Relevant Date.

9. Replacement of Note Certificates

If any Note Certificate is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the Specified Office of the Registrar and the Transfer Agent having its Specified Office in Luxembourg, subject to all applicable laws and stock exchange requirements, upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Issuer may reasonably require. Mutilated or defaced Note Certificates must be surrendered before replacements will be issued.

10. Trustee and Agents

Under separate agreement between the Borrower and the Trustee, the Trustee is entitled to be indemnified and relieved from responsibility in certain circumstances and, under the Trust Deed, to be paid its costs and expenses in priority to the claims of the Noteholders. In addition, the Trustee is

entitled to enter into business transactions with the Issuer, the Borrower and any entity relating to the Issuer or the Borrower without accounting for any profit.

In connection with the exercise by it of any of its trusts, powers, authorities and discretions (including, without limitation, any modification, waiver, authorisation, determination or substitution), the Trustee shall have regard to the general interests of the Noteholders as a class but shall not have regard to any interests arising from circumstances particular to individual Noteholders (whatever their number) and, in particular but without limitation, shall not have regard to the consequences of any such exercise for individual Noteholders (whatever their number) resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory or any political sub-division thereof and the Trustee shall not be entitled to require, nor shall any Noteholder be entitled to claim, from the Issuer, the Trustee or any other person any indemnification or payment in respect of any tax consequence of any such exercise upon individual Noteholders except to the extent already provided for in Condition 7 (*Taxation*) and/or any undertaking given in addition to, or in substitution for, Condition 7 (*Taxation*) pursuant to the Trust Deed.

In acting under the Agency Agreement and in connection with the Notes, the Agents act solely as agents of the Issuer and (to the extent provided therein) the Trustee and do not assume any obligations towards or relationship of agency or trust for or with any of the Noteholders. Under separate agreement between the Borrower and the Agents, the Agents are entitled to be indemnified and relieved from certain responsibilities in certain circumstances.

The initial Agents and their initial Specified Offices are listed below. The Issuer reserves the right (with the prior approval of the Trustee) at any time to vary or terminate the appointment of any Agent and to appoint a successor principal paying agent or registrar and additional or successor paying agents and transfer agents; *provided, however, that* the Issuer shall at all times maintain (a) a principal paying agent and a registrar, (b) a paying agent and a transfer agent in Luxembourg and New York, and (c) a paying agent with a specified office in a member state of the European Union that will not be obliged to withhold or deduct tax pursuant to European Union Directive on the Taxation of Savings Income in the form of Interest payments (Directive 2003/48/EC) or any other European Union Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced to conform to, such Directive.

Notice of any change in any of the Agents or in their Specified Offices shall promptly be given to the Noteholders in accordance with Condition 14 (*Notices*).

11. Meetings of Noteholders; Modification and Waiver; Substitution

- (a) *Meetings of Noteholders:* The Trust Deed contains provisions for convening meetings of Noteholders to consider matters relating to the Notes, including the modification of any provision of the Loan Agreement or any provision of these Conditions or the Trust Deed. Such a meeting may be convened on no less than 14 days' notice by the Trustee or the Issuer or by the Trustee upon the request in writing of Noteholders holding not less than one-tenth of the aggregate principal amount of the outstanding Notes. The quorum at any meeting convened to vote on an Extraordinary Resolution will be one or more persons holding or representing more than half of the aggregate principal amount of the outstanding Notes or, at any adjourned meeting, one or more persons holding or representing whatever the principal amount of the outstanding Notes held or represented, unless the business of such meeting includes consideration of proposals *inter alia*, (i) to change any date fixed for payment of principal or interest in respect of the Notes, (ii) to reduce the amount of principal or interest payable on any date in respect of the Notes, (iii) to alter the method of calculating the amount of any payment in respect of the Notes or the date for any such payment, (iv) to change the currency of payments under the Notes, (v) to change the quorum requirements relating to meetings or the majority required to pass an Extraordinary Resolution, (vi) to alter the governing law of the Conditions, the Trust Deed or the Loan Agreement, (vii) to change any date fixed for payment of principal or interest under the Loan Agreement, (viii) to alter the method of calculating the amount of any payment under the Loan Agreement or (ix) to change the currency of payment or, without prejudice to the rights under Condition 11(b) (*Modification of Waiver*) below, change the definition of "Event of Default" under the Loan Agreement (each, a "Reserved Matter"), in which case the necessary quorum will be one or more persons holding or representing not less than two-thirds, or at any

adjourned meeting not less than one-third, in principal amount of the Notes for the time being outstanding. Any Extraordinary Resolution duly passed at any such meeting shall be binding on all the Noteholders, whether present or not.

In addition, a resolution in writing signed by or on behalf of Noteholders of at least 90 per cent. in principal amount of the Notes outstanding who for the time being are entitled to receive notice of a meeting of Noteholders under the Trust Deed will take effect as if it were an Extraordinary Resolution. Such a resolution in writing may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Noteholders.

- (b) *Modification and waiver:* The Trustee may, without the consent of the Noteholders, agree to any modification of these Conditions or the Trust Deed or, pursuant to the Transferred Rights, the Loan Agreement (other than in respect of a Reserved Matter) which is, in the opinion of the Trustee, proper to make if, in the opinion of the Trustee, such modification will not be materially prejudicial to the interests of Noteholders and to any modification of the Notes or the Trust Deed which is of a formal, minor or technical nature or is to correct a manifest error.

In addition, the Trustee may, without the consent of the Noteholders, authorise or waive any proposed breach or breach of the Notes or the Trust Deed by the Issuer or, pursuant to the Transferred Rights, the Loan Agreement by the Borrower, or determine that any event which would or might otherwise give rise to a right of acceleration under the Loan Agreement shall not be treated as such (other than a proposed breach or breach relating to the subject of a Reserved Matter) if, in the opinion of the Trustee, the interests of the Noteholders will not be materially prejudiced thereby.

Unless the Trustee agrees otherwise, any such modification, authorisation or waiver shall be notified to the Noteholders as soon as practicable thereafter and in accordance with Condition 14 (*Notices*).

- (c) *Substitution:* The Trust Deed contains provisions under which the Issuer may, without the consent of the Noteholders, transfer the obligations of the Issuer as principal debtor under the Trust Deed and the Notes to a third party provided that certain conditions specified in the Trust Deed are fulfilled. So long as any of the Notes are listed on the Luxembourg Stock Exchange, in the event of such substitution, the Luxembourg Stock Exchange will be informed of such substitution, a supplemental offering circular will be produced and will be made publicly available at the Specified Offices of the Transfer Agent and the Paying Agent in Luxembourg and such substitution shall be notified to the Noteholders as soon as practicable thereafter and in accordance with Condition 14 (*Notices*).

12. Enforcement

At any time after an Event of Default (as defined in the Loan Agreement) or Relevant Event (as defined below) shall have occurred and be continuing, the Trustee may, at its discretion and without notice, institute such proceedings as it thinks fit to enforce its rights under the Trust Deed in respect of the Notes, but it shall not be bound to do so unless:

- (a) it has been so requested in writing by the Holders of at least one-quarter in principal amount of the outstanding Notes or has been so directed by an Extraordinary Resolution; and
- (b) it has been indemnified and/or provided with security to its satisfaction.

No Noteholder may proceed directly against the Issuer unless the Trustee, having become bound to do so, fails to do so within a reasonable time and such failure is continuing.

The Trust Deed also provides that, in the case of an Event of Default or a Relevant Event, the Trustee may, and shall if requested to do so by Noteholders of at least one-quarter in principal amount of the Notes outstanding or if directed to do so by an Extraordinary Resolution and, in either case, subject to it being secured and/or indemnified to its satisfaction, (1) require the Issuer to declare all amounts payable under the Loan Agreement by the Borrower to be due and payable (where an Event of Default has occurred and is continuing), or (2) enforce the security created in the Trust Deed in favour of the Noteholders (in the case of a Relevant Event). Upon repayment of the Loan following an Event of Default, the Notes will be redeemed or repaid at the principal amount thereof together with interest accrued to the date fixed for redemption together with any additional amounts due in respect thereof pursuant to Condition 7 (Taxation) and thereupon shall cease to be outstanding.

For the purposes of these Conditions, “Relevant Event” means the earlier of (i) the failure by the Issuer to make any payment of principal or interest on the Notes when due to the extent it is

obligated to do so pursuant to these Conditions; (ii) the filing of an application for the institution for insolvency proceedings over the assets of the Issuer in Germany; (iii) the filing of a notice of the Issuer with the Federal Authority for Financial Services Supervision (*Bundesanstalt für Finanzdienstleistungsaufsicht*) pursuant to Section 46b of the German Banking Act (*Kreditwesengesetz*); (iv) the issuance of any orders by the Federal Government with respect to the Issuer pursuant to Section 47 of the German Banking Act (*Kreditwesengesetz*), including a moratorium; or (v) the taking of any action in furtherance of the dissolution (*Auflösung*) of the Issuer.

For the avoidance of doubt, no additional amounts (other than additional amounts payable in respect of applicable Ukrainian withholding tax at a rate of up to 2 per cent.) shall be payable if and to the extent that such withholding or deduction is required following and on account of a Relevant Event.

13. Further Issues

The Issuer may from time to time, with the consent of the Borrower and without the consent of the Noteholders and in accordance with the Trust Deed, create and issue further notes having the same terms and conditions as the Notes in all respects (or in all respects except for the first payment of interest) so as to form a single series with the Notes. Such further Notes shall be issued under a deed supplemental to the Trust Deed. In relation to such further issue, the Issuer will enter into a loan agreement supplemental to the Loan Agreement with the Borrower on the same terms as the original Loan Agreement (or on the same terms except for the first payment of interest) subject to any modifications which, in the sole opinion of the Trustee, would not materially prejudice the interests of the Noteholders. The Issuer will provide a further fixed charge and absolute assignment by way of security in favour of the Trustee of its rights under such supplemental loan agreement equivalent to the rights charged and assigned as Security Interests in relation to the Issuer's rights under the original Loan Agreement which will, together with the Security Interests referred to in the Conditions, secure both the Notes and such further Notes.

14. Notices

Notices to the Noteholders will be sent to them by first class mail (or its equivalent) or (if posted to an overseas address) by airmail at their respective addresses on the Register. Any such notice shall be deemed to have been given on the fourth day after the date of mailing. In addition, so long as Notes are listed on the Luxembourg Stock Exchange and the rules of that Exchange so require, notices to Noteholders will be published on the date of such mailing in a daily newspaper of general circulation in Luxembourg (which is expected to be the *Luxemburger Wort*) or, if such publication is not practicable, in a leading English language daily newspaper having general circulation in Europe.

15. Governing Law and Jurisdiction

- (a) *Governing law:* The Notes and the Trust Deed and all matters arising from or connected with the Notes and the Trust Deed are governed by, and shall be construed in accordance with, English law.
- (b) *Jurisdiction:* The Issuer has in the Trust Deed (i) agreed for the benefit of the Trustee and the Noteholders that the courts of England shall have exclusive jurisdiction to settle any dispute (a "Dispute") arising from or connected with the Notes; (ii) agreed that those courts are the most appropriate and convenient courts to settle any Dispute and, accordingly, that it will not argue that any other courts are more appropriate or convenient; (iii) designated a person in England to accept service of any process on its behalf; (iv) consented to the enforcement of any judgment; and (v) to the extent that it may in any jurisdiction claim for itself or its assets immunity from suit, execution, attachment (whether in aid of execution, before judgment or otherwise) or other legal process, and to the extent that in any such jurisdiction there may be attributed to itself or its assets or revenues such immunity (whether or not claimed), agreed not to claim and irrevocably waived such immunity to the full extent permitted by the laws of such jurisdiction. The Trust Deed also states that nothing contained in the Trust Deed prevents the Trustee or any of the Noteholders from taking proceedings relating to a Dispute ("Proceedings") in any other courts with jurisdiction and that, to the extent allowed by law, the Trustee or any of the Noteholders may take concurrent Proceedings in any number of jurisdictions.

There will appear at the foot of the Conditions endorsed on or (as the case may be) attached to each Individual Note Certificate the names and Specified Offices of the Registrar, the Paying Agents and the Transfer Agents as set out at the end of this Offering Circular.

TERMS OF THE LOAN AGREEMENT

The following is the text of the Loan Agreement, which has been entered into between the Bank and the Borrower.

THIS AGREEMENT is made on 15 July 2004

BETWEEN:

- (1) THE KYIV CITY COUNCIL, a legal entity under the laws of Ukraine, whose principal office is at 36 Khreshchatyk Street, 01044 Kyiv, Ukraine (the "Borrower"), represented by Mr Oleksandr Omelchenko, the Kyiv City Mayor, acting pursuant to the authority granted under applicable Ukrainian legislation; and
- (2) BAYERISCHE HYPO- UND VEREINSBANK AG a bank established under the laws of Germany and whose registered office is at Am Tucherpark 16, 80538 Munich, Germany (the "Lender").

WHEREAS:

- (A) The Borrower is seeking funds for the satisfaction of the budgetary expenditure objectives of the City of Kyiv, particularly to finance investments and expenditures in the areas of capital construction, transportation infrastructure (including the construction of the Podilsky bridge over the Dnipro River) and public utilities.
- (B) The Lender is willing to provide financing to the Borrower pursuant to the terms and conditions set forth in this Agreement.

It is agreed as follows:

1. DEFINITIONS AND INTERPRETATION

1.1 Definitions

In this Agreement the following terms have the meanings given to them in this Clause 1.1:

"**Acceleration Notice**" has the meaning set forth in Clause 15.8 (*Rights of Lender upon Occurrence of an Event of Default*).

"**Additional Amounts**" has the meaning set forth in sub-clause 8.1.1 (*Additional Amounts*).

"**Agency**" means any agency, authority, central bank, department, committee, government, legislature, minister, ministry, official or public or statutory Person (whether autonomous or not) of, or the government of, any state and, for the avoidance of doubt, includes the legislature and administration of the Borrower.

"**Agreed Funding Source**" shall mean any Person to whom the Lender owes any Indebtedness (including securities), which Indebtedness was incurred solely and expressly to fund the Loan (including a designated representative of such Person).

"**Agreed Funding Source Agreements**" means the Trust Deed; the Notes; the subscription agreement dated 15 July 2004 in respect of the Notes between the Lender, the Borrower and Deutsche Bank Securities Inc. and Morgan Stanley & Co. International Limited, as joint lead managers, and the managers referred to therein; the agency agreement to be dated on or about 22 July 2004 among the Lender, Deutsche Bank AG London, as principal paying agent and paying agent, Deutsche Bank Luxembourg S.A. as Luxembourg paying agent and transfer agent, Deutsche Bank Trust Company Americas as registrar, paying agent and transfer agent, and Deutsche Trustee Company Limited, as trustee; in each case as amended from time to time; and any other agreements entered into in connection with the Agreed Funding Source.

"**Budget Accounts**" means the 2003 Budget of the Borrower, as approved by Resolution No. 232/392 of the Kyiv City Council dated 28 December 2002 "On the Budget of the City of Kyiv for the Year 2003" as amended on 29 May 2003, 26 June 2003 and 31 July 2003, together with any further amendments thereto, the report on the execution of the 2003 Budget of the Borrower as approved by Resolution No. 151/1361 of the Kyiv City Council dated 15 April 2004 and the 2004 Budget of the Borrower, as approved by Resolution No. 267/1142 of the Kyiv City Council dated 18 December 2003 "On the Budget of the City of Kyiv for the Year 2004" as amended on 18 March 2004 and 15 April 2004, together with any further amendments thereto.

“**Business Day**” means any day (other than a Saturday or Sunday) on which banks generally are open for general business (including dealings in foreign currencies) in New York City, London and Kyiv.

“**Capital Adequacy Requirements**” means a request or requirement relating to the maintenance of capital, including one which makes any change to, or is based on any alteration in, the interpretation of the International Convergence of Capital Measurement and Capital Standards (a paper prepared by the Basle Committee on Banking Regulations and Supervision, dated July 1988, and amended in November 1991) or which increases the amounts of capital required thereunder, other than a request or requirement made by way of implementation of the International Convergence of Capital Measurement and Capital Standards in the manner in which it is being implemented at the date hereof.

“**Change of Law**” means any of the enactment or introduction of any new law; the variation, amendment or repeal of an existing or new law; any ruling on or interpretation or application by a competent authority of any existing or new law; and the decision or ruling on, the interpretation or application of, or a change in the interpretation or application of, any law by any court of law, tribunal, central bank, monetary authority or agency or any Taxing Authority or fiscal or other competent authority or agency; which, in each case, occurs after the date hereof. For this purpose the word “law” means all or any of the following whether in existence at the date hereof or introduced hereafter and with which it is obligatory or customary for banks or other financial institutions or, as the case may be, companies in the relevant jurisdiction to comply:

- (a) any statute, treaty, order, decree, instruction, letter, directive, instrument, regulation, ordinance or similar legislative or executive action by any national or international or local government or authority or by any ministry or department thereof and other agencies of state power and administration (including, but not limited to, taxation departments and authorities); and
- (b) any letter, regulation, decree, instruction, request, notice, guideline, directive, statement of policy or practice statement given by, or required of, any central bank or other monetary authority, or by or of any Taxing Authority or fiscal or other authority or agency (whether or not having the force of law).

“**City Assets**” means all of the assets which constitute the communal (municipal) property of the territorial community of the City of Kyiv and in respect of which the Borrower and/or any Relevant Entity exercise(s) ownership rights, management rights or any similar rights, and all of the undertakings, receivables, budget revenues and monetary funds of the Borrower and/or any Relevant Entity, to the extent that such assets, property, undertakings, receivables, revenues and/or funds can be subject to a Security Interest, present or future, to secure the Indebtedness of the Borrower or any Relevant Entity.

“**Collection Account**” means an account of the Lender with Deutsche Bank AG London, Collection Account Number 0313943.

“**Conditions**” means the terms and conditions of the Notes as scheduled to the agreed form of the Trust Deed as the same may be modified prior to the Drawdown Date.

“**Conditions Precedent**” has the meaning set forth in Clause 3 (*Availability of the Loan*).

“**Default**” means any event that is, or after notice or passage of time or both would be, an Event of Default.

“**Disbursement Account**” means such account of the Borrower in Ukraine, the details of which the Borrower shall have advised the Lender in writing prior to the Drawdown Date.

“**Dispute**” has the meaning set forth in Clause 25.2 (*English Courts*).

“**Drawdown Date**” has the meaning set forth in Clause 3 (*Availability of the Loan*).

“**Event of Default**” has the meaning set forth in Clause 15.1 (*Circumstances which Constitute Events of Default*).

“**Germany**” means the Federal Republic of Germany and any political sub-division or agency thereof or therein.

“**Indebtedness**” means any legal obligation for the payment or repayment of borrowed money.

“Interest Payment Date” means 15 January and 15 July of each year in which the Loan remains outstanding, being the last day of the corresponding Interest Period, or if such day is not a Business Day, the next succeeding Business Day, the first such date being 15 January 2005, and the last such date being the Repayment Date.

“Interest Period” means, except as otherwise provided herein, any of those periods mentioned in Clause 4 (*Interest Periods*).

“Interest Rate” means, except as otherwise provided herein, the interest rate specified in Clause 5.2 (*Calculation of Interest*).

“law” means any statute, treaty, order, decree, instruction, letter, directive, instrument, regulation, ordinance or similar legislative or executive action by any national or international or local government or authority or by any ministry or department thereof and other agencies of state power and administration (including, but not limited to, taxation departments and authorities), whether in existence at the date hereof or introduced hereafter.

“Loan” has the meaning set forth in Clause 2 (The Loan).

“Notes” means the \$200,000,000 8.625 per cent. Puttable Loan Participation Notes due 2011 of the Lender to be issued on or about 22 July 2004 for the sole purpose of financing the Loan.

“Offering Circular” means the offering circular dated on or about 15 July 2004, relating to the issuance of the Notes by the Lender to the Agreed Funding Source.

“Officers’ Certificate” means a certificate signed by two duly authorised officers of the Borrower.

“Opinion of Counsel” means a written opinion from legal counsel who is reasonably acceptable to the Lender (and to the party designated as trustee under the Agreed Funding Source Agreements). The counsel may be an employee of or counsel to the Borrower or the Lender (or the trustee under the Agreed Funding Source Agreements).

“Permitted Security Interest” means:

- (a) any Security Interest arising by operation of law which has not been foreclosed or otherwise enforced against the assets to which it applies; or
- (b) any Security Interest existing on any property at the time of its acquisition; or
- (c) any Security Interest upon any property to secure indebtedness incurred for the purpose of financing the acquisition of such property (or property which forms part of a class of assets of a similar nature where the Security Interest is by reference to the constituents or such class from time to time); or
- (d) any Security Interest securing or providing for the payment of indebtedness incurred in connection with any Project Financing provided that such Security Interest applies solely to (x) any property which is, or forms part of, the subject of such Project Financing or (y) revenues or claims which arise from the operation, failure to meet specifications, exploitation, sale or loss, or failure to complete or damage to, any such property; or
- (e) any renewal or extension of any Security Interest described in sub-paragraphs (b)-(e) above, provided that the principal amount of the indebtedness secured thereby is not increased.

“Person” means any individual, corporation, partnership, association, joint venture, joint-stock company, limited liability company, trust, unincorporated organisation or government or any Agency or political subdivision thereof.

“Proceedings” has the meaning set forth in Clause 25.4 (*Right of Lender to Take Proceedings Outside England*).

“Project Financing” means any arrangement for the provision of funds which are to be used solely to finance a project for the acquisition, construction, development or exploitation of any property pursuant to which the Persons providing such funds agree that the principal source of repayment of such funds will be the project and the revenues (including insurance proceeds) generated by such project.

“Put Option” has the meaning set forth in the Conditions.

“Put Option Aggregate Payment Notice” has the meaning set forth in the Conditions.

“Put Settlement Date” has the meaning set forth in the Conditions.

“Qualifying Jurisdiction” means any jurisdiction which has a double taxation treaty with Ukraine under which the payment of interest by Ukrainian borrowers to lenders in the jurisdiction in which a lender is incorporated is generally able to be made (upon completion of any necessary formalities required in relation thereto) without deduction or withholding of Ukrainian income tax or subject to deduction or withholding of such tax at a rate not exceeding 2 per cent.

“Relevant Entity” means, with the exception of the Borrower itself, any executive, governing, administrative or other body, department, committee, commission, division, unit or entity of any kind of, operating under the authority of, or representing the Borrower or the territorial community of the City of Kyiv (including, without limitation, the Kyiv City State Administration, its Main Financial Department, and any of its other departments and units), but not including (i) any municipal (communal) or other enterprise in which the Borrower has any direct or indirect ownership interest and (ii) any enterprise or entity for whose obligations the Borrower is not liable under applicable Ukrainian legislation.

“Relevant Event” has the meaning set forth in the Trust Deed.

“Repayment Date” means 15 July 2011 or, if such day is not a Business Day, the next succeeding Business Day.

“Rules” has the meaning set forth in Clause 25.9 (*Arbitration*).

“Securities Act” means the U.S. Securities Act of 1933.

“Security Interest” means any mortgage, charge, pledge, lien or other security interest (but excluding any lien arising by operation of law).

“Taxes” has the meaning set out in Clause 8.1 (*Additional Amounts*).

“Tax Indemnity Amounts” has the meaning set out in Clause 8.3 (*Tax Indemnity*).

“Taxing Authority” has the meaning set out in Clause 8.1 (*Additional Amounts*).

“Trust Deed” means the trust deed to be dated on or about 22 July 2004 between the Lender and Deutsche Trustee Company Limited, as trustee.

“Ukraine” shall mean Ukraine and any province or political sub-division or Agency thereof or therein.

“unpaid sum” has the meaning set forth in Clause 16.1 (*Default Interest Periods*).

Other Definitions

- (a) the “Lender” shall be construed so as to include its and any subsequent successors, assignees and chargees in accordance with their respective interests;
- (b) the “equivalent” on any given date in one currency (the “first currency”) of an amount denominated in another currency (the “second currency”) is a reference to the amount of the first currency which could be purchased with the amount of the second currency at the spot rate of exchange quoted on the relevant Reuters page or, where the first currency is (i) hryvnia and the second currency is (ii) U.S. dollars or as the case may be euros (or vice versa), as quoted by the National Bank of Ukraine at or about noon (London time or Brussels time (as applicable) or, as the case may be, Kyiv time) on such date for the purchase of the first currency with the second currency;
- (c) “repay” (or any derivative form thereof) shall, subject to any contrary indication, be construed to include “prepay” (or, as the case may be, the corresponding derivative form thereof); and
- (d) “VAT” shall be construed as a reference to (a) any tax imposed in compliance with the Sixth Directive of the Council of the European Economic Communities (77/388/EEC) (including in relation to the United Kingdom, value added tax imposed by the Value Added Tax Act 1994 and any legislation supplemental thereto); and (b) any other tax of a similar fiscal nature whether imposed in a member state of the European Union in substitution for or in addition to such tax, or imposed elsewhere.

1.2 Interpretation

Unless the context otherwise requires,

1.2.1 a term has the meaning assigned to it;

- 1.2.2 “or” is not exclusive;
- 1.2.3 words in the singular include the plural, and in the plural include the singular;
- 1.2.4 provisions apply to successive events and transactions;
- 1.2.5 references to “\$” or “U.S. dollars” are to United States dollars and references to “hryvnia” are to Ukrainian hryvnia.

Any references to the rights of the Lender in this Agreement shall be read as references to rights of the Trustee pursuant to the charge and assignment referred to in Clause 21.3 (*Assignments by the Lender*) except as in relation to the Reserved Rights as specified in Clause 4 of the Trust Deed.

1.3 Statutes

Any reference in this Agreement to a statute shall be construed as a reference to such statute as the same may have been, or may from time to time be, amended or re-enacted.

1.4 Headings

Clause and Schedule headings are for ease of reference only.

1.5 Amended Documents

Except where the contrary is indicated, any reference in this Agreement to this Agreement or any other agreement or document shall be construed as a reference to this Agreement or, as the case may be, such other agreement or document as the same may have been, or may from time to time be, amended, varied, novated or supplemented.

1.6 Agreed Form

Any reference herein to a document being in “agreed form” means that the document in question has been agreed between the proposed parties thereto, subject to any amendments that the parties may agree upon prior to the Drawdown Date.

1.7 The Kyiv City Council

The Kyiv City Council is a body of local self-governance representing the territorial community of the City of Kyiv and acting in the interests thereof under applicable Ukrainian legislation.

2. THE LOAN

The Lender grants to the Borrower, upon the terms and subject to the conditions hereof, a single disbursement term loan facility in the amount of \$200,000,000 (the “Loan”), funded by the Agreed Funding Source.

3. AVAILABILITY OF THE LOAN

The Loan will be available by way of a single advance that will be made by the Lender to the Disbursement Account, and the Borrower will draw down the Loan, on 22 July 2004 (the “Drawdown Date”), or such later date as may otherwise be agreed by the parties to this Agreement, if:

- 3.1.1 Deutsche Bank Securities Inc. and Morgan Stanley & Co. International Limited, as joint lead managers, have received the condition precedent documents as listed in the Agreed Funding Source Agreements in form and substance satisfactory to them (the “Conditions Precedent”);
- 3.1.2 the Lender has received full funding of the Loan from the Agreed Funding Source; and
- 3.1.3 no event has occurred or circumstance arisen which would, whether or not with the giving of notice and/or the passage of time and/or the fulfilment of any other requirement, constitute an event described under Clause 15 (*Events of Default*) and the representations set out in Clause 11 (*Representations and Warranties of the Borrower*) are true and accurate in all material respects on and as of the proposed date for the making of such Loan.

4. INTEREST PERIODS

Except as otherwise specified herein, the period for which the Loan is outstanding shall be divided into successive semi-annual periods, ending on and excluding 15 January and 15 July, each of which, other than the first (which shall commence on, and shall include, 22 July 2004 and shall end on, but

shall exclude, 15 January 2005), shall start on, and shall include, the last day of the preceding such period (each, an “Interest Period”).

5. PAYMENT AND CALCULATION OF INTEREST

5.1 Payment of Interest

Not later than 10.00 a.m. (New York City time) one Business Day prior to each Interest Payment Date the Borrower shall pay to the Collection Account all accrued and unpaid interest calculated to the last day of each Interest Period on the outstanding principal amount of the Loan.

5.2 Calculation of Interest

The Loan shall bear interest at the rate of 8.625 per cent. per annum (the “Interest Rate”). The amount of interest payable on each Interest Payment Date other than the first Interest Payment Date shall be calculated by applying the Interest Rate to the amount of the Loan, dividing the product by two, and rounding the resulting figure to the nearest cent, half a cent being rounded upwards. The amount of interest payable on the first Interest Payment Date shall be \$8,289,583.33. When interest is required to be calculated for any period other than an Interest Period, it shall be calculated on the basis of a year of 360 days consisting of 12 months of 30 days each, and, in the case of an incomplete month, the actual number of days elapsed.

6. REPAYMENT

Subject to Clause 15.8 (*Rights of Lender upon Occurrence of an Event of Default*), not later than 10.00 a.m. (New York City time) one Business Day prior to the Repayment Date, the Borrower shall repay in full the Loan and, to the extent not already paid in accordance with Clause 5.1 (*Payment of Interest*), all accrued and unpaid interest, any Additional Amounts and any Tax Indemnity Amounts calculated to the last day of the last Interest Period.

7. PREPAYMENT

7.1 Prepayment for Tax Reasons

If, as a result of the application of or any amendment to or change (including a change in interpretation or application) in the double taxation treaty between Ukraine and Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes) or the laws or regulations of Ukraine or Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes) or of any political subdivision thereof or any Agency therein, the Borrower would thereby be required to pay any Additional Amounts in respect of Taxes pursuant to Clause 8.1 (*Additional Amounts*) (other than Additional Amounts payable in respect of applicable Ukrainian withholding tax at a rate of up to 2 per cent.) or Tax Indemnity Amounts pursuant to Clause 8.3 (*Tax Indemnity*), then, provided that the Borrower cannot avoid the obligation to pay such Additional Amounts or Tax Indemnity Amounts by taking reasonable measures, the Borrower may (without premium or penalty), upon not less than 30 calendar days’ written notice to the Lender (and to the party designated as trustee under the Agreed Funding Source Agreements), including or attaching an Officers’ Certificate to the effect that the Borrower would be required to pay such Additional Amounts or Tax Indemnity Amounts prepay the Loan in whole (but not in part) at any time together with all accrued and unpaid interest, any Additional Amounts and any Tax Indemnity Amounts. No such notice shall be given earlier than 90 calendar days prior to the earliest date on which the Borrower would be obligated to pay such Additional Amounts or Tax Indemnity Amounts, as the case may be.

Without prejudice to any other requirement in this Agreement, any notice of prepayment given by the Borrower pursuant to this Clause 7.1 (*Prepayment for Tax Reasons*) hereof shall be irrevocable, shall specify the date upon which such prepayment is to be made and shall oblige the Borrower to make such prepayment one Business Day prior to such date.

7.2 Prepayment in the event of the exercise of any Put Option

In the event that any Put Option is exercised in accordance with the Conditions and subject to receipt of the Put Option Aggregate Payment Notice, the Borrower shall be required to prepay the Loan together with all accrued and unpaid interest and any Additional Amounts and any Tax Indemnity Amounts outstanding hereunder on the Business Day prior to the Put

Settlement Date to the extent and in the amount that the Lender is required to pay the holders of Notes as a result thereof, as set forth in the Put Option Aggregate Payment Notice delivered at least ninety (90) days prior to the Put Settlement Date.

7.3 Costs of Prepayment

The Borrower shall, on the date of prepayment, pay all accrued and unpaid interest, any Additional Amounts and any Tax Indemnity Amounts (each only with respect to the amount subject to such prepayment), as of such date of prepayment and all other amounts payable to the Lender hereunder in connection with such prepayment. The Borrower shall indemnify the Lender on demand against any administrative and legal costs and expenses reasonably incurred and properly documented by the Lender on account of any prepayment made in accordance with this Clause 7 (*Prepayment*).

7.4 No Other Prepayments

The Borrower shall not prepay the whole or any part of the amount of the Loan except at the times and in the manner expressly provided for in this Agreement.

7.5 Purchase of Instruments Issued to the Agreed Funding Source

The Borrower may purchase instruments issued to the Agreed Funding Source at any time in the open market or otherwise. If such instruments are surrendered by the Borrower to the Lender, as issuer of such instruments, for cancellation (together with an authorisation addressed to the registrar under the Agreed Funding Source Agreements to cancel such instruments), the principal amount of the Loan corresponding to the principal amount of such cancelled instruments shall be deemed repaid (by surrender of such instruments) and extinguished for all purposes as of the date of such cancellation, together with accrued interest and other amounts (if any) payable thereon and no further payment shall be made or required to be made by the Borrower in respect of such amount.

8. TAXES

8.1 Additional Amounts

8.1.1 All payments made by the Borrower in respect of the Loan shall be made free and clear of and without deduction or withholding for or on account of any present or future taxes, duties, assessments, fees or other governmental charges (collectively, "Taxes") imposed or levied by or on behalf of Ukraine or Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes) or any political subdivision or taxing authority thereof or therein in each of the preceding jurisdictions (each, a "Taxing Authority"), unless the Borrower is required to withhold or deduct Taxes by law or by the interpretation or administration thereof. For the avoidance of doubt, this Clause 8.1 shall not apply to any Taxes on income payable by the Lender in Germany (or any Qualifying Jurisdiction).

8.1.2 If at any time the Borrower is required to withhold or deduct any amount for or on account of Taxes imposed or levied by or on behalf of any Taxing Authority within Ukraine or Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes) from any payment made under or with respect to the Loan, the Borrower shall, on the due date for such payment, pay such additional amounts ("Additional Amounts") as may be necessary so that the net amount received by the Lender (including Additional Amounts) in U.S. dollars after such withholding or deduction will not be less than the amount the Lender would have received if such Taxes had not been withheld or deducted and free from liability in respect of such withholding or deduction; provided, however, that (i) for the avoidance of doubt, such Additional Amounts shall not be payable with respect to any Taxes on income payable by the Lender in Germany (or any Qualifying Jurisdiction) and (ii) such Additional Amounts (other than Additional Amounts payable in respect of applicable Ukrainian withholding tax at a rate of up to 2 per cent.) shall not be payable if and to the extent that such withholding or deduction is required following and on account of a Relevant Event.

8.1.3 The Borrower will also:

- (a) make such withholding or deduction; and

(b) remit the full amount deducted or withheld to the relevant authority in accordance with applicable law.

8.1.4 At least 30 calendar days prior to each date on which any payment under or with respect to the Loan is due and payable, if the Borrower will be obligated to pay Additional Amounts (other than Additional Amounts payable in respect of applicable Ukrainian withholding tax at a rate of up to 2 per cent.) with respect to such payment (upon and subject to written notice by the Lender or by the party designated as trustee under the Agreed Funding Source Agreements), the Borrower will deliver to the Lender (and to the party designated as trustee under the Agreed Funding Source Agreements) an Officers' Certificate stating the fact that such Additional Amounts will be payable and the amounts so payable.

8.1.5 If the Lender pays any amount in respect of such Taxes, the Borrower shall reimburse the Lender in U.S. dollars for such payment on demand.

8.1.6 Whenever this Agreement mentions, in any context, the payment of amounts based upon the principal or premium, if any, interest or of any other amount payable under or with respect to the Loan, this includes, without duplication, payment of any Additional Amounts and Tax Indemnity Amounts that may be applicable.

The foregoing provisions shall apply, modified as necessary, to any Taxes imposed or levied by any Taxing Authority in any jurisdiction in which any successor obligor to the Borrower is organized.

8.2 Payments

The Borrower shall use all reasonable efforts to assist the Lender in ensuring that all payments made under this Agreement are exempt from deduction or withholding of Tax.

8.3 Tax Indemnity

Without prejudice to, and without duplication of, the provisions of Clause 8.1 (*Additional Amounts*), (a) if at any time the Lender makes or is required to make any payment to a Person (other than to or for the account of the Agreed Funding Source) on account of Tax (other than Taxes on income payable by the Lender in Germany or any Qualifying Jurisdiction) in respect of the Loan or in respect of the Agreed Funding Source Agreements imposed by any Taxing Authority of or in Ukraine, Germany or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes, or any liability in respect of any such payment is asserted, imposed, levied or assessed against the Lender, the Borrower shall, as soon as reasonably practicable following, and in any event within 30 calendar days of, written demand made by the Lender, indemnify the Lender against such payment or liability, together with any interest, penalties, costs and expenses payable or incurred in connection therewith; and (b) if at any time a Taxing Authority imposes an obligation on the Lender to withhold or deduct any amount on any payment made or to be made by the Lender to or for the account of the Agreed Funding Source and the Lender is required by any Agreed Funding Source Agreements to pay additional amounts to such Agreed Funding Source in connection therewith, the Borrower shall, as soon as reasonably practicable following, and in any event within 30 calendar days of, written demand made by the Lender, pay to the Lender an amount equal to such additional amounts as would be necessary to have been paid to such Agreed Funding Source so that the net amount received by the Agreed Funding Source (including such additional amounts) in U.S. dollars after such withholding or deduction will not be less than the amount such Agreed Funding Source would have received if such withholdings or deductions had not been made and free from liability in respect of such withholding or deduction. Any payments required to be made by the Borrower under this Clause 8.3 are collectively referred to as "Tax Indemnity Amounts". For the avoidance of doubt, the provisions of this Clause 8.3 shall not apply to any withholding or deductions of Taxes with respect to the Loan which are subject to payment of Additional Amounts under Clause 8.1 (*Additional Amounts*).

8.4 Tax Claims

If the Lender intends to make a claim for any Tax Indemnity Amounts pursuant to Clause 8.3 (*Tax Indemnity*), it shall notify the Borrower thereof; provided that nothing herein shall require the Lender to disclose any confidential information relating to the organisation of its affairs.

8.5 Tax Credits and Tax Refunds

8.5.1 If any Additional Amounts are paid under Clause 8.1 (*Additional Amounts*) or Tax Indemnity Amounts are paid under Clause 8.3 (*Tax Indemnity*) by the Borrower for the benefit of the Lender and the Lender, in its reasonable opinion, determines that it has received or been granted a credit against, a relief or remission for, or a repayment of, any Tax, then, if and to the extent that the Lender, in its opinion, determines that such credit, relief, remission or repayment is in respect of or calculated with reference to the deduction or withholding giving rise to such Additional Amounts or, in the case of Tax Indemnity Amounts, with reference to the liability, expense or loss to which the payment giving rise to such Tax Indemnity Amounts relates, the Lender shall, to the extent that it can do so without prejudice to the retention of the amount of such credit, relief, remission or repayment, pay to the Borrower such amount as the Lender shall, in its opinion, have concluded to be attributable to such deduction or withholding or, as the case may be, such liability, expense or loss; provided that the Lender shall not be obliged to make any payment under this Clause 8.5 in respect of such credit, relief, remission or repayment until the Lender is in its opinion satisfied that its tax affairs for its tax year in respect of which such credit, relief, remission or repayment was obtained have been finally settled. Any such payment shall, in the absence of manifest error and subject to the Lender specifying in writing in reasonable detail the calculation of such credit, relief, remission or repayment and of such payment and providing relevant supporting documents evidencing such matters, be conclusive evidence of the amount due to the Borrower hereunder and shall be accepted by the Borrower in full and final settlement of its rights of reimbursement hereunder in respect of such deduction or withholding. Nothing contained in this Clause 8.5 shall interfere with the right of the Lender to arrange its tax affairs generally in whatever manner it thinks fit nor oblige the Lender to disclose any information relating to its tax affairs generally or any computations in respect thereof.

8.5.2 If as a result of a failure to obtain relief from deduction or withholding of any Tax imposed by Ukraine or Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes) (i) such Tax is deducted or withheld by the Borrower and pursuant to Clause 8.1 (*Additional Amounts*) an increased amount is paid by the Borrower to the Lender in respect of such deduction or withholding, and (ii) following the deduction or withholding of Tax as referred to above, (A) the Borrower applies on behalf of the Lender to the relevant Ukrainian Taxing Authorities for a tax refund and such tax refund is credited by the Ukrainian Taxing Authorities to the Lender or (B) if such tax refund is otherwise credited by a relevant Taxing Authority to the Lender, pursuant to a final decision of such Taxing Authority, the Lender shall as soon as reasonably possible notify the Borrower of the receipt of such tax refund and promptly transfer the entire amount of the tax refund to a bank account of the Borrower specified for that purpose by the Borrower.

8.6 Representations of the Lender

The Lender represents that (a) it is a bank which at the date hereof is a resident of Germany, is subject to taxation in Germany on the basis of its registration as a legal entity, location of its management body or another similar criterion and it is not subject to taxation in Germany merely on income from sources in Germany or connected with property located in Germany; (b) it will account for the Loan on the date of closing on its balance sheet as an asset under “loans and advances to customers” and any arrangements in connection with the Agreed Funding Source as a liability under “certificated liabilities” and (c) at the date hereof, it does not have a permanent establishment in Ukraine for purposes of applicable Ukrainian tax legislation. The Lender shall make reasonable and timely efforts to assist the Borrower to obtain relief from withholding of Ukrainian income tax pursuant to the double taxation treaty between Ukraine and the jurisdiction in which the Lender is incorporated, including its obligations under Clause 8.8 (*Delivery of Forms*). The Lender makes no representation as to the application or interpretation of any double taxation treaty between Ukraine and the jurisdiction in which the Lender is incorporated.

8.7 **Exceptions**

The Lender agrees promptly, upon becoming aware of such, to notify the Borrower if it ceases to be resident in Germany or a Qualifying Jurisdiction or if any of the representations set forth in Clause 8.6 (*Representations of the Lender*) are no longer true and correct. If the Lender ceases to be resident in Germany or a Qualifying Jurisdiction, then, except in circumstances where the Lender has ceased to be resident in Germany or a Qualifying Jurisdiction by reason of any Change of Law (including a change in a double taxation treaty or in such law or treaty's application or interpretation), in each case taking effect after the date of this Agreement, the Borrower shall not be liable to pay to the Lender under Clause 8.1 (*Additional Amounts*) or Clause 8.3 (Tax Indemnity) any sum in excess of the sum it would have been obliged to pay if the Lender had not ceased to be resident in Germany or a Qualifying Jurisdiction.

8.8 **Delivery of Forms**

The Lender shall within 30 calendar days of the request of the Borrower, to the extent it is able to do so under applicable law including Ukrainian laws, deliver to the Borrower a certificate issued by the competent state authority in Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes) confirming that the Lender is a tax resident in Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes) and such other information or forms as may need to be duly completed and delivered by the Lender to enable the Borrower to apply to obtain relief from deduction or withholding of Ukrainian Tax after the date of this Agreement, including under the double taxation treaty, or, as the case may be, to apply to obtain a tax refund if a relief from deduction or withholding of Ukrainian Tax has not been obtained. The Lender shall, within 30 calendar days of the request of the Borrower, to the extent it is able to do so under applicable law including Ukrainian laws, from time to time deliver to the Borrower any additional duly completed application forms as need to be duly completed and delivered by the Lender to enable the Borrower to apply to obtain relief from deduction or withholding of Ukrainian Tax or, as the case may be, to apply to obtain a tax refund if a relief from deduction or withholding of Ukrainian Tax has not been obtained. The certificate and, if required, other forms referred to in this Clause 8.8 shall be duly signed by the Lender, if applicable, and stamped or otherwise approved by the competent state authority in Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes) and apostilled or otherwise legalised. If a relief from deduction or withholding of Ukrainian Tax under this Clause 8.8 has not been obtained and further to an application of the Borrower to the relevant Ukrainian Taxing Authorities the latter makes a tax refund to the Borrower, then, if and to the extent that the Borrower has failed to make payment of Additional Amounts in relation to the payments under this Agreement from which no such relief as aforesaid was obtained, the Borrower shall promptly transfer to the Lender an amount in U.S. dollars equivalent to such refund. The Borrower shall pay all costs (including, but not limited to, currency conversion costs) associated with such transfer.

9. **TAX RECEIPTS**

9.1 **Notification of Requirement to Deduct Tax**

If, at any time, the Borrower is required by law to make any deduction or withholding from any sum payable by it hereunder, or if thereafter there is any change in the rates at which or the manner in which such deductions or withholdings are calculated, the Borrower shall promptly notify the Lender.

9.2 **Evidence of Payment of Tax**

9.2.1 The Borrower will make all reasonable endeavours to obtain certified copies, and translations into English, of tax receipts evidencing the payment of any Taxes so deducted or withheld from each Taxing Authority imposing such Taxes. The Borrower will furnish to the Lender (and to the party designated as trustee under the Agreed Funding Source Agreements), within 60 calendar days after the date the payment of any Taxes so deducted or withheld is due pursuant to applicable law, either certified copies of tax receipts evidencing such payment by the Borrower or, if such receipts are not obtainable, other evidence of such payments by the Borrower.

9.2.2 The Lender will make all reasonable endeavours to obtain certified copies, and translations into English, of tax receipts evidencing the payment of any Taxes so deducted or withheld from each Taxing Authority imposing such Taxes. The Lender will furnish to the Borrower, within 60 calendar days after the date the payment of any Taxes so deducted or withheld is due pursuant to applicable law, either certified copies of tax receipts evidencing such payment by the Lender or, if such receipts are not obtainable, other evidence of such payments by the Lender.

10. CHANGES IN CIRCUMSTANCES

10.1 Increased Costs

If, by reason of (i) any Change of Law, other than a Change of Law which relates only to the basis or rate of Tax on the net income of the Lender, and/or (ii) compliance with any Capital Adequacy Requirement, reserve or deposit requirement or any other request from or requirement of any central bank or other fiscal, monetary or other authority which has effect in Germany (or any Qualifying Jurisdiction in which the Lender or any successor thereto is resident for tax purposes):

10.1.1 the Lender incurs an additional cost as a result of the Lender's entering into or performing its obligations, including its obligation to make the Loan, under this Agreement (excluding Taxes payable by the Lender on its overall net income); or

10.1.2 the Lender becomes liable to make any additional payment on account of Tax or otherwise, not being a Tax imposed on its net income, on or calculated by reference to the amount of the Loan and/or to any sum received or receivable by it hereunder except where compensated under Clause 8.1 (*Additional Amounts*) or under Clause 8.3 (*Tax Indemnity*);

then the Borrower shall, from time to time within 30 calendar days of written demand of the Lender, pay to the Lender amounts sufficient to hold harmless and indemnify it from and against, as the case may be, such properly documented cost or liability; provided that the Lender will not be entitled to indemnification where such increased cost or liability arises as a result of the gross negligence, fraud or wilful default of the Lender; and provided that the amount of such increased cost or liability shall be deemed not to exceed an amount equal to the proportion of any cost or liability which is directly attributable to this Agreement.

10.2 Increased Costs Claims

If the Lender intends to make a claim pursuant to Clause 10.1 (*Increased Costs*), it shall notify the Borrower thereof and provide a written description in reasonable detail of the relevant Change of Law or Capital Adequacy Requirement, as the case may be, including a description of the relevant affected jurisdiction or country and the date on which the change in circumstances took effect; provided that nothing herein shall require the Lender to disclose any confidential information relating to the organisation of its or any other Person's affairs. The written description shall demonstrate the connection between the change in circumstance and the increased costs and shall be accompanied by relevant supporting documentation evidencing the matters described therein.

10.3 Illegality

If, at any time after the date of this Agreement, it is unlawful for the Lender to make, fund or allow to remain outstanding the Loan made or to be made by it hereunder or to maintain the Agreed Funding Source then the Lender shall, after becoming aware of the same, deliver to the Borrower a written notice, setting out in reasonable detail the nature and extent of the relevant circumstances, to that effect and:

10.3.1 if the Loan has not then been made, the Lender shall not thereafter be obliged to make the Loan; and

10.3.2 if the Loan is then outstanding and the Lender so requests, the Borrower shall, on the latest date permitted by the relevant law or such earlier day as the Borrower elects (as notified to the Lender upon not less than 30 calendar days' written notice prior to the date of repayment), repay the Loan together with accrued and unpaid interest thereon and all other amounts owing to the Lender hereunder.

10.4 **Mitigation**

If circumstances arise which would result in:

10.4.1 any payment falling due to be made by or to the Lender or for its account pursuant to Clause 10.3 (*Illegality*);

10.4.2 any payment falling due to be made by the Borrower pursuant to Clause 8.1 (*Additional Amounts*); or

10.4.3 a claim for indemnification pursuant to Clause 8.3 (*Tax Indemnity*) or Clause 10.1 (*Increased Costs*),

then, without in any way limiting, reducing or otherwise qualifying the rights of the Lender or the Borrower's obligations under any of the above mentioned provisions, the Lender shall, upon becoming aware of the same, notify the Borrower thereof and, in consultation with the Borrower and to the extent it can lawfully do so and without prejudice to its own position, take reasonable steps to remove such circumstances or mitigate the effects of such circumstances including, without limitation, by the change of its lending office or transfer of its rights or obligations under this Agreement to another bank; provided that the Lender shall be under no obligation to take any such action if, in its opinion, to do so might have any adverse effect upon its business, operations or financial condition or might be in breach of any arrangements which it may have made in connection with the Agreed Funding Source.

11. **REPRESENTATIONS AND WARRANTIES OF THE BORROWER**

The Borrower makes the following representations and warranties and acknowledges that the Lender has entered into this Agreement in reliance on those representations and warranties.

11.1 **Status**

The Borrower is a body of local self-governance representing the territorial community of the City of Kyiv and acting in the interests thereof under applicable Ukrainian legislation.

11.2 **Due Authorisation**

The Borrower has duly authorised, executed and delivered this Agreement.

11.3 **Governmental Approvals**

All actions or things required to be taken, fulfilled or done by laws or regulations of Ukraine (including, without limitation, the obtaining of any consent, approval (including exchange control approval), authorisation, order, licence or qualification of or with any court or governmental agency), and all registrations, filings or notarisations required by laws or regulations of Ukraine (except for those referred to in Clause 14.1 (*Maintenance of Legal Validity*) below), in order to ensure (i) the due execution, delivery and performance by the Borrower of this Agreement, (ii) the compliance by the Borrower with all the provisions of this Agreement and (iii) the consummation of the transactions contemplated by this Agreement have been (or will, prior to the Drawdown Date, have been) obtained, fulfilled or done and are (or will, prior to the Drawdown Date, be) in full force and effect.

11.4 **Purpose of Agreement**

The Borrower has entered into this Agreement to finance the budgetary expenditure objectives of the City of Kyiv, including the realisation of projects in the areas of capital construction, transportation infrastructure (including the construction of the Podilsky bridge over the Dnipro River) and public utilities.

11.5 **Pari Passu Obligations**

The obligations of the Borrower under this Agreement will rank at least *pari passu* in right of payment with all other unsecured and unsubordinated obligations of the Borrower, except as otherwise provided by mandatory provisions of applicable law.

11.6 **Validity and Admissibility in Evidence**

All acts, conditions and things required to be done, fulfilled and performed (other than by the Lender) to make this Agreement admissible in evidence in Ukraine (whether in arbitration proceedings or otherwise) have been done, fulfilled and performed.

11.7 Valid and Binding Obligations

The obligations expressed to be assumed by the Borrower in this Agreement are legal, valid and binding, and enforceable against it in accordance with their terms, except that the enforcement thereof may be limited by bankruptcy, insolvency, fraudulent conveyance, reorganisation, moratorium and other similar laws relating to or affecting creditors' rights generally.

11.8 No Stamp Taxes

Under the laws of Ukraine in force at the date hereof, it is not necessary that any stamp, registration (other than a fee payable with respect to the registration of this Agreement with the National Bank of Ukraine) or similar Tax be paid on or in relation to this Agreement.

11.9 No Events of Default

No event has occurred or circumstance arisen which would (whether or not with the giving of notice and/or the passage of time and/or the fulfilment of any other requirement) constitute an event described under Clause 15 (*Events of Default*).

11.10 No Material Proceedings

There are no lawsuits, litigation or other legal or administrative or arbitration proceedings current or pending or, to the best of the knowledge and belief of the Borrower, threatened before any court, tribunal, arbitration panel or Agency which might (a) prohibit the execution and delivery of this Agreement or the Borrower's compliance with its obligations hereunder or (b) adversely affect the right and power of the Borrower to enter into this Agreement or (c) have a material adverse effect on the sources and amounts of revenue of the Borrower or in the proposed expenditure of the Borrower, each as set out in the Budget Accounts, which might affect the investment decision of the Agreed Funding Source.

11.11 Budget Accounts

The Budget Accounts of the Borrower have been prepared in accordance with the Budget Code of Ukraine, dated 21 June 2001 as amended, and other applicable Ukrainian legislation.

11.12 No Material Adverse Change

Since 31 December 2003 there has been no material adverse change or any development involving a prospective material adverse change of which the Borrower is or might reasonably be expected to be aware in the sources and amounts of revenue of the Borrower or in the proposed expenditure of the Borrower, each as set out in the Budget Accounts, which might affect the investment decision of the Agreed Funding Source.

11.13 Execution of Agreement

Its execution and delivery of this Agreement and its exercise of its rights and performance of its obligations hereunder do not and will not:

11.13.1 conflict with or result in a breach of any of the terms or provisions of, or constitute a default under, any material indenture, trust deed, mortgage or other material contract, agreement or instrument or treaty to which the Borrower is a party or by which it, or any of its properties or assets, is bound;

11.13.2 violate or conflict with any existing applicable law, rule, regulation, judgment, order, directive or decree of any government, governmental body or court in Ukraine binding upon the Borrower; or

11.13.3 give rise to any event of default or moratorium in respect of any of the obligations of the Borrower or the creation of any lien, encumbrance or other security interest (howsoever described) in respect of any of the assets of the Borrower.

11.14 Availability of Municipal (Communal) Property for Enforcement or Execution

To the extent permitted by applicable Ukrainian law, all and any property in the municipal (communal) ownership of the territorial community of the City of Kyiv is and will be available for enforcement or execution of any order or judgment made or given as a result of any Proceedings against the Borrower.

11.15 Repetition

Each of the representations and warranties contained in Clause 11 (*Representations and Warranties of the Borrower*) shall be deemed to be repeated by the Borrower on the date for the making of the Loan. Each of the representations and warranties contained in Clauses 11.9 (*No Events of Default*), 11.10 (*No Material Proceedings*) and 11.12 (*No Material Adverse Change*) shall be deemed to be repeated by the Borrower, by reference to the facts and circumstances then existing, on each Interest Payment Date, except that the words “or the passage of time” in Clause 11.9 (*No Events of Default*) shall be deemed deleted in relation to every such repetition.

12. REPRESENTATIONS AND WARRANTIES AND AGREEMENT OF THE LENDER

12.1 Representations and Warranties

In addition to the representations and warranties set forth in Clause 8.6 (*Representations of the Lender*), the Lender makes the representations and warranties set out in sub-clause 12.1.1 (*Status*) to sub-clause 12.1.4 (*No Conflicts*), inclusive, and acknowledges that the Borrower has entered into this Agreement in reliance on those representations and warranties.

12.1.1 Status

The Lender is duly incorporated under the laws of Germany and is resident for German taxation purposes in Germany and has full corporate power and authority to enter into this Agreement and any other agreements relating to the Agreed Funding Source, and to undertake and perform the obligations expressed to be assumed by it herein and therein.

12.1.2 Authorisation

Each of this Agreement and each of the Agreed Funding Source Agreements entered into by the Lender has been duly authorised, executed and delivered by the Lender, and is a legal, valid and binding obligation of the Lender, enforceable against the Lender in accordance with its terms, except that the enforcement thereof may be subject to bankruptcy, insolvency, fraudulent conveyance, reorganisation, moratorium and other similar laws relating to or affecting creditors' rights generally.

12.1.3 Consents and Approvals

All authorisations, consents and approvals required by the Lender for or in connection with the execution of this Agreement and any other agreements relating to the Agreed Funding Source and the performance by the Lender of the obligations expressed to be undertaken in such agreements have been obtained and are in full force and effect.

12.1.4 No Conflicts

The execution of this Agreement and any Agreed Funding Source Agreements to which the Lender is a party and the undertaking and performance by the Lender of the obligations expressed to be assumed by it herein and therein will not conflict with, or result in a breach of or default under, the laws of Germany.

12.2 Noteholder Meetings

The Lender shall, promptly upon request by the Borrower, convene a meeting of holders of Notes in accordance with the terms and conditions of the Notes and the provisions of the Trust Deed.

13. FINANCIAL INFORMATION

13.1 Delivery

The Borrower shall supply or procure to be supplied to the Lender, in sufficient copies as may reasonably be required by the Lender, all such information as the Luxembourg Stock Exchange (or any other or further stock exchange or stock exchanges or any other relevant authority or authorities on which the instruments issued to the Agreed Funding Source may, from time to time, be listed or admitted to trading) may require in connection with the listing or admittance to trading on such stock exchange or relevant authority of instruments issued to the Agreed Funding Source.

13.2 Budget Accounts

The Borrower shall ensure that:

13.2.1 each set of budget accounts delivered by it pursuant to Clause 13.1 (*Delivery*) is prepared in accordance with the Budget Code of Ukraine dated 21 June 2001, as amended, and other applicable Ukrainian legislation; and

13.2.2 it provides to the Lender within 10 days of any request by the Lender and at the time of the despatch to the Lender of its budget accounts pursuant to Clause 13.1 (*Delivery*), and in any event not later than 30 days after the dates on which the budget accounts relating to the next financial year and the resolution of the Kyiv City Council on the approval of reports and execution of the budget of the City of Kyiv for the relevant financial year are published, an Officers' Certificate certifying that up to a specific date not earlier than seven days prior to the date of such Officers' Certificate (the "Certified Date") the Borrower has complied with its obligations under this Agreement (or, if such is not the case, giving details of the circumstances under such non-compliance) and that as at such date there did not exist nor had there existed at any time prior thereto since the Certified Date in respect of the previous such certificate (or, in the case of the first such certificate, since the date of this Agreement) any Event of Default or (if such is not the case) specifying the same.

14. COVENANTS

14.1 Maintenance of Legal Validity

The Borrower shall obtain, comply with the terms of and do all that is necessary to maintain in full force and effect all authorisations, approvals, licences and consents required in or by the laws and regulations of Ukraine to enable it lawfully to enter into and perform its obligations under this Agreement and to ensure the legality, validity, enforceability or admissibility in evidence in Ukraine of this Agreement, including, but not limited to, the ratification (approval upon execution) of this Agreement by the decision of the Kyiv City Council and the registration of this Agreement with the National Bank of Ukraine.

14.2 Untrue Representations

Before the making of the Loan, the Borrower shall notify the Lender of the occurrence of any event which results in or may reasonably be expected to result in any of the representations contained in Clause 11 (*Representations and Warranties of the Borrower*) being untrue at or before the time of the making of such Loan.

14.3 Notification of Events of Default

The Borrower shall promptly on becoming aware thereof inform the Lender of the occurrence of any Event of Default and, upon receipt of a written request to that effect from the Lender, confirm to the Lender that, save as previously notified to the Lender or as notified in such confirmation, no Event of Default has occurred.

14.4 Claims *Pari Passu*

The Borrower shall ensure that at all times the claims of the Lender against it under this Agreement rank at least *pari passu* with the claims of all the other unsecured and unsubordinated creditors of the Borrower, except as otherwise provided by mandatory provisions of applicable law.

14.5 Negative Pledge

So long as the Loan or any part of it has not been repaid in full, the Borrower will not create or permit to subsist any Security Interest (other than a Permitted Security Interest) upon the whole of any part of the City Assets to secure any Indebtedness of the Borrower or any Relevant Entity or any guarantee or indemnity by the Borrower or any Relevant Entity of any Indebtedness unless, at the same time or prior thereto, the obligations under this Agreement (i) are secured equally and rateably therewith or (ii) have the benefit of such other security or other arrangement which is equivalent in all material respects to such Security Interest and which shall be approved by the Lender.

14.6 Stay, Extension and Usury Laws

The Borrower covenants (to the extent that it may lawfully do so) that it shall not at any time insist upon, plead, or in any manner whatsoever claim or take the benefit or advantage of, any stay, extension or usury law wherever enacted, now or at any time hereafter in force, which may affect the covenants or the performance of this Agreement; and the Borrower (to the

extent it may lawfully do so) hereby expressly waives all benefit or advantage of any such law, and covenants that it shall not, by resort to any such law, hinder, delay or impede the execution of any power herein granted to the Lender (or granted to the party designated as trustee under the Agreed Funding Source Agreements by such Agreed Funding Source Agreements), but shall suffer and permit the execution of every such power as though no such law had been enacted.

14.7 Use of Proceeds of the Loan

The Borrower shall use the proceeds of the Loan in the manner described in the “Use of Proceeds” section of the Offering Circular.

14.8 Put Option

Upon the exercise of any Put Option, the Borrower shall prepay the Loan, in whole or in part, pursuant to and subject to the conditions described in Clause 7.2 (*Prepayments in the event of the exercise of any Put Option*).

15. EVENTS OF DEFAULT

15.1 Circumstances which Constitute Events of Default

Each of Clause 15.2 (*Failure to Pay*) to Clause 15.7 (*Authorisations*), inclusive, constitutes an “Event of Default” with respect to the Loan.

15.2 Failure to Pay

The Borrower fails to pay any amount of principal, interest, Additional Amounts or Tax Indemnity Amounts under the Loan, in the currency and in the manner specified herein, when the same becomes due and payable, and such failure is not remedied within 7 Business Days of the due date for payment.

15.3 Obligations

The Borrower defaults in the performance or observance of any of its obligations other than that set out in Clause 15.2 (*Failure to Pay*) under or in respect of this Agreement and such default (if capable of being remedied) is not remedied within 35 days after the Lender has given written notice thereof to the Borrower requiring the same to be remedied (it being understood that a default in respect of the undertaking set forth in Clause 14.5 (*Negative Pledge*) shall be deemed capable of remedy for the purposes hereof).

15.4 Cross Default

Any Indebtedness of the Borrower or any Relevant Entity shall become due and payable prior to the stated maturity thereof other than at the option of the debtor following a default of the Borrower or any Relevant Entity, or the Borrower or any Relevant Entity shall fail to make the final payment of principal in respect of any Indebtedness of the Borrower or any Relevant Entity on the date on which such final payment is due and payable or at the expiration of any grace period originally applicable thereto or any guarantee or indemnity given by the Borrower or any Relevant Entity in respect of Indebtedness (the underlying obligation in respect of which such guarantee or indemnity has been given having become due and payable prior to the stated maturity thereof otherwise than at the option of the debtor following a default or the debtor having failed to make the final payment of principal in respect of such underlying obligation on the date on which such final payment is due and payable or at the expiration of any grace period originally applicable thereto) shall not be honoured when due and called upon; provided that the aggregate amount of the relevant Indebtedness in respect of which one or more of the events mentioned in this Clause 15.4 shall have occurred equals or exceeds \$10,000,000 (or its equivalent in any other currency or currencies); and provided, further, that any secured Indebtedness that by its terms is fully non-recourse to the Borrower or any Relevant Entity shall not be counted as Indebtedness for purposes of this Clause 15.4.

15.5 Moratorium

A moratorium is placed on the payment of principal of, or interest on, all or any part of any Indebtedness of the Borrower or any Relevant Entity.

15.6 **Validity and Illegality**

15.6.1 The validity of this Agreement is contested by the Borrower or any Agency of the Borrower or the Borrower or any Agency of the Borrower shall deny any of the Borrower's obligations under this Agreement; or

15.6.2 it is, or will become, unlawful for the Borrower to perform or comply with any of its obligations under this Agreement; or

15.6.3 any of such obligations shall become unenforceable or cease to be legal, valid and binding in a manner which has a material adverse effect on the rights or claims of the Lender under this Agreement.

15.7 **Authorisations**

Any regulation, decree, consent, approval, licence or other authority necessary to enable the Borrower to enter into or perform its obligations under this Agreement or for the validity or enforceability thereof shall expire or be withheld, revoked or terminated or otherwise cease to remain in full force and effect or shall be modified in a manner which has a material adverse effect upon the rights or claims of the Lender under this Agreement.

15.8 **Rights of Lender upon Occurrence of an Event of Default**

If an Event of Default occurs under this Agreement and is continuing, the Lender (if it receives instructions from the party designated as trustee of the Agreed Funding Source in accordance with the provisions of the Agreed Funding Source Agreements) and/or the party designated as trustee of the Agreed Funding Source in accordance with the terms of the Agreed Funding Source Agreements may, by written notice (an "Acceleration Notice") to the Borrower, (a) declare the obligations of the Lender hereunder to be terminated, whereupon such obligations shall terminate, and (b) declare the principal amount of, premium, if any, and accrued and unpaid interest, Additional Amounts and Tax Indemnity Amounts, if any, on the Loan to be immediately due and payable and the same shall become immediately due and payable, pursuant to and in accordance with the terms of the Agreed Funding Source Agreements.

15.9 **Other Remedies**

If an Event of Default occurs and is continuing, the Lender (and the party designated as trustee under the Agreed Funding Source Agreements) may pursue any available remedy to collect the payment of principal or interest on the Loan or to enforce the performance of any provision of this Agreement. A delay or omission by the Lender (or the party designated as trustee under the Agreed Funding Source Agreements) in exercising any right or remedy accruing upon an Event of Default shall not impair the right or remedy or constitute a waiver of or acquiescence in the Event of Default.

16. **DEFAULT INTEREST AND INDEMNITY**

16.1 **Default Interest Periods**

If any sum due and payable by the Borrower hereunder is not paid on the due date therefore in accordance with the provisions of Clause 19 (*Payments*) or if any sum due and payable by the Borrower under any judgment of any court in connection herewith is not paid on the date of such judgment, the period beginning on such due date or, as the case may be, the date of such judgment and ending on the date upon which the obligation of the Borrower to pay such sum (the balance thereof for the time being unpaid being herein referred to as an "unpaid sum") is discharged shall be divided into successive periods, each of which, other than the first, shall start on the last day of the preceding such period and the duration of each of which shall, except as otherwise provided in this Clause 16 (*Default Interest and Indemnity*), be selected by the Lender, but shall in any event not be longer than one month.

16.2 **Default Interest**

During each such period relating thereto as is mentioned in Clause 16.1 (*Default Interest Periods*) an unpaid sum shall bear interest at a rate per annum equal to the Interest Rate.

16.3 **Payment of Default Interest**

Any interest which shall have accrued under Clause 16.2 (*Default Interest*) in respect of an unpaid sum shall be due and payable and shall be paid by the Borrower at the end of the period by reference to which it is calculated or on such other dates as the Lender may specify by written notice to the Borrower.

16.4 Borrower's Indemnity

The Borrower undertakes to indemnify the Lender against any reasonably incurred and properly documented cost, claim, loss, expense (including legal fees) or liability, together with any VAT thereon, which it may sustain or incur as a consequence of the occurrence of any Event of Default or any default by the Borrower in the performance of any of the obligations expressed to be assumed by it in this Agreement.

16.5 Unpaid Sums as Advances

Any unpaid sum shall, for the purposes of this Clause 16 (*Default Interest and Indemnity*) and Clause 10.1 (*Increased Costs*), be treated as an advance and accordingly in this Clause 16 (*Default Interest and Indemnity*) and Clause 10.1 (*Increased Costs*) the term "Loan" includes any unpaid sum and the term "Interest Period", in relation to an unpaid sum, includes each such period relating thereto as is mentioned in Clause 16.1 (*Default Interest Periods*).

17. AMENDMENTS TO AGREED FUNDING SOURCE AGREEMENTS

Any amendment to, or waivers of any provision of, the Agreed Funding Source Agreements shall be prohibited without the prior express written consent of the Borrower, which consent shall not be unreasonably withheld (other than amendments or waivers that are made pursuant to any legal, regulatory or accounting requirements, with respect to which the Lender shall consult with the Borrower to the extent reasonably practicable).

18. CURRENCY OF COLLECTION ACCOUNT AND CURRENCY INDEMNITY

18.1 Currency of Collection Account

The U.S. dollar is the currency of account and payment for each and every sum at any time due from the Borrower hereunder.

18.2 Currency Indemnity

If any sum due from the Borrower under this Agreement or any order or judgment given or made in relation hereto has to be converted from the currency (the "first currency") in which the same is payable hereunder or under such order or judgment into another currency (the "second currency") for the purpose of (a) making or filing a claim or proof against the Borrower, (b) obtaining an order or judgment in any court or other tribunal or (c) enforcing any order or judgment given or made in relation hereto, the Borrower shall indemnify and hold harmless the Lender from and against any loss suffered or reasonably incurred as a result of any discrepancy between (i) the rate of exchange used for such purpose to convert the sum in question from the first currency into the second currency and (ii) the rate or rates of exchange at which the Lender may in the ordinary course of business purchase the first currency with the second currency upon receipt of a sum paid to it in satisfaction, in whole or in part, of any such order, judgment, claim or proof.

19. PAYMENTS

19.1 Payments to the Lender

On each date on which this Agreement requires an amount denominated in U.S. dollars to be paid by the Borrower, the Borrower shall make the same available to the Lender by payment in U.S. dollars and in same day funds on such date, or in such other funds as may for the time being be customary in London for the settlement in London of international banking transactions in U.S. dollars, to the Collection Account. The Borrower shall procure that the bank effecting payment on its behalf confirms to the Lender, or to such Person as the Lender may direct, by tested telex or authenticated SWIFT message one Business Day prior to the date that such payment is required to be made by this Agreement, the payment instructions relating to such payment.

19.2 Alternative Payment Arrangements

If, at any time, it shall become impracticable, by reason of any action of any governmental authority or any Change of Law, exchange control regulations or any similar event, for the Borrower to make any payments hereunder in the manner specified in Clause 19.1 (*Payments to the Lender*), then the Borrower may agree with the Lender alternative arrangements for such payments to be made; provided that, in the absence of any such agreement, the Borrower shall be obliged to make all payments due to the Lender in the manner specified herein.

19.3 **No Set-off**

All payments required to be made by the Borrower hereunder shall be calculated without reference to any set-off or counterclaim and shall be made free and clear of and without any deduction for or on account of any set-off or counterclaim.

20. **FEES, COSTS AND EXPENSES**

20.1 **Costs relating to Preservation of Rights**

The Borrower shall, from time to time on demand of the Lender, reimburse the Lender for all costs and expenses (including legal fees) together with any VAT incurred in or in connection with the preservation or the enforcement of any of the rights of the Lender under this Agreement.

20.2 **Taxes**

The Borrower shall pay all stamp, registration and other taxes to which this Agreement or any judgment given in connection with this Agreement is or at any time may be subject and shall, from time to time on demand of the Lender, indemnify the Lender against any liabilities, costs, claims and expenses resulting from any failure to pay or any delay in paying any such tax.

20.3 **Costs relating to Amendments and Waivers**

The Borrower shall, from time to time on demand of the Lender (and without prejudice to the provisions of Clause 20.1 (*Costs relating to Preservation of Rights*)) (and the party designated as trustee under the Agreed Fund Source Agreements) compensate the Lender (and, as the case may be, such trustee) at such daily and/or hourly rates as the Lender (or, as the case may be, such trustee) shall from time to time reasonably determine for all time expended by the Lender (or, as the case may be, such trustee), their respective directors, officers and employees, and for all costs and expenses (including telephone, fax, copying, travel and personnel costs) they may incur, in connection with the Lender (and, as the case may be, such trustee) taking such action as it may consider appropriate or in complying with any request by the Borrower in connection with:

20.3.1 the granting or proposed granting of any waiver or consent requested under this Agreement by the Borrower;

20.3.2 any actual or potential breach by the Borrower of any of its obligations under this Agreement;

20.3.3 the occurrence of any event which is an Event of Default or a Default; or

20.3.4 any amendment or proposed amendment to this Agreement requested by the Borrower.

21. **ASSIGNMENTS AND TRANSFERS**

21.1 **Binding Agreement**

This Agreement shall be binding upon and inure to the benefit of each party hereto and its or any subsequent successors and assigns.

21.2 **No Assignments and Transfers by the Borrower**

The Borrower shall not be entitled to assign or transfer all or any of its rights, benefits and obligations hereunder.

21.3 **Assignments by the Lender**

The Lender may not assign or transfer, in whole or in part, any of its rights and benefits or obligations under this Agreement except (i) the charge by way of first fixed charge granted by the Lender in favour of the Trustee of the Lender's rights and benefits under this Agreement and (ii) the absolute assignment by way of security by the Lender to the Trustee of certain rights, interest and benefits under this Agreement, in each case, pursuant to Clause 4 of the Trust Deed.

22. **CALCULATIONS AND EVIDENCE OF DEBT**

22.1 **Basis of Accrual of Interest**

Interest shall accrue from day to day and shall be calculated on the basis of a year of 360 days consisting of 12 months of 30 days each and, in the case of an incomplete month, the actual number of days elapsed.

22.2 Evidence of Debt

The Lender shall maintain, in accordance with its usual practice, accounts evidencing the amounts from time to time lent by and owing to it hereunder; in any legal action or proceeding arising out of or in connection with this Agreement, in the absence of manifest error and subject to the provision by the Lender to the Borrower of written information describing in reasonable detail the calculation or computation of such amounts together with the relevant supporting documents evidencing the matters described therein, the entries made in such accounts shall be conclusive evidence of the existence and amounts of the obligations of the Borrower therein recorded.

22.3 Change of Circumstance Certificates

A certificate signed by two authorised signatories of the Lender describing in reasonable detail (a) the amount by which a sum payable to it hereunder is to be increased under Clause 8.1 (*Additional Amounts*) or (b) the amount for the time being required to indemnify it against any such cost, payment or liability as is mentioned in Clause 8.3 (*Tax Indemnity*) or Clause 10.1 (*Increased Costs*) shall, in the absence of manifest error, be *prima facie* evidence of the existence and amounts of the specified obligations of the Borrower.

23. REMEDIES AND WAIVERS, PARTIAL INVALIDITY

23.1 Remedies and Waivers

No failure by the Lender to exercise, nor any delay by the Lender in exercising, any right or remedy hereunder shall operate as a waiver thereof, nor shall any single or partial exercise of any right or remedy prevent any further or other exercise thereof or the exercise of any other right or remedy. The rights and remedies herein provided are cumulative and not exclusive of any rights or remedies provided by law.

23.2 Partial Invalidity

If, at any time, any provision hereof is or becomes illegal, invalid or unenforceable in any respect under the law of any jurisdiction, neither the legality, validity or enforceability of the remaining provisions hereof nor the legality, validity or enforceability of such provision under the law of any other jurisdiction shall in any way be affected or impaired thereby.

24. NOTICES

24.1 Communications in Writing

Each communication and document to be made or delivered hereunder shall be made in writing and, unless otherwise stated, shall be made by fax, hand, or courier addressed as follows:

if to the Borrower:

The Kyiv City Council
36 Khreshchatyk Street
01044 Kyiv
Ukraine

Fax number: +380 44 254 1665

Attention: Viktor Mykhailovych Padalka

if to the Lender:

Bayerische Hypo- und Vereinsbank AG
Arabellastrasse 12
D-81925 Munich

Fax: +49 (89) 37815964

Attention: Framework & Documentation Services (MOO6CM)

24.2 Delivery

Each communication and document to be made or delivered by one party to another pursuant to this Agreement shall, unless that other party has by 15 calendar days' written notice to the same specified another address, be made or delivered to that other party at the address or fax number specified in Clause 24.1 (*Communications in Writing*) and shall be effective upon receipt by the addressee on a business day in the city of the recipient; provided, however that (i) any such communication or document which would otherwise take effect after 4:00 p.m. on any

particular day shall not take effect until 10:00 a.m. on the immediately succeeding business day in the city of the addressee and (ii) any communication or document to be made or delivered by one party to the other party shall be effective only when received by such other party and then only if the same is expressly marked for the attention of the department or officer identified with the such other party's signature below, or such other department or officer as such other party shall from time to time specify for this purpose.

25. LAW, JURISDICTION AND ARBITRATION

25.1 English Law

This Agreement and all matters arising from or connected with it are governed by, and shall be construed in accordance with, English law.

25.2 English Courts

The courts of England shall have exclusive jurisdiction to settle any dispute (a "Dispute") arising from or connected with this Agreement (including a Dispute regarding the existence, validity or termination of this Agreement or the consequences of its nullity).

25.3 Appropriate Forum

The parties agree that the courts of England are the most appropriate and convenient courts to settle Disputes between them and, accordingly, that they will not argue to the contrary.

25.4 Right of Lender to Take Proceedings Outside England

Clause 25.2 (*English Courts*) is for the benefit of the Lender only. As a result, nothing in this Clause 25 prevents the Lender from taking proceedings relating to a Dispute ("Proceedings") in any other courts with jurisdiction. To the extent allowed by law, the Lender may take concurrent Proceedings in any number of jurisdictions.

25.5 Service of Process (Borrower)

The Borrower agrees that the documents which start any Proceedings and any other documents required to be served in relation to those Proceedings may be served on it by being delivered to Law Debenture Corporate Services Limited at its registered office (being, at the date hereof, Fifth Floor, 100 Wood Street, London EC2V 7EX, United Kingdom). If such person is not or ceases to be effectively appointed to accept service of process on behalf of the Borrower, the Borrower shall, on the written demand of the Lender addressed to the Borrower and delivered to the Borrower appoint a further person in England to accept service of process on its behalf and, failing such appointment within 15 days, the Lender shall be entitled to appoint such a person by written notice addressed to the Borrower and delivered to the Borrower. Nothing in this paragraphs shall affect the right of the Lender to serve process in any other manner permitted by law. This clause applies to Proceedings in England and to Proceedings elsewhere.

25.6 Service of Process (Lender)

The Lender agrees that the documents which start any Proceedings and any other documents required to be served in relation to those Proceedings may be served on it by being delivered to Bayerische Hypo- und Vereinsbank AG, London Branch at 41 Moorgate, London EC2R 6PP or at any address of the Lender in Great Britain at which service of process may be served on it in accordance with Part XXIII of the Companies Act 1985. Nothing in this paragraph shall affect the right of the Borrower to serve process in any other manner permitted by law. This clause applies to Proceedings in England and to Proceedings elsewhere.

25.7 Consent to Enforcement, etc.

Each of the Lender and the Borrower consents generally in respect of any Proceedings to the giving of any relief or the issue of any process in connection with such Proceedings including, without limitation, the making, enforcement or execution of any order or judgement which is made or given in such Proceedings against any property whatsoever, including, to the extent not expressly prohibited by applicable Ukrainian law, any property in the municipal (communal) ownership of the territorial community of the City of Kyiv, irrespective of its use or intended use.

25.8 Waiver of Immunity

The Borrower waives generally all immunity it or its assets or revenues may otherwise have in any jurisdiction, including immunity in respect of:

25.8.1 the giving of any relief by way of injunction or order for specific performance or for the recovery of assets or revenues; and

25.8.2 the issue of any process against its assets or revenues for the enforcement of a judgment or, in an action in rem, for the arrest, detention or sale of any of its assets and revenues.

25.9 Arbitration

If any Dispute arises from or in connection with this Agreement, or any supplement, modifications or additions thereto, the Lender may elect, by notice to the Borrower, to settle such claim by arbitration in accordance with the following provisions. The Borrower hereby agrees that (regardless of the nature of the Dispute) any Dispute may be settled by arbitration in accordance with the Rules of Arbitration of the International Chamber of Commerce (the "Rules") as at present in force by a panel of three arbitrators appointed in accordance with the Rules. The seat of arbitration shall be London, England. The procedural law of arbitration shall be English law. The language of any arbitral proceedings shall be English.

26. RIGHTS OF THIRD PARTIES

A Person who is not a party to this Agreement has no rights under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Agreement.

27. ENGLISH LANGUAGE

27.1 Each communication and document to be made or delivered by one party to another pursuant to this Agreement shall be in the English language or accompanied by a translation into English certified (by an officer of the person delivering the same) as being a true and accurate translation. In the event of any discrepancies between the English and any Ukrainian versions of such communication or document, or any dispute regarding the interpretation of any provision in the English or any Ukrainian versions of such communication or document, the English version of such communication or document shall prevail, unless the document is a statutory or other official document.

27.2 This Agreement has been set forth and signed in both English and Ukrainian, provided, however, that in the event of any conflict or inconsistency or in case of doubt as to the proper interpretation or construction of this Agreement, the English text shall be controlling.

28. COUNTERPARTS

This Agreement may be executed in any number of counterparts and by different parties hereto in separate counterparts, each of which when so executed shall be deemed to be an original and all of which when so executed shall constitute one and the same binding agreement between the parties.

29. EFFECTIVENESS OF THE LOAN

The parties hereto intend to be bound by the provisions of this Agreement subject to the entry into force of the decision of the Kyiv City Council ratifying (approving upon execution) this Agreement and the Agreed Funding Source Agreements to which the Borrower is a party.

THE ISSUER

Bayerische Hypo- und Vereinsbank Aktiengesellschaft (“HypoVereinsbank” or the “Issuer” and, together with its consolidated subsidiaries, “HVB Group” or the “Group”), formed by the merger of Bayerische Vereinsbank AG (“Bayerische Vereinsbank”) and Bayerische Hypotheken- und Wechsel-Bank AG in 1998, is the parent company of HVB Group. Since December 2000, Bank Austria Aktiengesellschaft (“Bank Austria”), which had acquired Creditanstalt-Bankverein in 1997, combining Austria’s two largest banks (together, “Bank Austria Creditanstalt”), has been part of HVB Group. HVB Group is one of Europe’s leading providers of banking and financial services. Based on consolidated assets of Euro 483 billion at 31 March 2004, HVB Group is the second largest bank in Germany.

HVB Group offers a comprehensive range of banking and financial products and services to a broad range of customer groups in the retail, corporate and public sectors. HypoVereinsbank is one of only three private sector banks in Germany with the status of a mixed mortgage bank, meaning it is allowed to engage in commercial banking as well as mortgage banking activities, including in particular the issuance of Pfandbriefe for the purpose of refinancing its mortgage and public sector loans.

HypoVereinsbank has its registered office at Am Tucherpark 16, 80538 Munich, Germany, and is registered in the Commercial Register of Munich under number HRB 42148. Bayerische Vereinsbank was established on 11 April 1869 under the laws of Germany.

Share Capital

The issued and fully paid capital stock of HypoVereinsbank as of 15 April 2004 was Euro 2,252,097,420 divided into:

- (a) Euro 2,208,436,620 ordinary bearer shares, divided into 736,145,540 no-par value shares;
- (b) Euro 43,660,800 registered preference shares without voting rights, divided into 14,553,600 no-par value shares.

Supervisory Board and Management Board

Like all German stock corporations, HypoVereinsbank has a two-tier board system. The Management Board (*Vorstand*) is responsible for the management of HypoVereinsbank and the representation of HypoVereinsbank with respect to third parties, while the Supervisory Board (*Aufsichtsrat*) appoints and removes the members of the Management Board and supervises the activities of the Management Board.

The composition of the Supervisory Board and the Management Board of HypoVereinsbank and the primary occupations and residences of the members of its Supervisory Board are as follows:

Supervisory Board

Dr. Dr. h.c. Albrecht Schmidt, Chairman
Peter König, Deputy Chairman
Dr. Hans-Jürgen Schinzler, Deputy Chairman
Dr. Manfred Bischoff
Dr. Mathias Döpfner
Volker Doppelfeld
Klaus Grünewald
Anton Hofer
Max Dietrich Kley
Friedrich Koch
Hanns-Peter Kreuser
Dr. Lothar Meyer
Herbert Munker
Dr. Siegfried Sellitsch
Professor Dr. Wilhelm Simson
Professor Dr. Dr. h.c. Hans-Werner Sinn
Maria-Magdalena Stadler
Ursula Titze
Jens-Uwe Wächter
Helmut Wunder

Management Board

Dieter Rampl (Spokesman)

Dr. Stefan Jentzsch

Dr. Michael Kemmer

Michael Mendel

Gerhard Randa

Dr. Wolfgang Sprißler

Since the Issuer's sole obligation in respect of the Notes is to make certain payments as and when payments on the Loan are received pursuant to the Loan Agreement, financial information relating to the Issuer is not included in this Offering Circular.

THE CITY OF KYIV

Introduction and History

The City of Kyiv, which was founded over 1,500 years ago, is among the oldest cities in the world. One time capital of Kyivan Rus, the ancient Slavic state, it is now the capital of the independent nation of Ukraine. Today's Kyiv, with a population of approximately 2.6 million, is the financial, commercial, political, scientific and cultural centre of Ukraine.

Kyiv covers an area of more than 835 square kilometres and stands on both sides of the Dnipro River, which is the third longest river in Europe and runs from Russia through Byelorussia and Ukraine and into the Black Sea. The average temperature in Kyiv ranges from approximately 23.9°C in July to approximately minus 2.6°C in January.

Selected Financial and Economic Data

The following table sets out certain financial and economic data for the City for the periods specified:

	Year ended 31 December				
	2000	2001	2002	2003	2004 ⁽¹⁾
	(UAH millions)				
City Financial Data:					
Revenues:					
Tax revenues	3,155.3	3,977.4	3,739.3	3,303.2	3,050.2
Non-tax revenues	259.5	340.2	188.3	258.8	247.1
Revenues from Capital Transactions.....	0	21.6	220.7	421.9	419.9
Purpose Funds	106.6	286.0	100.4	262.9	321.7
Grants and subsidies from the State Budget.....	4.4	336.0	236.6	336.5	437.1
Transfer of funds from deposits	—	—	—	—	252.0
Total City revenues.....	3,525.8	4,961.2	4,485.3	4,583.3	4,728.0
Expenditures:					
Budget expenditures.....	2,219.2	2,855.2	2,703.4	3,817.0	5,382.0
Funds transferred to the State Budget	1,235.4	2,201.7	1,713.5	903.2	563.8
Total City expenditure.....	3,454.6	5,056.9	4,416.9	4,720.2	5,945.8
Surplus (deficit)⁽²⁾⁽³⁾	71.2	(95.7)	68.4	(136.9)	(1,217.8)

	Year ended 31 December				
	2000	2001	2002	2003	2004 ⁽⁷⁾
	(UAH billions except per capita GCP and GDP, population and inflation rates)				
City Economic Data:					
GCP at current prices:					
- Industry	3.5	4.1	4.5	5.3 ⁽⁴⁾	6.1
- Services	19.1	27.1	30.7	36.2	42.4
Total GCP at current prices	22.6	31.2	35.2	41.5⁽⁴⁾	48.5
Population (thousands).....	2,637	2,611 ⁽⁵⁾	2,616	2,639	2,745
GCP per capita at current prices (in UAH).....	8,570	11,949	13,456	15,726	17,668
City average annual rate of inflation.....	28.2	12.0	0.8	0.7	0.8
City Consumer Price Index (per cent.).....	130.0	107.0	103.6	108.1	n/a ⁽⁶⁾
Producer Price Index (per cent.).....	118.9	101.0	99.3	111.2	n/a ⁽⁶⁾
Ukraine Economic Data:					
Ukraine Consumer Price Index (per cent.).....	125.8	106.1	99.4	108.2	n/a ⁽⁶⁾
GDP at current prices.....	170.1	204.2	225.8	264.2	317.5
GDP per capita at current prices (in UAH).....	3,436	4,195	4,685	5,525	6,694

Notes:

- (1) Figures reflect the planned City Budget as approved by the City Council, not the results of implementation.
- (2) The deficit for 2001 reflects reserves from the 2000 budget year being used to make additional expenditures beyond revenues in the 2001 budget year. The deficit for 2003 and the deficit budgeted for 2004 principally reflect borrowings being made in the relevant budget year to finance expenditures in excess of revenues. The general fund of the City Budget, which constitutes 80% of the overall City Budget, had a surplus of UAH 148.2 million in 2003.
- (3) Any surplus in a given budget year is carried over into the corresponding budget category for the following year.

- (4) Preliminary data.
 (5) Figures reflect the results of the general census.
 (6) Information not available.
 (7) Forecast.

See “Presentation of Financial and Other Information – Exchange Rates” for the relevant U.S. dollar exchange rates.

Overview of Municipal Administration

The administrative-territorial structure of Ukraine is comprised of 24 oblasts (regions), the cities of Kyiv and Sevastopol, which have a special status as municipalities, and the Autonomous Republic of the Crimea. The Law of Ukraine on Local Self-Government, as adopted on 21 May 1997 (the “Law on Local Government”), provides for the system of local self-government in Ukraine and the organisation, legal status and responsibilities of bodies and officials of local governments in Ukraine. The status of Kyiv as the capital of Ukraine is regulated by the Law of Ukraine “On the Capital”, as adopted on 15 January 1999 (the “Law on the Capital”). Under the Law on the Capital, the City has the legal status of a municipality and the City Council is able to enter into contracts and legally act in its own name as a separate legal entity.

The City has two levels of government: the municipal government and the 10 self-administered municipal districts into which the City is divided. The two principal bodies in the municipal government are the City Council and the Kyiv City State Administration.

The City Council is a representative body currently comprised of 90 deputies and the Mayor. The City Council adopts City rules and regulations, approves the City Budget, determines the rates for local taxes and charges, approves programmes of economic and cultural development, manages the City’s communal property and exercises certain other powers in accordance with the Law on the Capital and other laws of Ukraine. However, rates of income tax, which is the most significant source of income for the City, are determined by the State.

Unlike other cities in Ukraine where the city council’s executive committee acts as the executive branch of the municipal government, in Kyiv the executive functions are performed by the Kyiv City State Administration, as provided for by Article 118 of the Constitution of Ukraine and Section 2 of the Final Provisions of the Law on the Capital. The Kyiv City State Administration, which is legally separate from the City Council, is both the executive body of the City Council and a local body of the executive branch of the State. In its capacity as the executive branch of the municipal government, the Kyiv City State Administration is accountable to, and is controlled by, the City Council. In its capacity as a local body of the executive branch of the State, it is accountable to the President of Ukraine and the Cabinet of Ministers of Ukraine and makes decisions on certain issues within the territory of Kyiv that relate to the State.

City Council

The City Council consists of the Mayor and City Council deputies, each of whom is elected by direct vote of residents of the City for terms of four years. The City Council meets at least once per quarter. The City Council’s current 90 deputies represent 12 political parties and coalitions. The most influential are the “Yednist” and “Nasha Ukrayina”. The “Yednist” party in Ukraine is headed by the current Mayor of Kyiv. The most recent elections for the City Council were held in 2002 and the next elections are due to be held in 2006.

The following table sets out the current political composition of the City Council resulting from the municipal elections held in 2002:

Political Party/Coalition	Number of Seats	Percentage of All Seats
Yednist ⁽¹⁾	34	38
Nasha Ukrayina.....	19	21
Yedyna Ukrayina	7	8
Kyiv Trudovi	9	10
Stolychnyi Region.....	9	10
Yevropeiska Stolytsa	8	9
Non-aligned	4	4
Total	90	100

Note:

- (1) Political party of the current Mayor of Kyiv.

The City Council's activities are carried out through the following 12 standing commissions:

- Commission on Budget and Socio-Economic Development;
- Commission on Urban Development and Land Use;
- Commission on City-Owned Properties;
- Commission on Legal Policies and Ethics Rules for Deputies;
- Commission on the Protection of Health and Social Services;
- Commission on Ecological Policies;
- Commission on Housing and Municipal Services and Fuel and Energy;
- Commission on Humanitarian Issues;
- Commission on Self-Government and Information Policies;
- Commission on Transport and Communications;
- Commission on Industries and Entrepreneurship; and
- Commission on Market Relations.

The standing commissions are formed by the City Council from among the City Council deputies to identify, study and review on a preliminary basis issues that are within the responsibility of the City Council and to monitor the implementation of the decisions of the City Council. In addition to the 12 standing commissions, the City Council also has the ability to establish interim commissions to address specific issues on the basis of the authority granted by local self-government legislation.

The responsibilities of the City Council include, among others:

- adopting City rules and regulations;
- approval of programmes for social, economic and cultural development, as well as special-purpose programmes relating to other issues of self-government;
- approval of the City Budget, making amendments to it and approval of its performance report;
- determination of local taxes and duties as well as their rates within the limits established by applicable law;
- approval of agreements made by the Mayor on behalf of the City Council with respect to the matters reserved for the City Council's exclusive authority;
- adoption of decisions to issue municipal bonds;
- adoption of decisions to receive loans from other sources (including from other local budgets), as well as to transfer funds within the City Budget;
- adoption of decisions to approve a preferential local tax and duty payment structure in accordance with applicable legislation;
- determination of the amount of income payable to the City Budget for the businesses, institutions and organisations that are owned by the City;
- adoption of decisions regarding the sale of City property in accordance with applicable legislation; approval of City privatisation programmes, including determination of which businesses to privatise; and adoption of decisions relating to the establishment, liquidation, restructuring and reorientation of City-owned businesses, institutions and organisations;
- adoption of decisions to delegate to other bodies some responsibilities relating to the management of City-owned property and defining the limits of those responsibilities, as well as the terms of their exercise;
- establishment of ad hoc bodies and services to carry out joint projects with other City-owned facilities or to provide joint financing (maintenance) for City businesses, institutions and organisations, and defining the terms of reference of these bodies and services;
- adoption of decisions to establish joint ventures with City-owned businesses, including those involving foreign investments;
- adoption of decisions to regulate land relations;
- determination of land tax rates and the rate of payment for the use of City-owned natural resources; and

- adoption of decisions to establish special free zones and other zones, to change the status of these zones and submission of relevant proposals on these matters to appropriate bodies; and provision of consent on the establishment of such zones at the initiative of the President of Ukraine or the Cabinet of Ministers of Ukraine.

Only the City Council is legally authorised to carry out external borrowing on behalf of the City.

The senior members of the City Council are:

Oleksandr Omelchenko is the Mayor of Kyiv and is also the head of the Kyiv City State Administration. Mr Omelchenko was born in 1938 and is a graduate of the Kyiv Construction Institute and Kyiv Institute of National Economy. See “– The Mayor of Kyiv” below.

Volodymyr Yalovy is the Deputy Mayor of Kyiv and Secretary of the City Council. Mr Yalovy was born in 1953 and is a graduate of the Kryvorizky Mining Institute.

The Mayor of Kyiv

The Mayor is elected by residents of Kyiv for a term of four years. The Mayor is the highest official within the City and heads the City Council. The responsibilities of the Mayor include, among others:

- organisation and supervision of the performance of functions by City executive bodies and supervision of the observance of the Constitution and Ukrainian legislation in the City;
- management of City Council personnel;
- convening sessions of the City Council, preparation of the agenda for such sessions and chairing the plenary sessions of the City Council;
- preparation of programmes for social, economic and cultural development of the City;
- preparation of the City Budget and reports on the City Budget’s implementation;
- appointment and dismissal of the chief officers of the Kyiv City State Administration;
- disposition of the budget funds pursuant to the provisions of the City Budget;
- representation of the City in relations with state authorities, other administrative units and in international relations;
- execution of agreements on behalf of the City;
- preparation of draft Ukrainian legislation related to the City;
- participation in the sessions of the Cabinet of Ministers of Ukraine, with the right of “advisory vote” (a non-counting vote) on issues related to the City; and
- approval of the appointment of the chief officers of City-owned businesses and of dually-subordinated operating units of the Kyiv City State Administration.

The Mayor can be removed from office by a decision of the President of Ukraine upon: (i) his application to the City Council requesting his removal from office; (ii) termination of his citizenship; (iii) a court verdict being entered against him; (iv) his violation of the statutory restrictions with respect to the simultaneous holding by the Mayor of certain positions; (v) a court decision rendering him incapable, missing or dead; and (vi) his death. In addition, the Mayor can be removed from office if he violates the laws or Constitution of Ukraine or the rights and freedoms of individuals or fails to exercise the powers granted to the Mayor by law. In the cases described in the preceding sentence, the issue of the removal of the Mayor from office must be considered by the City Council following the submission of a petition by not less than half of the deputies of the City Council.

The current Mayor of Kyiv is Oleksandr Omelchenko. He was re-elected Mayor in 2002 for a second four-year term expiring in 2006. In 1999, Mr Omelchenko was elected with 72.3 per cent. of the popular vote and in 2002 he was elected with 63.6 per cent. of the popular vote. He is a member of the “Yednist” political party.

The Law on the Capital requires that the head of the City Council and the head of the Kyiv City State Administration be the same person. Accordingly, Mr Omelchenko currently serves as the head of both of these bodies. According to the Law of Ukraine “On Civil Service”, the maximum age for civil service in Ukraine is 60 years for men and 55 years for women, but under certain circumstances these ages may be extended for up to five years. In his capacity as Mayor, Mr Omelchenko’s term of office is not subject to a mandatory retirement age. However, in his capacity as the Head of the Kyiv City State Administration, Mr Omelchenko reached the age of 65 on 9 August 2003, which placed him beyond the five-year extension. Pursuant to the Law on Local Government and the Law on the

Capital, the removal of the Head of the Kyiv City State Administration from office is required to be made by a separate decision of the President of Ukraine. As a result, Mr Omelchenko's having attained the age of 65 did not lead to the automatic termination of his term of office as the Head of the Kyiv City State Administration. In December 2003, the Constitutional Court of Ukraine issued a decision that a mayor of Kyiv who is simultaneously head of the Kyiv City State Administration is not subject to maximum age restrictions for holding office. Accordingly, Mr Omelchenko is not subject to mandatory retirement during his current term.

Kyiv City State Administration

The Kyiv City State Administration is the executive body of the City Council and is also a part of the executive branch of the State. The activities of the Kyiv City State Administration are regulated by the Law of Ukraine "On Local State Administrations" of 9 April 1999.

The Head of the Kyiv City State Administration is appointed to office and dismissed from office by the President of Ukraine on the basis of a recommendation by the Cabinet of Ministers of Ukraine. Deputy Heads of the Kyiv City State Administration whose powers relate to the Kyiv City State Administration in its capacity as a local branch of the State, including the First Deputy Head, are appointed and dismissed by the Mayor upon approval of the President of Ukraine and the Cabinet of Ministers of Ukraine. Deputy Heads of the Kyiv City State Administration whose powers relate to the Kyiv City State Administration's capacity as the executive body of the City Council are appointed and dismissed by the Mayor upon approval of the City Council. The current head of the Kyiv City State Administration is the Mayor of Kyiv. Therefore, the Mayor currently serves as the head of both the City Council and the Kyiv City State Administration.

As a local branch of the State, the Kyiv City State Administration functions within the structures of both the City Council and the State according to the principle of dual subordination, whereby it is accountable and reports to:

- the City Council with regard to responsibilities it performs in its capacity as the executive body of the City Council; and
- the President of Ukraine, the Cabinet of Ministers of Ukraine and other bodies of the executive branch of the State in its capacity as a local branch of the State.

The Kyiv City State Administration is currently composed of various offices, services, departments, committees and branches and their respective subsidiary organisations responsible for the administration and operation of the City. The organisation of the Kyiv City State Administration consists of three levels: operating units directly subordinated to the City; operating units dually subordinated to the City and the State; and territorial branches of the State. Activities of directly subordinated operating units are controlled by the Kyiv City State Administration. Dually subordinated operating units report equally to the Kyiv City State Administration and the relevant bodies of the State and their heads are appointed by the head of the Kyiv City State Administration, with the approval of the State. Territorial branches of central executive bodies report directly to the State and co-ordinate their activities with the Kyiv City State Administration.

Operating units directly subordinated to the City include, among others:

- General Administration Office of the Kyiv City State Administration;
- Main Office of Housing Economy;
- Main Office of Housing Supply;
- Main Office of Communal Property of the City of Kyiv;
- Main Office of Municipal Improvements Control and External Design;
- Main Office of Fuel and Energy and Energy Saving;
- Main Office of Internal Policy;
- Main Office of Interaction with Media and Public Relations;
- Main Office of Consumer Markets and Trade;
- Main Office of Consumer Services and Markets;
- Office of State Architectural and Construction Control;
- Office of Veterinary Maintenance;
- Office of Environmental Protection;

- Main Office of Pricing Policy;
- Main Office of Ritual Services;
- Main Office of Industry, Transport and Communications;
- Main Office on Entrepreneurship;
- Office of Women, Invalids, Veterans of War and Labour Matters;
- Service of Minors' Matters;
- Department of Labour Protection;
- Main Office of Legal Policy;
- Main Office of Physical Culture and Sports;
- Main Office of Municipal and Hotel Economy and Tourism; and
- Main Office of Land Resources.

Operating units dually subordinated to the City and the State include, among others:

- Main Financial Office;
- Main Office of Economics and Investments;
- Main Office of Youth and Family Matters;
- Main Office of Culture and Art;
- Main Office of Urban Development, Architecture and Urban Area Design;
- Main Office of Education and Science;
- Main Office of Health Protection and Health Care;
- Main Office of Emergency Situations;
- Main Office of Social Security;
- Main Office of Population's Protection from Chernobyl Effects;
- Main Office of Labour and Employment; and
- Office of Nationalities and Migration Matters.

Territorial branches of central executive bodies include, among others:

- Regional Branch of the State Property Fund;
- Kyiv Customs House;
- Kyiv Branch of the NBU;
- State Tax Administration in the City of Kyiv;
- Department of the State Treasury in the City of Kyiv;
- Branch Office of the Securities Commission; and
- Office of the Pension Fund of Ukraine.

The Kyiv City State Administration's operating units, including the Main Financial Office and others, are responsible for external debt management and the efficient use of the City's borrowed funds.

The senior members of the Kyiv City State Administration are, in addition to the Mayor:

Ivan Fomenko is the First Deputy Head of the Kyiv City State Administration responsible for the general management and supervision of the activities of the offices and departments of the Kyiv City State Administration. Mr Fomenko was born in 1942 and is a graduate of the Kyiv Engineering and Construction Institute.

Valeriy Borysov is the First Deputy Head of the Kyiv City State Administration/Head of the Main Office of Economy and City Development, responsible for Economic Policy and Development. His areas of responsibility include co-ordination of the City's economic policy and development and structural transformation of the City's economy. Mr Borysov was born in 1957 and is a graduate of the Kyiv Institute of the Food Industry.

Viktor Padalka is the Deputy Head of the Kyiv City State Administration/Head of the Main Financial Office, responsible for Financial Policy. His areas of responsibility include co-ordination of the City's

financial, investment and taxation policy and supervision of the performance of the City Budget. Mr Padalka was born in 1952 and is a graduate of the Kyiv Institute of National Economy.

Mykhailo Pozhyvanov is the Deputy Head of the Kyiv City State Administration. His areas of responsibility include housing and utilities, hotel economy and the development of tourism. Mr Pozhyvanov was born in 1960 and is a graduate of the Moscow Institute of Steel and Alloys.

Administrative Districts of the City

The administrative structure of the City is comprised of 10 City districts. The districts are administrative units, each of which is organised and administered by a district council and a district state administration as described below. Prior to an administrative restructuring at the end of 2001, there were 14 districts as well as the settlement of Pushcha-Vodytsya. The basic principles of the City's administrative structure are prescribed by the Law on the Capital.

The following table sets out the population and territorial size of each of the City's 10 districts and the number of deputies in the respective district councils:

No.	District	Population (thousands)	Territory (thousands of hectares)	Number of Deputies in District Council
1.	Holosiyivsky	208.9	15.6	60
2.	Darnytsky	290.6	13.3	60
3.	Desnyansky.....	340.2	14.8	50
4.	Dniprovsky.....	331.5	6.7	60
5.	Obolonsky	306.9	11.0	50
6.	Pechersky	130.4	2.0	45
7.	Podilsky	181.4	3.4	55
8.	Svyatoshynsky	318.4	10.1	60
9.	Solomyansky.....	297.2	4.0	60
10.	Shevchenkivsky.....	233.5	2.7	60

Each City district is organised and administered on the same lines as the City, having its own district council and district state administration. District councils are separate legal entities from the City Council. District state administrations function in the districts of the City and are accountable on one hand to the district council and on the other hand to the Kyiv City State Administration, in the same way that the Kyiv City State Administration is accountable on one hand to the City Council and on the other hand to the State. The City Council is responsible for the administration of the districts. Deputies of each district council elect a head of the district from among themselves.

The City Council may delegate to the district councils the right to manage land, buildings and fixtures and movable property belonging to the City and located in their respective districts. The districts manage the assets entrusted to them within the scope set out under applicable legislation. Such powers are limited with regard to sale and encumbering of assets. Certain assets of the City (such as schools and hospitals) have been transferred to the City districts and are legally owned by the districts, although the City may require the districts to transfer such assets back to it, subject to taking certain actions. District councils also have the authority, based on a delegation of power from the City Council, to form, approve and execute district budgets and to exercise other powers under applicable legislation. The districts are prohibited from receiving loans and credits.

The Judicial System in Kyiv

Ukraine operates a unified judicial system with national courts operating throughout Ukraine, including the Kyiv Commercial Court and local common courts. There are no municipal courts, as the entire judicial system is national. The Kyiv Commercial Court hears disputes relating to the commercial interests of businesses and organisations. Common courts are courts of general jurisdiction and adjudicate civil, criminal and administrative cases as courts of first instance. There are 10 local common courts operating in Kyiv, corresponding to and located in the 10 administrative districts of the City. Also located in the City are the Kyiv Commercial Appellate Court and the Kyiv Court of Appeals, which are the first courts of appeal for the Kyiv Commercial Court and the local common courts, respectively. Criminal and civil proceedings in the City as well as in the rest of Ukraine are governed by the relevant national legislation, which is binding on the courts in the City. See "Ukraine – Political Structure and Recent Developments – The Judicial System and Legal Framework".

Major Activities of the City

Overview

The main responsibilities of the City include the administration and management of its own property and financial funds, the provision of public services, the provision of support for economic development, urban development and planning and the implementation of Ukrainian regulations and administration.

In 2003, the expenditures of the City Budget were on the following primary activities: education; health care; welfare (social services); housing and utilities; construction; transport and infrastructure; culture and art; and environmental protection. See “City Budget and Financial Information-Budget Expenditures” for details of such expenditures. These services are provided directly by the City as well as by various independent businesses or businesses controlled by the City, whose costs are subsidised by the City.

Education

The City’s education activities include, among others, funding and operating schools, boarding schools, technical schools and colleges and certain municipal institutions of higher education (academies and institutes).

As at 31 December 2003, there were 1,344 educational institutions operating in the City and supervised by the Main Education and Science Department of the Kyiv City State Administration for the benefit of approximately 792,368 persons, including 667 pre-schools, 529 day secondary schools, 31 vocational schools and 117 institutions of higher education (comprising 67 universities and institutes and 50 colleges); 320 of these institutions are private, self-financed institutions and 1,024 are being financed from the 2004 City Budget. Institutions of higher education such as institutes, academies and universities are funded by the State Budget and private sources, although certain municipal institutions are funded by the City. The City undertakes certain activities in connection with the welfare of students in higher education in the City.

From 1999 to 2002, the City created 5,712 new student places at existing and new educational institutions, and 1,280 additional places were created within existing educational institutions in 2003.

The City Council has adopted a programme entitled “Education in the Capital (2001-2005)”, which sets out the legal and organisational framework for the future development of public education in the City.

Health Care

The City provides primary health and ambulatory care, hospitals and health education to residents of Kyiv. State guaranteed medical care for Kyiv residents is financed from the City Budget and from City district budgets. There are currently 97 City-funded, State-funded and privately-funded hospitals and 238 clinics operating in Kyiv. The 2004 City Budget provides for the financing of 67 hospitals and 100 outpatient clinics, sub-clinics and other medical care institutions such as child-care homes and maternity hospitals. Kyiv has a centralised ambulance service, which includes four major stations located across the City operated by the Main Health Care Department of the Kyiv City State Administration. The activities of medical institutions of the City are performed in accordance with a number of municipal medical programmes, which operate pursuant to the Law of Ukraine “Fundamentals of the Health Care Legislation of Ukraine” of 19 November 1992.

City residents may choose private health care as an alternative. Voluntary medical insurance and private medical care continue to develop in parallel with state guaranteed medical services. Certain national medical institutions are also located in the City but are financed from the State Budget and other sources and not from the City Budget or City district budgets.

The City believes that the entire Ukrainian health care sector, including Kyiv’s health care system, needs substantial financial investment. Due to lack of financial resources, Kyiv’s health care system is unable to ensure the ability to provide an adequate level of quality health care to all segments of the City’s population. Medical clinics and centres have been required to narrow their range of medical research and have been unable to introduce new technologies due to lack of funds. There is a high rate of acute infection sickness among the City’s population, and there has been an increase in the rates of occurrences of AIDS and certain other diseases in recent years. The City’s proposed investment projects in the health care sector include the construction of a blood transfusion centre that meets European quality standards.

In order to improve the financing of the health care institutions in the City, the Kyiv City State Administration prepared a draft Law of Ukraine “On the Experiment in the City of Kyiv on Mandatory Medical Insurance”, which was submitted to Parliament in 2001. Such law, if approved by Parliament, is expected to improve the financing of health care in the City and thereby contribute to the modernisation and self-sufficiency of Kyiv’s medical institutions.

Welfare (Social Services)

The City provides a wide range of social services for its residents, including:

- social services for retired and disabled people;
- social services and policy development for youths and juveniles;
- public assistance to families with more than one child, low-income families and disabled people;
- payment of compensation to rehabilitated people; and
- provision of benefits to Chernobyl victims.

The 2004 City Budget provides for the funding of numerous social service centres in the City, including two boarding schools for disabled children providing 490 beds, five homes for elderly and disabled people providing 2,017 beds, 14 district social service centres and divisions for needy and disabled people, three orphanages, a women’s family violence shelter, a labour rehabilitation centre for the mentally handicapped and a veterans’ centre. In each of 2001, 2002 and 2003, approximately 50,000 people received some form of social welfare service.

All pensions in Ukraine are paid out of the Pension Fund of Ukraine, a national non-budgetary fund, although the City has disbursed additional payments for unemployed pensioners and certain other categories of pensioners, including veterans of the Second World War. Certain categories of residents of the City are eligible for, and receive social support from, national funds such as child and maternity benefits.

Housing and Utilities

Housing

Kyiv has 61.5 million square metres of buildings, of which 49.8 million square metres comprise residential property. Approximately 45.5 million square metres of the total area of buildings are owned by the City. The remaining 16 million square metres are owned by the State, State-owned businesses, municipal businesses and private businesses.

Since the initiation of the City’s Housing Privatisation Programme, which began in 1993, approximately 74 per cent. of the housing units in the City have been transferred free of charge to their occupants. Most of the remaining housing units in Kyiv are owned by the City and let to City residents at lower than market rates. The City also finances the construction of new housing, which is either sold or transferred free of charge to City residents. Building affordable housing is a policy objective for the Kyiv City State Administration. In 2003, the City built approximately 16 per cent. of all of the municipal housing built in Ukraine in that year, which is more than the amount built by any other region or City in Ukraine. New housing projects in the City are mainly taking place on the left bank of the Dnipro River.

The City is responsible for the maintenance of City-owned apartment buildings in Kyiv, including buildings in which apartments within the buildings have been transferred to City residents as part of the Housing Privatisation Programme. In each of 2000, 2001, 2002 and 2003, City residents paid approximately 60 per cent. of the estimated cost of maintaining and providing communal services to their apartment buildings. The City expects that the full cost of maintaining City-owned residential property will be transferred to the occupants of such property within the next several years. The timing in which this will occur is subject to political decision-making and is therefore uncertain.

Utilities

Currently, approximately 95 per cent. of the total cost of utilities is borne by the residents of the City, with the remainder subsidised by the City. Subsidies and benefits for utilities from the City Budget are generally only provided to qualifying low-income families, war veterans, retired military personnel and Chernobyl victims. Pursuant to applicable law, such expenses of the City are to be compensated by a grant provided to the City from the State Budget, but in practice such expenses are often not compensated in a timely manner.

The City's public utilities assets are in poor condition, and the public utility system is characterised by declining quality of services, irregularity of supply and increasing prices of services. Investments are necessary for upgrading existing facilities, introducing resource-saving technologies and constructing new facilities necessary for the functioning and development of the City. The City Budget is essentially the only source of funds for capital investments in the public utilities area, as municipal businesses do not have their own funds for improvements and expansion, and the shortage of funds in this area is exacerbated by a failure of consumers to make payments for public services on a timely basis. The most significant proposed investment projects in this area for the 2004 budget year are construction of sewage collectors, assembly of an aeration plant, construction of a waste recycling plant and certain construction projects to improve the quality of the water supply. See “– Construction” below.

Electricity. Electric power for Kyiv is generated mainly by Kyivenergo, a company which is majority owned by the State and partly owned by the City but is managed by the City. The power supply for the City is considered to be adequate with the exception of the central part of the City, where it is provided by old substations built in the mid-1960s, which are unable to sustain increasing loads and do not meet safety requirements. The City does not subsidise the cost of electricity to Kyiv residents, although industrial consumers pay substantially higher tariffs for electricity than the general population.

Gas. Gas supply and maintenance of the gas network is provided by Kyivgas, a company in which the City owns a controlling interest. Kyivgas's gas supply network extends for approximately 3,224.0 kilometres. In 2003, Kyiv consumers received over 4.4 billion cubic metres of natural gas, less than 7.2 per cent. of which was supplied to residential customers. Since 1990, there has been a trend of decreased consumption of natural gas at plants and factories and increased consumption of natural gas by residential customers. As at 1 January 2003, approximately 77 per cent. of the total number of apartments in the City had access to gas services, with 22 per cent. relying on electrical appliances for cooking.

Central heating. Principal service providers for the generation and transfer of central heating to City residents include Kyivenergo and Ukr-Can Power. Ukr-Can Power is a joint venture between the State and a private entity. In 2003, City residents paid approximately 90 per cent. of the cost of such heat, and the remainder was paid by the City. In previous years the percentage paid by residents was significantly lower, but such percentage has increased with the improvement of the economic well-being of the population and improvements in collecting payments from consumers.

Water. The principal owner and service provider of the water supply system in the City is the Kyivvodokanal company, which is majority-owned by the City. In 2003, Kyivvodokanal supplied on average approximately 1.3 million cubic metres of drinking water per day. The total length of the City's water supply system exceeds 4,000 kilometres and the length of the water pipeline that feeds water into the water supply system is 62 kilometres. The City's water is supplied from three independent sources: the Dnipro River and Desna River (together accounting for approximately 80 per cent. of supply) and underground natural reservoirs. In 2003, Kyiv citizens paid 100 per cent. of the cost of water.

Sewage. The City's sewage system is over 2,500 kilometres long. All sewage run-off is subject to treatment. The capacity of the sewage treatment system is 1,800,000 cubic metres per day, which exceeds the annual amount of sewage run-off water. The Kyivvodokanal company operates waste water processing facilities supplied by 33 pump stations. In 2003, City residents paid 100 per cent. of the cost of waste disposal services. The City's sewage system is functioning at capacity and requires expansion. Moreover, the quality of Kyiv's sewage water treatment is considered to be below acceptable standards. For example, approximately 35 per cent. of the total length of Kyivvodokanal's sewage network is beyond the usage life recommended by the manufacturer. Water supply problems have arisen due to insufficient sewage capabilities. The City intends to sell part of its shareholding in the Kyivvodokanal company in order, among other things, to attract investment for the purpose of funding improvements to the sewage system. See “–Privatisation” and “City Budget and Financial Information – Indebtedness of the City of Kyiv – Guarantees”.

Construction

The City's construction activities include construction and reconstruction projects in the areas of transport and infrastructure, public utilities, housing, health care facilities, educational facilities, cultural facilities and other areas.

Construction is the largest expenditure item in the 2004 City Budget, as was the case in 2003. Construction expenditures in 2003 were almost three times greater than in 2002. This increase in

construction activity is attributable to construction projects being undertaken in 2003 using financing obtained during 2003, including an offering of notes and domestic borrowings. Construction activities in 2004 include primarily transport and infrastructure projects, including the construction of the new Podilskiy bridge over the Dnipro River, a new cardiological centre, a new waste recycling plant, new metro lines, roads, sewage collectors and related infrastructure, the assembly of an aeration plant and certain construction projects to improve the quality of the water supply and other utility facilities. See “Use of Proceeds” and “City Budget and Financial Information – Budget Expenditures – Construction”.

The City Council has approved a master plan for the development of the City through the year 2020. The master plan provides for the main directions of the development of Kyiv in terms of new construction, infrastructure and architectural requirements, zoning and planning.

Transport and Infrastructure

The City is responsible for the maintenance and the cost of financing repairs, renovations and reconstruction of all roads and transport routes within Kyiv. Kyiv has extensive infrastructure that is operating at capacity and is in need of much upgrading, and demand for public transport services is expected to increase each year for the foreseeable future. Significant financing, including external borrowings, and investment is needed in order to upgrade and expand the City’s public transport system. The City seeks to develop the road and transport route network in Kyiv in order to bring it in line with European standards, particularly in terms of the time spent by residents to travel from their residences to work places. Specific proposed investment projects for the development of the City’s road and transport route network include the extension of several metro lines, substantial road-building in the Kharkovskiy district and the reconstruction of a rapid-transit tram line. See “–Construction” above. The City also partly subsidises the operating costs of the public transport system, on which more than 1.7 billion passenger journeys are made annually. The City intends to continue to increase the proportion of the cost of public transport borne by users and intends to increase fares to a level which fully covers the current operating costs of the public transport system, although it is not certain when such increase will take effect. See “–City Economy – Recent Rising Price of Oil”.

Roads

As at 31 December 2003, there were approximately 1,630 kilometres of roads in Kyiv, 1,605 kilometres of which are hard-surface streets and highways. Kyiv’s roads include 11 radial highways, two meridional roads and two semi-ring roads. The City’s streets are illuminated by approximately 129,200 lamp posts, providing lighting for 98.9 per cent. of the road network.

While the City believes that the actual condition of the City’s existing roads is generally in line with European standards, the current extent of Kyiv’s road network (length of roads compared to size of territory and number of residents) is one of the lowest among European capitals, and traffic capacity in many areas is insufficient. The City considers reducing traffic congestion to be a policy priority and is taking various steps to attempt to alleviate it, such as constructing underground pedestrian walkways. (See also “–Environmental Protection” below regarding further measures to reduce traffic which are under consideration.) Currently the City funds the construction, renovation and maintenance of all major roads in Kyiv from the City Budget and funds provided by the State Budget.

Public Transport

Metro. The Kyiv metro extends over 54.9 kilometres and includes 619 metro cars, 42 stations and three lines as at 1 January 2004. Approximately 598 million passenger journeys were made on the Kyiv metro in 2003. The metro is the major part of the City’s transport system and is owned by the City. The metro system is being expanded. Two new metro stations were built in 2003 and further stations are currently under construction. The City subsidises the metro operating and maintenance expenses not otherwise covered by passenger fares. The Kyiv metro is not subsidised by the State Budget.

Ground Transport. As at 31 December 2003, the City’s ground public transport infrastructure consists of 111 kilometres of tram lines, 172 kilometres of trolley lines and 490 kilometres of bus lines. Approximately 210 million, 310 million and 350 million passenger journeys were made on the Kyiv tram, trolley and bus systems, respectively, in 2003. There were 149 regular bus routes and 317 “shuttle” bus routes, 41 trolley routes and 26 tram routes and the City’s municipal transport companies had a fleet of 1,243 buses, 400 trolleys, 372 tram cars and 4 funicular trams. Currently,

ground transport services are subsidised by the City to cover operating and maintenance expenses not otherwise covered by passenger fares as well as to subsidise the travel of special categories of passengers. The companies that run the ground transport system are owned and controlled by the City. In 2003, subsidies to cover running costs for ground transport equalled UAH 154.2 million, compared to UAH 142.0 million allocated in 2002.

The City seeks to improve the quality of its public transport system so as to bring it in line with European standards, including with respect to the areas of maximum passenger load on public transport during rush hours and accessibility of public transport to disabled customers. The City has prioritised the use of the metro due to it being the most environmentally sound type of public transport. See “City Budget and Financial Information – Budget Expenditures – Transport and Infrastructure”.

Airports

There are two airports operating in the vicinity of the City: Boryspil Airport and Zhulyany Airport. Boryspil Airport is the main international airport in Ukraine and it is owned and operated by the State. Zhulyany Airport is principally used for domestic flights and it is owned by the City. Zhulyany airport is in need of reconstruction and expansion in order to provide more international flights.

Telecommunications

The public switched telecommunications network in Kyiv is owned and operated by Ukrtelecom, a joint stock company controlled by the State. The City is not a shareholder in the company and does not provide financing from the City Budget for operational costs or the construction of telephone switch facilities. Telecommunications infrastructure currently covers a majority of the geographic area of the City, and full coverage of the City is expected to be achieved in 2004.

Culture and Art

The City’s culture and art activities include establishing and operating museums, galleries, libraries, public archives, theatres, concert organisations, clubs, cinemas, recreation and entertainment parks, cultural and art projects, State and City holiday events, festivals, exhibitions and concerts. The City has a “Culture and Art of the Capital – Years 2003-2005” programme, which provides for a number of projects to preserve Kyiv’s historical and cultural heritage, including restoration of the Kyiv-Pechersk Lavra Cave Monastery, which is being funded jointly by the City and the State, and the reconstruction of the Kyiv Zoo facilities and the construction of the National Puppet Theatre, which are being funded solely by the City.

Environmental Protection

Environmental protection activities are largely performed by the State. The City nonetheless provides a variety of environmental protection services including the disposal of domestic and industrial waste and the disposal of nuclear waste from medical and scientific research institutions within the City. The City also provides sanitary and public hygiene monitoring services. The City’s environmental protection activities are funded from Purpose Funds in the City Budget. See “City Budget and Financial Information – Budget Expenditures – Purpose Fund Expenditures”.

Pollution from industrial businesses located within the City limits has decreased in recent years, due to a decline in industrial production. However, the growth in the number of cars has led to a significant increase in automobile-generated emissions. The City continues to take a number of measures relating to the control of pollution and the protection of the environment, including increasing control over emission of pollutants (including by assessing fines), increasing the environmental safety of the City’s public transport and establishing a municipal environmental enforcement authority. The City is considering various schemes to reduce traffic pollution in the city centre, such as imposing tolls on the City’s bridges to reduce the volume of traffic and replacing buses with electric trams or trolley buses. It is also considering various incentives to move industrial plants out of the City. In addition, the City intends to construct a new waste recycling plant for sorting and recycling household and industrial waste and four new primary waste sorting stations during 2004-2005. See “–Construction” above.

Law Enforcement and Emergency Services

The State Budget currently finances all law enforcement services for the City. The Ministry of Internal Affairs is responsible for the maintenance of order in the City, the security of individuals and the protection of property. The Main Department of the Ministry of Internal Affairs is located in Kyiv, and there are also 10 district departments of the Ministry of Internal Affairs in the City. The State Fire Safety Department operates more than 25 fire stations within the City. This department has

approximately 166 fire engines and employs approximately 2,764 people in the City. The City is not responsible for maintenance and operation of the penal system, which is within the competence of the State authorities. The City recently obtained the right under Ukrainian law to establish a municipal police force by way of a resolution of the City Council.

City Economy

In 2003, Kyiv accounted for approximately one sixth of the gross domestic product of Ukraine. Industries such as machine building, metal working and food production have traditionally been, and continue to be, important industrial sectors of the municipal economy. The industrial sector, which includes machine building and metal working, chemicals and petrochemicals, electric power, food production, production of clothes and shoes, textiles, paper, wood and other processing, manufacturing and related industrial areas, is the largest source of employment in the City, providing employment to more than 280,000 people. Key services areas of the Kyiv economy include transport and communications, trade, food services, material and technical supply and procurement, science and scientific services and financial services. The City is the largest educational centre in Ukraine and has 67 universities and approximately 322,400 students. Approximately 2 million visitors a year attend international exhibitions and trade fairs held in the City.

The importance of Kyiv in the Ukrainian economy is demonstrated by the following table, which shows the percentage of the Ukrainian economy represented by Kyiv in the categories listed and for the years listed:

	1990	1999	2000	2001	2002	2003
	(per cent.)					
Indicator						
Population.....	5.1	5.3	5.3	5.4	5.5	5.6
Manpower resources (average annual labour force).....	5.9	6.0	6.2	6.6	6.9	7.1 ⁽¹⁾
Gross City Product/Gross Domestic Product.....	8.4	10.2	15.7	17.3	17.5	17.6 ⁽¹⁾
Industrial output.....	6.2	4.8	5.1	5.2	5.1	4.6
Capital investments.....	6.3	15.9	16.1	17.3	15.9	16.6
Volume of foreign direct investment	n/a ⁽²⁾	31.8	33.3	33.8	34.1	31.9
Housing construction.....	6.6	12.0	15.5	16.9	16.4	15.6
Retail trade	7.7	15.3	14.3	14.8	14.8	15.3
Services sector revenue.....	8.6	12.6	14.7	19.5	22.0	n/a ⁽²⁾
Net profit of companies located in jurisdiction.....	6.4	38.0	47.9	56.0	62.0	47.4

Source: State Committee of Statistics

Notes:

(1) Preliminary data.

(2) Information not available.

Demographics

Kyiv is the largest city in Ukraine, with a population of 2.6 million, representing approximately 5.6 per cent. of the total population of Ukraine. Since 1990, the City's population has remained generally constant, notwithstanding deaths exceeding births, due primarily to migration to the City from other regions of Ukraine, which is in turn due to more favourable economic and social residential conditions in the City compared to other regions of Ukraine.

The City is highly urbanised. Population density is 3,221 inhabitants per square kilometre. However, 67 per cent. of the City's territory is covered by public parks, and population density in the City's territory that does not constitute public park land is approximately 10,000 inhabitants per square kilometre.

In 2003, the number of deaths in the City exceeded births by approximately 4,859. The mortality rate for residents of working age remains high. Deaths among people of working age amounted to 25 per cent. of all deaths in 2001, of which males constituted 74 per cent. The relatively low birth rate and high death rate among younger people has led to an increase in the average age of the population. At the beginning of 2004, 15.4 per cent. of the total population of the City was under 15 years of age and 18.7 per cent. of the total population of the City was over 55 years of age, as compared to 23 per cent. and 15 per cent., respectively, in 1990. The average life expectancy of residents of Kyiv has

increased from 70.5 years in 1990 to 71.5 years in 2003. Infant mortality has decreased from 10.2 per 1,000 in 2000 to 9.3 per 1,000 in 2002 to 6.8 per 1,000 at the beginning of 2004.

The following table sets out information on the birth and death rates in the City from 1999 to 2003:

	1999	2000	2001	2002	2003
Indicator					
Number of births.....	18,323	18,954	19,360	21,156	23,275
Birth rate per 1,000	7.0	7.2	7.3	8.1	8.8
Number of deaths.....	26,042	26,603	27,168	27,641	28,134
Death rate per 1,000.....	9.9	10.1	10.3	10.6	10.7

Source: State Committee of Statistics

At present, the City's labour force (those people capable of employment) is approximately 78 per cent. of the resident population, or 2,069,000 people. The City projects that the total population of the City will stay generally constant through 2020 and that the size of the labour force in the City will gradually increase in the coming years due primarily to the migration to the City of people seeking employment.

Employment and Wages

On average during 2003, there were approximately 1,448,000 people working in the City (approximately 55 per cent. of Kyiv's total resident population), as compared with 1,410,000 people in 2002. The increase from 2002 to 2003 is largely attributable to the migration of people from other parts of Ukraine to Kyiv. The City believes that the number of workers in the City at present is relatively stable.

In 2003, the public sector of the economy (including both City and State employees) employed approximately 637,000 people and the private sector employed approximately 811,000 people. The gap between the number of people working in the public and the private sectors is gradually widening, with the number of private sector employees growing larger by comparison with the public sector. The widening of the gap between private sector employees and public sector employees is being offset in part by the high level of construction activity, primarily on housing, in respect of which the City, either directly or through businesses it owns or controls, is a significant employer.

Since 1997, there have been no strikes, lock-outs or other industrial action by employees of the City or City-owned businesses.

Composition of Employed Labour Force

The following table shows the total number of people employed in the public and private sectors in both the City and in Ukraine for the periods indicated, in thousands of persons and percentages. Percentages are expressed as a proportion of the total labour force of the City or of Ukraine, as the case may be:

	1999		2000		2001		2002		2003	
	Kyiv	Ukraine ⁽¹⁾								
Public sector ⁽²⁾	618	7,640	604	7,232	596	7,120	635	7,276	637	7,062
	47%	35%	46%	34%	45%	34%	45%	34%	44%	33%
Private sector, mixed and foreign.....	694	14,184	711	14,038	729	13,822	775	14,124	811	14,338
	53%	65%	54%	66%	55%	66%	55%	66%	56%	67%
Labour in employment.....	1,312	21,824	1,315	21,270	1,325	20,942	1,410	21,400	1,448	21,400
	69%	73%	68%	71%	69%	70%	71%	70	70	69
Labour force ⁽³⁾	1,902	29,900	1,923	30,000	1,927	30,000	1,977	30,571	2,069	31,014

Source: State Committee of Statistics

Notes:

(1) Preliminary data.

(2) Includes both City and State employees and employees of City- and State-owned businesses. The City employed 4,144, 4,144, 5,258 and 4,810 people, respectively, as at 31 December 2000, 2001, 2002 and 2003.

(3) Based on figures calculated by the Ministry of Labour of Ukraine using an internationally accepted methodology of household surveys, which includes all persons capable of working between the ages of 15 and 70.

As of 1 April 2004, the City and City districts employed 4,810 people, or 0.23 per cent. of the employed labour force in Kyiv. The City anticipates that the number of City and City district employees will remain stable in the coming years.

The following table sets out the average number of employees in Kyiv in certain principal sub-sectors for the years indicated:

	1999	2000	2001	2002	2003 ⁽¹⁾
	(thousands)				
Sub-sector					
Industry ⁽²⁾	201.2	211.9	249.3	250.7	280.2
Construction	111.1	114.5	121.5	127.8	99.3
Trade and public catering.....	145.0	150.9	252.9	276.0	283.3
Transport, communication and post	107.4	99.3	113.9	125.8	125.4
Financial sector	28.0	25.5	44.5	35.8	55.4
Other ⁽³⁾	719.4	712.2	664.6	595.1	604.7
Total	1,312.1	1,314.3	1,332.8	1,411.2	1,448.3

Source: State Committee of Statistics

Notes:

(1) Preliminary data.

(2) Includes machine building and metal working, chemicals and petrochemicals, electric power, food production, production of clothes and shoes, textiles, paper, wood and other processing, manufacturing and related industrial areas.

(3) Other includes public sector and other non-principal sub-sectors.

In 2003, the average number of full-time employees in large and medium-size businesses in Kyiv was 865,900 people or 60 per cent. of the total labour force in employment.

Wages

In 2003, the average monthly nominal wage in Kyiv was UAH 761, an increase of 18.3 per cent. as compared to 2002. The average real wage, adjusted to take into account increases in the consumer price index, was 16.9 per cent. higher in 2003 than in 2002.

In March 2004, the average monthly nominal wage in Kyiv equalled UAH 858.7, an increase of 30.1 per cent. by comparison with the level of March 2003, while the average real wage was 34 per cent. higher than in March 2003. In the last quarter of 2003, the 10 per cent. of the City in the highest income bracket received 5.9 times more income than the 10 per cent. of the population in the lowest income bracket.

The table below sets out the average monthly wages by sub-sector of the City economy for the years indicated:

	1999	2000	2001	2002	2003
	(UAH)				
Sub-sector					
Industry ⁽¹⁾	295	399	533	636	768
Construction	333	460	628	671	816
Trade	409	516	619	741	852
Transport.....	298	414	571	712	816
Communications and post.....	722	949	1,134	1,311	1,488
Financial services.....	921	1,231	2,000	2,089	2,105
Total average monthly wage	303	405	549	643	761

Source: State Committee of Statistics

Note:

(1) Includes machine building and metal working, chemicals and petrochemicals, electric power, food production, production of clothes and shoes, textiles, paper, wood and other processing, manufacturing and related industrial areas.

Unemployment

Employment levels in the City have remained relatively stable over the last five-year period. In the period from 2001 to 2003, the average employment level was approximately 94 per cent. of the City's labour force. In December 2003, the officially registered rate of unemployment in Kyiv was 0.42 per cent. of the economically active population, while according to the International Labour Organisation ("ILO") methodology, the number of unemployed people was 73,860 or 5.1 per cent. The ILO

methodology unemployment rate is the ratio of unemployed persons aged 15-70 to the economically active (i.e. employable) population, whereas the official rate reflects only unemployed persons who have formally registered as such with the relevant City and City district employment centres. Under ILO methodology, the unemployed are defined as persons aged 15 to 70 who (i) are without work, (ii) are seeking work or have tried to establish a business within the most recent four week period and (iii) are available to start working (i.e. to be employed) within the next two week period. The City expects the ILO methodology unemployment rate in the City to decrease slightly from 2001-2003 levels to a level of approximately 5 per cent. in 2004-2005.

The City believes that unemployment remains low in the City and that this is attributable to the high level of investment and development in the City and the high educational levels in the Kyiv labour force.

Gross City Product

Based on preliminary estimates, the GCP of Kyiv was UAH 41.5 billion (US\$7.8 billion) as at 31 December 2003. This represents 17.6 per cent. of the GDP of Ukraine as at 31 December 2003. The City's GCP in actual prices grew at an average rate of 121.4, 106.4 and 110.1 per cent. in 2001, 2002 and 2003, respectively.

Although large industrial businesses remain an important component of GCP, the services sector has grown significantly in recent years. As reflected in the following tables, the percentage of GCP attributable to services has in each year since 2001 exceeded by more than four times the percentage attributable to the industrial sector, demonstrating that services have played the dominant role in Kyiv's economy in recent years. The City expects that the industrial sector will grow at a faster rate than the services sector in the coming years because, due to financial and management difficulties, many large industrial businesses in the City are currently utilising only a small portion of their production capacity and therefore have excess capacity to meet existing demand and additional demand from increased domestic consumption and export opportunities.

The following table sets out Kyiv's annual GCP at current prices by sector expressed as a percentage of total GCP:

	As at 31 December				
	2000	2001	2002	2003 ⁽¹⁾	2004 ⁽²⁾
	(per cent.)				
Sector					
Industrial:					
Industry ⁽³⁾	15.5	13.0	12.9	12.7	12.6
Construction	4.5	4.3	3.6	3.7	3.7
Total industrial	20.0	17.3	16.5	16.4	16.3
Services:					
Transport and telecommunications..	19.0	17.8	15.6	15.4	15.2
Retail, food service, material and technical supply and sales	26.0	27.4	26.3	27.0	27.2
Financial services.....	5.7	7.1	7.7	7.6	7.4
Real estate related services, including leasing, and services to legal entities	12.6	13.9	16.6	16.8	17.0
Other services	16.7	16.5	17.3	16.8	16.9
Total services	80.0	82.7	83.5	83.6	83.7
GCP at current prices	100.0	100.0	100.0	100.0	100.0

Source: State Committee of Statistics

Notes:

- (1) Preliminary data. Not yet approved by the State Committee of Statistics. Based on information from the Programme for Socio-Economic and Cultural Development for 2003.
- (2) Forecast.
- (3) Includes machine building and metal working, chemicals and petrochemicals, electric power, food production, production of clothes and shoes, textiles, paper, wood and other processing, manufacturing and related industrial areas.

Industrial Sector

The industrial sector, which comprises machine building and metal working, chemicals and petrochemicals, electric power, food production, production of clothes and shoes, textiles, paper, wood and other processing, manufacturing and related industrial areas, plays an important role in the economy of Kyiv. There are more than 13,000 industrial businesses operating in the City, with the most important industrial areas being machine building, metal working, food production, electric power and chemicals and petrochemicals. There is a recent and continuing trend in the City's industrial sector towards the manufacturing of a larger proportion of end-products aimed directly at consumers in the domestic market.

Kyiv has the most developed construction industry in Ukraine. The construction industry in Kyiv comprises over 9,120 privately owned, City-owned and State-owned companies, which provide a range of construction services. Aggregate public and private investments in construction in 2003 amounted to UAH 9.9 billion, and the aggregate area of constructed residential property constituted over one million square metres. Approximately 7.5 per cent. of investments in construction in 2003 were financed from the City Budget. The "Kyivmiskbud" holding company is the largest construction enterprise in the City and is 80 per cent. owned by the City. Kyivmiskbud is comprised of more than 60 construction and construction services businesses and had an approximately 35 per cent. share of the Kyiv construction market in 2003. Construction as a percentage of GCP decreased from 4.5 per cent. in 2000 to 3.7 per cent. in 2003 while the industrial sector as a whole (including construction) as a percentage of total GCP decreased from 20.0 per cent. in 2000 to 16.4 per cent. in 2003. This decrease is primarily attributable to the significant growth in the services sector relative to industry, rather than to a decrease in actual levels of construction or other industrial activity. In 2003, the industrial sector in the City employed 379,500 people, or 26.2 per cent. of the employed labour force in Kyiv. See "– Employment and Wages – Composition of Employed Labour Force" above.

Services Sector

Key areas for the City's services sector include transport and telecommunications, retail trade, food service, material and technical supply and procurement, financial services and real estate related services. Kyiv has an extensive transport and communications infrastructure and is a significant transport and communications centre. In addition, Kyiv is the scientific centre of Ukraine and one of the largest scientific centres in Europe. As of 31 December 2003, there were 364 organisations engaged in scientific and engineering activity in Kyiv. The City also has a highly developed network of financial institutions, banks, exchanges, investment funds and insurance companies. Demand for retail services and food services has grown in line with economic development in the City. The services sector as a percentage of GCP increased from 80.0 per cent. in 2000 to 83.6 per cent. in 2003.

Transport and telecommunications as a percentage of GCP decreased from 19.0 per cent. in 2000 to 15.4 per cent. in 2003. In 2003, transport and telecommunications employed 8.7 per cent. of the employed labour force in Kyiv. See "–Employment and Wages – Composition of Employed Labour Force" above.

Retail, food service, material and technical supply and sales as a percentage of GCP increased from 26.0 per cent. in 2000 to 27.0 per cent. in 2003. Retail, food service, material and technical supply and sales employed 19.6 per cent. of the employed labour force in Kyiv in 2003.

Financial services include finance, lending, insurance and pensions. Financial services have been relatively stable as a percentage of GCP since 2000 and represented 7.6 per cent. of GCP in 2003. Financial services employed 3.8 per cent. of the employed labour force in Kyiv in 2003.

Real estate related services, including leasing, and services to legal entities as a percentage of GCP increased from 12.6 per cent. in 2000 to 16.8 per cent. in 2003. Real estate related services, including leasing, and services to legal entities employed 14.6 per cent. of the employed labour force in Kyiv in 2003.

Recent Rising Price of Oil

The recent increases in the price of oil have led to increases in the costs of operating the City's public transport system. Notwithstanding such increases, the City has not yet increased the price of public transport. The City is considering increasing passenger fares but the timing of any such decision involves political considerations and it is not certain when such increase will take effect.

Privatisation

The privatisation programme in Ukraine, including that in Kyiv, was launched in 1992. The privatisation programme in Ukraine is administered by the State Property Fund, which, in consultation with certain other State ministries, identifies the objects to be privatised each year. Local authorities are responsible for the privatisation of assets owned by the relevant municipalities and residential property. Under applicable privatisation laws and policies, businesses in certain strategic sectors such as military, power generation and certain mining areas are specifically excluded from the privatisation programme and may only be privatised with the approval of Parliament.

The Kyiv privatisation programme, adopted by the City Council in 1999, provides for the sale to individuals and legal entities of ownership interests in, or outright sale of, objects including businesses, real estate interests, housing assets and uncompleted construction projects. The City privatised 7,166 objects between 1992 and the end of 2003, including 513 in 2001, 554 in 2002 and 821 in 2003. The sale of shares by the City in a privatisation is conducted exclusively by way of an independent valuation of the shares and a public competitive tender. The City's receipts from privatisation are typically not material in the context of the City Budget. See "City Budget and Financial Information – Budget Revenues". The City received revenues from privatisation in the amounts of UAH 62.9 million in 1999, UAH 106.0 million in 2000, UAH 156.4 million in 2001 UAH 194.7 million in 2002 and UAH 272.2 million in 2003 and expects to receive UAH 219.9 million in 2004. During the first three months of 2004, the City collected UAH 81.1 million from privatisation.

The main objectives of the Kyiv privatisation programme are (i) the generation of funds to the City Budget to be allocated to the City's investment programmes and (ii) the creation of a more effective system of management of privatised companies.

The City has decided to retain a significant shareholding in certain privatised companies. The City has the following policy in respect of companies in which it has a shareholding: (i) in companies in which the City holds more than 50 per cent. plus one share, the City will sell such number of shares that reduces its holding to 50 per cent. plus one share (this policy applies to companies such as Kyivmlyn, Kyivhlib and Kyivvodokanal); (ii) in companies in which the City holds less than 50 per cent. plus one share, the City will retain such shares; and (iii) businesses that are wholly-owned by the City will be transformed into joint stock companies and shareholdings in an amount of 50 per cent. minus one share will be sold. Even under this policy, the City continues to have a more significant involvement in what is often seen in the West as the private sector.

The basic principles of privatisation in Kyiv are provided in the Laws of Ukraine "On the Privatisation of State Property" and "On the Privatisation of Small State Businesses (Small Privatisation)". The Kyiv City State Administration, in its capacity as the executive body of the City Council, carries out the function of managing the assets owned by the City, such as acting as a shareholder in joint stock companies, and is also responsible for making decisions on the privatisation of particular property.

In 2004, the City intends to sell 29 per cent. less one share in the capital of State Public Utility Gas Supply Enterprise "Kyivgas", retaining a shareholding of 60 per cent. plus one share, and 25.5 per cent. in Open Joint Stock Company JSC Kyivvodokanal, retaining a shareholding 67 per cent.

See "City Budget and Financial Information – Assets of the City – Share Ownership".

Litigation

The City has been involved in litigation with a state-owned company, Ukrainian State Innovation Company ("USIC"), in connection with a claim by USIC against the City for payment of a debt in the amount of UAH 5.4 million. On 11 May 2004, the Kyiv City Commercial Court ordered the City to make payment to USIC in the amount of UAH 5.4 million in satisfaction of USIC's claim. The City intends to comply with the court order if it is unable to reach a settlement with USIC before the date on which it is required to make payment.

CITY BUDGET AND FINANCIAL INFORMATION

City Budgetary System

The budgetary system of Ukraine is comprised of the State Budget and local budgets. Local budgets include the budgets of oblasts, villages, regions, cities, districts and the Autonomous Republic of Crimea. The City Budget is a relatively independent budgetary system within the budget system of Ukraine.

Revenue of the City Budget is created by taxes, non-tax revenues and other receipts. Expenditure is divided into eight main items. Each of them is a focal point of the activity of the Kyiv City State Administration. In addition, there are separate expenditure items for funds transferred to the State Budget and subsidies from the City Budget to other local budgets.

The foundation of the City's budgetary system is the Budget Code, which requires that each of the State Budget and local budgets be divided into the two categories of general funds and special funds. Special funds include budget assignments for expenditure for a specifically designated purpose. General funds include all budget revenues other than those assigned to special funds. The sources of formation of general funds and special funds in each of the State Budget and the local budgets for a particular budget year are determined by the Law of Ukraine "On the State Budget of Ukraine" (the "State Budget Law") for that budget year. The City Council may establish a special fund only on the basis of the State Budget Law. Expenditures from special funds may only be made within the limits of the revenues allocated to the corresponding purpose.

City District Budgets

The City districts have been established by the City Council. The City district budgets are approved on an annual basis by City district councils in accordance with budget assignments from the City Council. (See "The City of Kyiv – Administrative Districts of the City" for a description of the organisational and administrative structure of the districts.) The City Council determines and approves budget assignment items and their scope for each particular year based on a consideration of the overall interests of the City and the specific needs of particular districts.

The City Council determines what part of revenues will be allocated to the City Budget and what part will be allocated to City district budgets, and the City Council determines the composition of revenues and expenditures of the City district budgets. Assignments of revenues from the City Budget to City district budgets are allocated either to the general fund or a special fund of such City district budgets. According to the 2004 City Budget Law, the City district budgets are entitled to allocate the following revenues to their special funds: (i) revenues of institutions and organisations financed from the relevant City district budget; (ii) revenues allocated to Purpose Funds established by the City's district councils; and (iii) revenues from the privatisation of the City-owned businesses and property within the relevant district. All of the remaining assignments from the City Budget are accrued to the general fund of the City district budgets. The 2004 City Budget Resolution refers to the following major allocations to the general funds of the City district budgets, among others: (i) a portion of personal income tax (19.8 per cent. of total income revenues of the City Budget) and of land tax (38.8 per cent of the total land tax revenues of the City Budget); (ii) charges for the issuance of licenses and certificates by the district authorities; (iii) State registration fees; (iv) rent payments with respect to City-owned property holdings and 50 per cent. of rent payments for other property owned by territorial communities of City districts; (v) local taxes and duties (other than municipal and market taxes, which are paid by City-owned businesses); (vi) payments for special use of natural resources; (vii) corporate income tax paid by City-owned businesses under the jurisdiction of the relevant district's tax authorities; (viii) the single tax on entrepreneurial activity and (ix) the home-craft tax.

Budgetary Relations between the State and Local Governments

The Budget Code governs the balance between the State Budget and local budgets and regulates payments from and to donor and recipient regions. According to the Budget Code, the State is responsible for all expenditures that have a national scope, such as defence, while local governments manage a significant portion of expenditure in the social sectors. Cities are responsible for providing local services, such as basic health and sanitation. The Budget Code also authorises the State to delegate to local governments the authority to undertake State public administration activities.

The Budget Code gives local governments the right to keep revenue from a variety of sources, including full entitlement to land tax and corporate income tax from communally owned businesses. Another important revenue source for local budgets is personal income tax. The Budget Code provides that revenues from certain Ukrainian national taxes collected within the jurisdiction of a

local government are either divided between the State Budget and the local budget or are retained in full by the local budget.

In addition, the State provides additional revenues to local governments in the form of inter-budgetary transfers from the State Budget to local budgets. The Budget Code envisages inter-budgetary transfers in the form of “levelling grants” and various designated purpose subsidies. Levelling grants are a feature of the budget system of Ukraine whereby the State grants funds to the budgets of certain regions and cities of Ukraine whose expected revenues are insufficient to fund necessary expenditures in the relevant budget year. Subsidies from the State Budget are paid directly to a local budget for a specific designated purpose and with predetermined terms and conditions of use.

During each of 2000, 2001 and 2002, Ukrainian taxes collected under the jurisdiction of the City accounted for approximately 20 per cent. of the total tax revenue of Ukraine and they accounted for around 30 per cent. in 2003. The State finances specific social and economic programmes of the City within the framework of the State Programme of Social and Economic Development of the City of Kyiv for the period ending 2010, approved by the Cabinet of Ministers of Ukraine on 15 December 1997 (the “Development Programme”). Prior to 2002, the State spent UAH 165.9 million on the implementation of the Development Programme. In particular, the State financed the construction and commissioning of various metro stations in the City, the construction of digital telephone systems and housing construction, among other things. Many of these programmes are funded directly by the State, in which case funds for these programmes do not pass through the City Budget. The State spent UAH 14.6 million in 2003 on implementation of the Development Programme.

The Law on the Capital provides that the State should finance all expenditures in connection with the City’s role as the capital of Ukraine in amounts specified in the State Budget for the relevant year and that the City Budget is also entitled to receive a subsidy for the performance of its role as the capital of Ukraine in an amount not less than 50 per cent. of the total tax revenues collected in the territory of the City. The City Budget has been awarded such a subsidy under the 2001 State Budget Law in an amount of UAH 150 million and under the 2004 State Budget Law (as amended) in an amount of UAH 55 million. The Budget Code, which was adopted after the Law on the Capital came into force, provides that subsidies to which the City is entitled should be targeted to specific expenditure items in the City Budget. The City received such targeted subsidies in 2002 and 2003, and the 2004 City Budget also provides for such targeted subsidies.

The Law on the Capital provides that decisions of the State that impose additional expenditures on the City must be accompanied by a transfer of financial resources to the City to enable it to implement such decisions. In practice, when the City loses revenues as a result of a new law being passed by the State, the City is permitted to reduce the amounts of transfers it makes to the State Budget in amounts equal to the amount of such loss of revenues. The Budget Code provides that the granting by the State of any tax privileges that decrease the revenues of local budgets should be accompanied by amendments to the State Budget Law providing for subsidies to the relevant local budgets in order to compensate them for the loss of revenues. See “– Budget Revenues – Tax Revenues” below.

Any change in Ukrainian legislation affecting the division of tax revenues between the State and local governments or the level of State funding for social and economic programmes in the City may have an adverse effect on the financial resources of the City. See “Risk Factors – Risks Associated with the City – The division of tax revenues with the State may not favour the City, thereby making it more difficult for the City to repay the Loan”.

Overview of Ukrainian Legislative Process

The source of national legislation is the Verkhovna Rada of Ukraine, the Ukrainian Parliament. The Parliament adopts “Laws of Ukraine”, which have the highest authority in the hierarchy of Ukrainian laws after the Constitution itself. The President, deputies of Parliament, the Cabinet of Ministers and the NBU each has the right to initiate legislation. The President also has the power to veto Parliamentary bills (this veto may in turn be overridden by Parliament). In addition, the President is authorised to initiate extraordinary sessions of Parliament and, under certain circumstances, may subject Parliament to early termination. At the same time, the Parliament has the ability to dismiss the President under an impeachment procedure. See “Ukraine – Political Structure and Recent Developments”.

The Ukrainian Parliament continues to implement ongoing tax legislation reform in Ukraine through the development of new tax legislation and by amending the existing tax laws, which may affect the amount of revenues received by the City Budget. See “Risk Factors – Risks Associated with the City

– The division of tax revenues with the State may not favour the City, thereby making it more difficult for the City to repay the Loan”. No assurance can be given that a change in the composition of Parliament, a new President or both will not result in legislation that will have an adverse effect on the City’s financial resources.

Budget Principles

The budget system in Ukraine is based on the following budgetary principles:

- Unity – Budgets exist within a uniform legal framework, a single monetary system and uniform budget regulation, with one system of budget classification and a uniform procedure for budget implementation and accounting and book-keeping.
- Balance – Expenditures from the budget must correspond to the volume of revenues to be received in the relevant budget period.
- Independence – Local budgets are independent and do not bear responsibility for the budgetary obligations of each other or of the State and vice versa. Local budgets have independent sources of revenues, and local governments approve their own local budgets and determine their own expenditures.
- Wholeness – All revenues and expenditures carried out by local government bodies must be included in the budget.
- Reasonableness – The budget is formed on the basis of realistic macro-indices of economic and social development and calculations of revenues and expenditures based on approved methods and rules.
- Efficiency – All participants in the budget process must aim to achieve scheduled goals while using budget funds in the most efficient manner possible.
- Consumer-proximity – The allocation of expenditures between the State Budget and local budgets must be based on the maximum proximity of public services to the ultimate consumer.
- Purpose – Budgetary funds must be used only for their purposes as set out in the budget.
- Transparency – Local budgets are approved and implemented by the relevant council (in Kyiv, the City Council).
- Responsibility – Each participant in the budgetary process is responsible for its own actions or failure to act at each stage of the budget process.

Budget Process

The City budget process is regulated by the Budget Code and by relevant legislation and resolutions of the City Council adopted pursuant to the Budget Code. The Budget Code came into force on 24 July 2001 and substantially revised and modernised the system of budgetary regulation in Ukraine.

The City budget process consists of the following phases:

- preparation of a draft City Budget by the Kyiv City State Administration;
- consideration and approval of the draft City Budget by resolutions of the City Council;
- implementation of the City Budget, including amendments being made to the relevant City Budget Resolution; and
- preparation and consideration of the report on the implementation of the City Budget and making decisions regarding such report.

The City budget process commences with the provision by the Ministry of Finance of Ukraine (the “Ministry of Finance”) to the Kyiv City State Administration of guidelines for conducting the calculations for a draft budget for the following budget year. The Kyiv City State Administration submits to the Ministry of Finance information necessary for the determination of amounts of inter-budgetary transfers and other relevant indices. The Main Financial Office instructs the main recipients of City Budget funds on the preparation of substantiated proposals on the budget funds needed for their activities for the following budget year. Based on an analysis of the submitted proposals, the Head of the Main Financial Office determines which proposals to include in the draft budget to be submitted for the consideration of the Kyiv City State Administration. The district state administrations also submit proposals for the draft budget to the Main Financial Office. Upon the approval by the Cabinet of Ministers of Ukraine of the draft State Budget Law, the Ministry of Finance informs the Kyiv City State Administration on the calculations of forecasted inter-budgetary transfers, methods of their determination and other indices relevant for the preparation of the draft

City Budget. After the approval of the draft State Budget Law in the second reading, the Cabinet of Ministers of Ukraine provides the Kyiv City State Administration with information on the estimated amounts of inter-budgetary transfers to be voted on by Parliament. Based on the foregoing information, the Kyiv City State Administration prepares a draft resolution on the City Budget.

The draft resolution on the City Budget must be approved by the Kyiv City State Administration before it is submitted to the City Council. The City Council by its resolution approves the City Budget for the following budget year not later than two weeks after the official publication of the State Budget Law. When approving the City Budget, the City Council must take into account the amounts of inter-budgetary transfers and other financial information relevant to the City Budget approved by the Parliament in the draft State Budget Law adopted in the second reading. In the event that the resolution on the City Budget is not approved by the City Council by 31 December of the year prior to the budget year, the Kyiv City State Administration is authorised to incur expenditures for purposes determined in the resolution on the City Budget for the previous budget year, subject to certain conditions and limitations. The last year in which this occurred was 1999, when the budget for the year 1999 was approved on 30 March 1999.

The resolution on the City Budget sets forth, among other things, the following:

- the total amount of revenues and expenditures (with allocation between the general and special funds);
- the maximum amount of budget deficit permissible in the City Budget for the relevant budget year, the maximum amount of indebtedness the City may incur during the relevant budget year and the authority of the City to grant guarantees and the amounts of such guarantees;
- the amounts of budget funds allocated to the main City Budget fund recipients;
- the classification of budget revenues;
- amounts of inter-budgetary transfers; and
- additional provisions regulating the budget implementation process.

Budget Implementation

Prior to July 2001, the City Budget was implemented pursuant to the Law on the Budgetary System of Ukraine, dated 5 December 1990, whereby City Budget funds were collected and distributed through authorised non-governmental commercial banks which maintained accounts of various recipients of City Budget funds. Since the entry into force of the relevant articles of the Budget Code on 24 July 2001, funds are collected and distributed by the City Department of the State Treasury of Ukraine (the “City Treasury”). The City Treasury implementation system provides for the consolidation of all of the City’s financial resources in accounts opened by the recipients of the City Budget funds with the City Treasury and envisages the opening of a separate budgetary account for each City Budget item. The City Treasury may also open non-budgetary accounts for the recipients of City Budget funds for transactions other than transactions connected to the implementation of the City Budget.

The Main Financial Office continues to be responsible for the general management and coordination of the implementation of the City Budget.

Recipients of City Budget funds submit their financial reports to the territorial departments of the State Treasury of Ukraine on terms and in the form prescribed by the State Treasury of Ukraine.

The City Treasury prepares and provides the Main Financial Office with monthly, quarterly and annual reports on the implementation of the City Budget on terms and in the form prescribed by the State Treasury of Ukraine and approved by the Ministry of Finance and the State Audit Chamber. Based on the submitted reports, the Main Financial Office provides the City Council with information on the status of implementation of the City Budget. In addition, the Main Financial Office prepares and submits quarterly and annual reports on the implementation of the City Budget for the review of the City Budget Commission within two months of the end of each quarter and year. The annual reports on the implementation of the City Budget are subject to approval by the City Council. After such approval, the City Budget Commission selects, by way of a tender, an independent auditing firm to carry out an audit of the financial accounts of the City related to the use of budget funds in the relevant budget year. Based on the results of such audit, the Main Financial Office submits, for the consideration of the City Budget Commission, suggestions for addressing deficiencies in the implementation of the City Budget for the previous year when implementing the City Budget in the following budget year.

The implementation of the City Budget is monitored by the City Budget Commission, and the Main Financial Office is responsible for ensuring that the City Budget complies with applicable Ukrainian budget legislation. In addition, the State Control and Audit Service of Ukraine monitors the legality and efficiency in the use of the City Budget funds and the authenticity of the reports on the implementation of the City Budget. The Kyiv Control and Audit Department is authorised to carry out inspections and audits of the City bodies as well as businesses, organisations and institutions funded from the City Budget and is authorised to suspend any transactions involving City Budget funds and budgetary appropriations and to reduce the appropriations due to recipients of City Budget funds.

Introduction to the City Budget

The principal sources of revenue for the City are: (i) taxes and fees (including City taxes and fees and the proportion of Ukrainian taxes and fees allocated to the City budget) and (ii) revenues from the use or sale of municipal property and income from investments in various businesses.

The City Budget is an itemised summary of expected revenue and expenditure, which in recent years has become increasingly detailed. The revenue base of the City Budget is estimated by taking into account the expected tax, non-tax and other revenues for the current year and forecasts of economic development in the City, such as forecasts of the employment level, the development of the taxable base and wholesale price indices within the City. Expenditure is estimated according to expected revenues and the planned social and economic programmes of the City.

The following table sets out revenues and expenditures of the City Budget for the years ended 31 December 2000, 2001, 2002 and 2003 and budgeted revenues and expenditures for the year ending 31 December 2004:

	Year ended 31 December				
	2000	2001	2002	2003	2004 ⁽¹⁾
	(UAH millions)				
Revenues:					
Tax revenues	3,155.3	3,977.4	3,739.3	3,303.2	3,050.2
Non-tax revenues	259.5	340.2	188.3	258.8	247.1
Revenues from Capital Transactions.....	0	21.6	220.7	421.9	419.9
Purpose Funds	106.6	286.0	100.4	262.9	321.7
Grants and subsidies from the State					
Budget.....	4.4	336.0	236.6	336.5	437.1
Transfer of funds from deposits	—	—	—	—	252.0
Total City revenues	3,525.8	4,961.2	4,485.3	4,583.3	4,728.0
Expenditures:					
Budget expenditures.....	2,219.2	2,855.2	2,703.4	3,817.0	5,382.0
Funds transferred to the State Budget ..	1,235.4	2,201.7	1,713.5	903.2	563.8
Total City expenditure	3,454.6	5,056.9	4,416.9	4,720.2	5,945.8
Surplus (deficit)⁽²⁾⁽³⁾	71.2	(95.7)	68.4	(136.9)	(1,217.8)

Source: Kyiv City State Administration, Main Financial Office

Notes:

- (1) Figures reflect the planned City Budget as approved by the City Council, not the results of implementation.
- (2) The deficit for 2001 reflects reserves from the 2000 budget year being used to make additional expenditures beyond revenues in the 2001 budget year. The deficit for 2003 and the deficit budgeted for 2004 principally reflect borrowings being made in the relevant budget year to finance expenditures in excess of revenues. The general fund of the City Budget, which constitutes 80% of the overall City Budget, had a surplus of UAH 148.2 million in 2003.
- (3) Any surplus in a given budget year is carried over into the corresponding budget category for the following year.

Non-Budgetary Funds

Prior to enactment of the Budget Code, pursuant to the Law on the Budgetary System of Ukraine, dated 5 December 1990, and the Law on Local Self-Government, the City was authorised to establish and operate an unlimited number of non-budgetary funds (“NBFs”) from various off-budgetary sources to be determined by the City Council including, among others: (i) fines for the violation of

consumers' rights; (ii) bank interest on the use of temporarily available off-budgetary funds; (iii) voluntary contributions of businesses, organisations, institutions and citizens; (iv) payments for the placement of advertisements; (v) payments for the right to rent non-residential premises; and (vi) proceeds from non-agricultural land auctions. The 2000 State Budget Law required the City to re-classify the NBFs into special funds of the City Budget. Since the enactment of the Budget Code, the City is prohibited from establishing NBFs but is permitted to continue to establish purpose funds ("Purpose Funds"), which are part of the City Budget. See "– Budget Revenues – Purpose Fund Revenues" and "– Budget Expenditures – Purpose Fund Expenditures" below.

Sources of NBFs established in the 2000 and 2001 City Budgets included:

- proceeds from investors' contributions made in the development of the City's infrastructure;
- payments for obtaining the right to place advertisements;
- rent receipts on City-owned non-residential property;
- proceeds from the sale of land lease rights and non-agricultural land; and
- registration fees for foreign investments.

Funds received from the foregoing NBFs were used for, among other purposes, capital expenditures (including reconstruction and development works) and expenses in connection with land reform such as inventory and expert evaluation of land.

In 1999, 2000 and 2001, revenues from NBFs were UAH 21.7 million, UAH 82.1 million and UAH 281.0 million, respectively. In 2002 and 2003, revenues from Purpose Funds were UAH 100.4 million and UAH 262.9 million, respectively. The planned revenues from Purpose Funds for 2004 as approved by the City Council are UAH 321.7 million.

Budget Revenues

The City categorises its Budget revenue into five main groups: (i) tax revenues; (ii) non-tax revenues; (iii) revenues from capital transactions; (iv) Purpose Fund revenues; and (v) grants and subsidies from the State Budget. In 2004, the Budget contains an additional category (transfer of funds from deposits) which comprises part of the unused U.S. dollar proceeds from the offering of notes in 2003 which had been deposited in a U.S. dollar bank account by the City in 2003 and converted into UAH and transferred to the City's UAH account with the Treasury in 2004.

The following are the revenues of the Budget for the years ended 31 December 2000, 2001, 2002 and 2003 and budgeted revenues for the year ending 31 December 2004:

	2000		2001		2002		2003		2004 ⁽¹⁾	
	UAH millions	per cent.	UAH millions	per cent.						
Revenues										
Tax revenues:										
Income taxes	2,741	77.6	3,463.3	69.8	3,162.5	70.5	2,611.5	57.0	2,334.1	49.4
Property taxes	43.9	1.3	43.9	0.9	47.0	1.0	48.1	1.1	46.5	1.0
Fees for use of natural resources..	207.7	5.9	259.0	5.2	276.0	6.2	324.0	7.1	340.1	7.2
Internal tax on commodities and services.....	68.4	1.9	60.1	1.2	75.6	1.7	92.3	2.0	121.5	2.6
Other taxes.....	99.4	2.8	151.0	3.0	178.2	4.0	227.3	5.4	208.0	4.4
Total tax revenues	3,155.3	89.5	3,977.4	80.1	3,739.3	83.4	3,303.2	72.2	3,050.2	64.5
Non-tax revenues	259.5	7.4	340.2	6.9	188.3	4.2	258.8	5.6	247.1	5.2
Revenues from capital transactions	0	0	21.6	0.4	220.7	4.9	421.9	9.2	419.9	8.9
Purpose Fund revenues	106.6	3.0	286.0	5.8	100.4	2.2	262.9	5.7	321.7	6.8
Grants and subsidies from the State										
Budget.....	4.4	0.1	336.0	6.8	236.6	5.3	336.5	7.3	437.1	9.2
Transfer of funds from deposits	—	—	—	—	—	—	—	—	252.0	5.4
Total revenues	3,525.8	100	4,961.2	100	4,485.3	100	4,583.3	100	4,728.0	100

Source: Kyiv City State Administration, Main Financial Office

Note:

(1) Figures reflect the planned City Budget as approved by the City Council, not the results of implementation.

Tax Revenues

Tax revenues are divided into five main items: (i) income taxes, (ii) property taxes, (iii) fees for use of natural resources, (iv) internal taxes on commodities and services and (v) other taxes.

Income Taxes

Income taxes comprise personal income tax and corporate income tax.

Prior to 1 January 2004, Ukrainian residents were taxed on their aggregate worldwide income at progressive rates of between 10 and 40 per cent. Income derived by Ukrainian residents from a source other than the taxpayer's principal place of employment, as well as Ukrainian-source income of a non-resident, were taxed at a flat rate of 20 per cent. Any individual who is physically present in Ukraine for more than 183 calendar days in a calendar year, is deemed a Ukrainian resident for personal income taxation purposes. Revenues from personal income tax are fully retained by, and are an important revenue base for, the City Budget. Personal income tax revenues of the City Budget amounted to UAH 214.8 million in 1999, UAH 1.23 billion in 2000, UAH 1.65 billion in 2001 and UAH 2.04 billion in 2002. In 2003, the City collected UAH 2.57 billion in personal income taxes.

Under the Personal Income Tax Law which entered into effect on 1 January 2004, the progressive rates previously in effect were replaced by a new flat rate tax of 13 per cent. (to be increased to 15 per cent. from 1 January 2007). The City expects to experience budget revenue losses as a result of the introduction of this new flat-rate tax because it will result in the pool of income tax revenue to be divided between the City and the State being smaller than under previous income tax rates. Under the 2004 City Budget, the City expects to collect UAH 2.3 billion in personal income taxes.

The City anticipates that certain factors will mitigate the potential adverse effect of the flat-rate income tax on the City Budget, including the 2004 City Budget. For example, the Budget Code provides that the granting by the State of any tax privileges that decrease the revenues of local budgets should be accompanied by amendments to the State Budget Law providing for subsidies to the relevant local budgets in order to compensate them for the loss of revenues. Moreover, the 2004 State Budget Law provides that the State will compensate the City for any shortfall in revenues. See “– Budget Expenditures – Funds Transferred to the State Budget”. The Cabinet of Ministers of Ukraine has approved the procedure for the compensation of local budgets for losses which may be incurred as a result of the introduction of the Personal Income Tax Law. See “– City Budgetary System – Budgetary Relations between the State and Local Governments” and “Risk Factors – Risks Associated with the City – The new flat-rate income tax in Ukraine may have a material adverse effect on the City's revenues and thus on its ability to repay its debts, including the Loan”. In addition, the City expects that tax evasion will be reduced as a result of the lower tax rates under the Personal Income Tax Law, which will mitigate the loss of personal income tax revenues.

Corporate income tax is levied on (i) Ukrainian business entities, (ii) non-resident individuals, legal entities and permanent establishments of non-residents that derive profits from Ukrainian sources and (iii) branches, divisions, and other separate units of Ukrainian business entities and non-resident entities that are located in a territorial community other than the territorial community of their parent entity and that are not legal entities. Prior to 1 January 2004, the basic corporate income tax rate was 30 per cent., but this was reduced to 25 per cent. with effect from 1 January 2004. In 2001, 100 per cent. of corporate income tax revenues accrued to the City Budget, and in 2002 only 50 per cent. of such revenues accrued to the City Budget. Under the 2003 State Budget Law and the 2004 State Budget Law, the City Budget is permitted to retain corporate income tax revenues only from City-owned businesses, while the majority of corporate income tax revenues is allocated to the State Budget.

Revenues from corporate income tax were UAH 774.5 million, UAH 1.51 billion, UAH 1.81 billion and UAH 1.12 billion in 1999, 2000, 2001 and 2002, respectively. The decrease from 2001 to 2002 was due primarily to the change in 2002 in the principles relating to the allocation of corporate income tax revenues between the City and the State described in the preceding paragraph. In 2003, the City collected UAH 46.5 million in corporate income tax. Under the 2004 City Budget, the City expects to collect UAH 29.8 million in corporate income tax. The decrease from 2002 to 2003 was due primarily to the change in 2003 providing that the City Budget may only retain corporate income tax revenues from City-owned businesses. Corresponding to the decreases in corporate income tax revenues from 2001 to 2002, from 2002 to 2003 and from 2003 to 2004 are decreases in the amounts of funds transferred from the City Budget to the State Budget between those respective years. See “– Budget Expenditures – Funds Transferred to the State Budget”.

Taxes on Vehicle Ownership

Taxes on vehicle ownership are applicable to vehicles that are registered in the City and are paid at different rates depending on the type of vehicle. The City's revenues from such vehicle ownership taxes amounted to UAH 25.4 million in 1999, UAH 43.9 million in 2000, UAH 43.9 million in 2001

and UAH 47.0 million in 2002. In 2003, the City collected UAH 48.1 million in vehicle ownership tax. According to the 2004 City Budget, the City is expected to collect UAH 46.5 million in vehicle ownership tax in 2004. Revenues from taxes on vehicle ownership increased from 1999 to 2000 and from 2001 to 2003 mainly due to increases in levels of vehicle ownership but were static from 2000 to 2001 due to variations in payment periods.

Fees for Use of Natural Resources

Fees for use of natural resources are comprised largely of land tax. Land tax is paid by private owners of land at different rates depending on the value and location of the land. The City Budget is permitted to retain 100 per cent. of the collected land tax, which constitutes a significant share of its revenue base. Land tax revenues of the City Budget amounted to UAH 126.6 million in 1999, UAH 205.2 million in 2000, UAH 259.0 million in 2001 and UAH 275.8 million in 2002. In 2003, the City collected UAH 323.8 million in land taxes. The increase in revenues over the period from 1999 to 2003 is principally attributable to the increase in the rate of land tax during that period. According to the 2004 City Budget, the City expects to collect UAH 340.0 million in land taxes in 2004.

Internal Taxes on Commodities and Services

Internal taxes on commodities and services include charges for licences on certain types of business and economic activity, such as the sale of petroleum products. Revenues from internal taxes on commodities and services amounted to UAH 98.6 million in 1999, UAH 68.4 million in 2000, UAH 60.1 million in 2001 and UAH 75.6 million in 2002. In 2003, the City collected UAH 92.3 million in internal taxes on commodities and services. The decrease in revenues from 1999 to 2001 is principally attributable to the number of taxpayers electing to pay the fixed tax on small businesses during those years, which resulted in those taxpayers no longer being liable to pay for certain categories of business licence (see “– Other Taxes” below), while the increase in revenues from 2001 to 2003 is principally attributable to the general increase in business and economic activity during those years. According to the 2004 City Budget, the City expects to collect UAH 121.5 million in internal taxes on commodities and services in 2004.

Other Taxes

Other taxes include local taxes, fixed taxes on small businesses, fixed agricultural taxes, tax violation penalties and certain other taxes. Revenues from other taxes were UAH 62.9 million, UAH 99.4 million, UAH 151.0 million and UAH 178.2 million in 1999, 2000, 2001 and 2002, respectively, and UAH 227.3 million in 2003. Under the 2004 City budget, the City expects revenues from other taxes of UAH 208.1 million in 2004.

Local taxes are those taxes which the City has discretion to levy (from a range of taxes determined by the State and subject to maximum rates set by the State). Local taxes comprise, among others, (i) advertisement taxes, (ii) communal (payroll) taxes, (iii) market charges, (iv) automobile parking duties and (v) hotel taxes (prior to 2004). Revenues from local taxes amounted to UAH 51.0 million in 1999, UAH 67.9 million in 2000, UAH 76.8 million in 2001, UAH 81.7 million in 2002 and UAH 93.7 million in 2003. Under the 2004 City Budget, the City expects to collect UAH 61.3 million in local taxes in 2004. The increase in revenues over the years from 1999 to 2003 is principally attributable to the increase in the rate of hotel taxes during that period, and the expected decrease from 2003 to 2004 is mainly due to the abolition of the hotel tax in 2003.

The fixed tax on small businesses is a fixed tax that small businesses may elect to pay in lieu of corporate or personal income tax if they meet certain criteria related to the amount of their profits. Revenues from the fixed tax on small businesses amounted to UAH 4.9 million in 1999, UAH 25.5 million in 2000, UAH 71.4 million in 2001, UAH 96.4 million in 2002 and UAH 133.4 million in 2003. The increases in revenues from the fixed tax on small businesses from 2000 to 2003 are attributable to more small businesses electing to pay this tax instead of corporate and personal income taxes and to increased small business activity over the relevant years. Under the 2004 City Budget, the City expects to collect UAH 146.8 million in fixed tax on small businesses in 2004.

Value-Added Tax

The Law of Ukraine “On Value-Added Tax” (the “VAT Law”) provides for the taxation of import and sales transactions in the territory of Ukraine at a 20 per cent. rate, which is charged on and over the contractual value of the relevant goods or services, which value includes any excise tax, import duty and other taxes or payments required under the applicable Ukrainian legislation. A zero per cent. tax rate is provided by the VAT Law for the export of goods and the provision or rendering of

works or services that are consumed outside of the customs territory of Ukraine. Under the draft 2005 budget resolution, it is proposed to introduce a VAT rate of 17 per cent. with effect from 1 January 2005. Since VAT is considered to serve an important macro-economic stabilisation function, all VAT revenues are allocated to the State Budget. The City Budget receives no revenues from VAT.

Tax Collection

The State Tax Administration of the City of Kyiv (the “Kyiv Tax Administration”) is responsible for the full and timely collection of taxes and other levies to the City Budget. The Kyiv Tax Administration reports to the State Tax Administration of Ukraine and supervises ten district Tax Inspectorates (“Tax Inspectorates”), which are responsible for the direct control over full and timely collection of taxes and other levies in the respective districts of the City. In addition to the foregoing tax authorities, the Kyiv City Tax Police Department, through a network of branches in the districts of the City (collectively, the “Tax Police”), is responsible for the prevention and elimination of tax law violations.

All taxpayers, whether legal entities or individuals, are required to register with the relevant Tax Inspectorate and Tax Police, to submit their tax returns and to make payments of taxes and other levies as provided by the applicable tax legislation of Ukraine. Upon registration by the taxpayer, the relevant Tax Inspectorate enters, and further maintains, records with respect to each individual taxpayer into the State Register of Individual Taxpayers and, with respect to each legal entity taxpayer, to the Unified Data Bank on Taxpayers which are Legal Entities and the Register of VAT payers.

On 1 April 2001, the Law of Ukraine “On the Procedure for the Discharge of Taxpayers’ Obligations to Budgets and State Special Purpose Funds” (the “Tax Arrears Law”) came into effect. Under the Tax Arrears Law, in the event of untimely or inadequate discharge of its tax obligations, a taxpayer is required to pay taxes in arrears in an amount agreed with the relevant Tax Inspectorate as well as fines and penalties. The Tax Arrears Law requires that a court order be obtained in order for the Tax Inspectorate to collect taxes in arrears. However, Tax Inspectorates may enforce a tax pledge over the assets of taxpayers in arrears. The Tax Arrears Law also provides a procedure for writing off taxes in arrears. This is in contrast to the previously existing mechanism whereby Tax Inspectorates would compile and maintain a register of tax violators. Pursuant to the Tax Arrears Law, the total amount of taxes outstanding as of 31 December 1999, and unpaid as of 21 February 2001, were written off. From 21 February 2001, the Tax Inspectorates write off “bad tax arrears” on a quarterly basis under a procedure agreed between the relevant Tax Inspectorate and the Ministry of Finance.

As at 31 December 2003, the City had an aggregate of UAH 40.3 million of tax revenues outstanding and unpaid to the City as compared with UAH 33.8 million as at 31 December 2002 and UAH 44.9 million at 31 December 2001. The largest component of these amounts are land taxes in arrears in an amount of UAH 23.5 million as at 31 December 2003.

Non-tax Revenues

Non-tax revenues are divided into five main items: (i) dividends from City shareholdings and interest on short-term bank deposits, (ii) administrative fees and rent from City-owned properties, (iii) administrative fines, (iv) revenues of medical, educational and other institutions funded by the City Budget and (v) other non-tax revenues. The majority of non-tax revenues accrue to special funds of the City Budget. Non-tax revenues accounted for approximately 4.2 per cent. of total revenues in 2002 and 5.6 per cent. of total revenues in 2003. Non-tax revenues are expected to account for approximately 5.2 per cent. of total revenues in 2004.

Total non-tax revenues of the City amounted to UAH 259.5 million in 2000, UAH 340.2 million in 2001, UAH 188.3 million in 2002 and UAH 258.8 million in 2003 and are budgeted to amount to UAH 247.1 million in 2004. The large decrease in non-tax revenues from 2001 to 2002 is due primarily to the fact that in 2002 there was a change in the principles relating to the treatment of privatisation revenues. Prior to 2002 they were allocated to non-tax revenues, and beginning in 2002 they have been allocated to revenues from capital transactions. In addition, prior to the approval of the Budget Code in mid-2001, the City received other non-tax revenues from interest on temporary funds, whereas temporary funds are now held by the State Treasury.

Non-tax revenues in 2003 included UAH 19.4 million mainly comprised of dividends from City shareholdings and interest on short-term bank deposits, which are budgeted to amount to UAH 24.5 million in 2004; UAH 23.6 million of revenues in the form of administrative fees and rent from City-owned properties, which are budgeted to amount to 67.1 million in 2004; UAH 190.6 million in

revenues of institutions funded by the City Budget, which are budgeted to amount to 108.7 million in 2004; UAH 2.7 million from various administrative fines, which are budgeted to amount to UAH 2.4 million in 2004; and UAH 22.5 million from other non-tax revenues, which are budgeted to amount to UAH 44.4 million in 2004.

Revenues from Capital Transactions

Revenues from capital transactions undertaken by the City are principally comprised of proceeds from the sale of the City-owned land and other property, including revenues from privatisation. Revenues from capital transactions amounted to nil in 2000, UAH 21.6 million in 2001, UAH 220.7 million in 2002 and UAH 421.9 million in 2003 and are budgeted to amount to UAH 419.9 million in 2004. The large increase in revenues from capital transactions from 2001 to 2002 is due primarily to the fact that in 2002 there was a change in the principles relating to the treatment of privatisation revenues. Prior to 2002, such revenues were classified as non-tax revenues.

Purpose Fund Revenues

Sources of Purpose Fund revenues contained in the 2002, 2003 and 2004 City Budgets include, among others:

- investors' contributions made in the development of the City's infrastructure (i.e. mandatory contributions required to be made by developers);
- registration fees for foreign investments (proceeds from investment agreements);
- charges for environmental pollution;
- payments for the right to temporary placement of external advertisements on City-owned facilities;
- payments for the right to rent non-residential premises;
- proceeds from the disposal of property and shareholdings;
- proceeds from sales of residential and non-residential premises;
- proceeds under agreements on reservation of land and out of public biddings with respect to the sale of rights to leased land; and
- income of City-owned businesses subject to allocation to the City Budget.

Aggregate Purpose Fund revenues amounted to UAH 100.4 million in 2002 and UAH 262.9 million in 2003. The 2004 City Budget provides for Purpose Fund revenues of UAH 321.7 million. The increase in revenues from 2002 to 2003 is principally attributable to the increase in investors' contributions made in the development of the City's infrastructure and reflects the increase in construction activity.

Purpose Fund revenues not spent in a given year are carried forward and are available for use within the same category of fund in the following year.

Grants and Subsidies from the State Budget

As a result of the enactment of the Budget Code, since 1 January 2002 the City Budget has been entitled to receive levelling grants and various subsidies from the State Budget and/or subsidies from other local budgets.

The City did not receive a levelling grant for either the 2002 or 2003 budget years.

The City Budget received revenues from various subsidies from the State Budget in aggregate amounts of UAH 342.3 million in 1999, UAH 4.4 million in 2000, UAH 336.0 million in 2001 and UAH 236.6 million in 2002. The low amount of subsidies received in 2000 as compared with 1999 and 2001 is attributable to the fact that in 2000 it was determined that a significant subsidy was not necessary due to an expected substantial increase in tax revenues from 1999 to 2000.

The City received UAH 336.5 million in total subsidies from the State in 2003 and expects to receive UAH 437.1 million in total subsidies from the State in the 2004 budget year (of which approximately UAH 92.4 million has been received to date), in addition to further subsidies in the amount of UAH 108 million which have been approved for the purposes described below. The subsidies in the 2003 City Budget included utilities subsidies and benefits of UAH 146.1 million (expected to be UAH 279.6 million in the 2004 budget year); veterans' benefits and transport subsidies for certain categories of citizens of UAH 67.1 million (expected to be UAH 44.6 million in the 2004 budget year); aid to low-income families and disabled people of UAH 29.7 million (expected to be UAH 33.0 million in the 2004 budget year); subsidies to victims of the Chernobyl disaster of UAH 52.2 million (expected

to be nil in the 2004 budget year); and the implementation of investment projects of UAH 12.1 million (expected to be nil in the 2004 budget year). The 2004 City Budget also provides for subsidies from the State for the construction of new metro lines of UAH 40.0 million. In addition, further subsidies in the amount of UAH 108 million have been approved, principally for increasing salaries, student scholarships and stipends and for performing the role of capital of Ukraine in 2004. The City believes there is a trend towards increasing levels of subsidies from the State, and this trend is expected to continue into the foreseeable future.

See “– City Budgetary System – Budgetary Relations between the State and Local Governments” and “Risk Factors – Risks Associated with the City – The division of tax revenues with the State may not favour the City, thereby making it difficult for the City to repay the Loan”.

Transfer of Funds from Deposits

Transfer of funds from deposits comprises part of the unused U.S. dollar proceeds from the offering of notes in 2003 which had been deposited in a U.S. dollar bank account with Commercial Bank Khreschatyk by the City in 2003 and which were converted into UAH and transferred to the City’s UAH account with the Treasury in 2004 prior to application to specified budgetary expenditures.

Budget Expenditures

In 2003, the expenditures of the City Budget were on six primary activities: education; health care; welfare (social services); housing and utilities; construction; and transport and infrastructure.

The following table sets out the expenditures of the City out of the City Budget for the years ended 31 December 2001, 2002 and 2003 and the budgeted expenditures for the year ending 31 December 2004:

	2001		2002		2003		2004 ⁽¹⁾	
	UAH millions	per cent.	UAH millions	per cent.	UAH millions	per cent.	UAH millions	per cent.
Expenditures								
Education.....	478.8	9.5	511.9	11.6	592.7	12.6	678.1	11.4
Health care.....	482.2	9.5	508.5	11.5	610.9	12.9	644.0	10.8
Welfare (social services).....	360.9	7.1	373.1	8.4	442.7	9.4	563.8	9.5
Housing and utilities.....	354.2	7.0	282.7	6.4	323.6	6.9	351.43	5.9
Construction	347.1	6.8	227.6	5.1	821.9	17.4	1,768.2	29.7
Transport and infrastructure	191.2	3.8	187.1	4.2	212.8	4.5	198.3	3.3
Other economic services	72.8	1.4	46.4	1.1	58.7	1.2	131.3	2.2
Public administration.....	24.4	0.5	106.9	2.4	132.7	2.8	152.4	2.6
Debt service	0	0.0	25.4	0.6	28.5	0.6	111.5	1.9
Culture and art	94.9	1.9	94.2	2.1	93.9	2.0	110.9	1.9
Physical culture and sport	26.7	0.5	37.1	0.8	88.0	1.9	70.8	1.2
Media.....	19.9	0.4	22.2	0.5	28.3	0.6	28.6	0.5
Purpose Fund expenditures.....	306.4	6.0	103.8	2.3	247.6	5.2	321.8	5.4
Prevention of and response to emergencies and natural disasters.....	1.0	0.0	0.0	0.0	2.6	0.1	3.1	0.1
Reserve fund.....	11.9	0.2	1.9	0.4	0.7	0.0	4.9	0.1
Other expenditures.....	82.8	1.6	174.6	4.0	131.6	2.5	243.0	4.1
Funds transferred to the State Budget and other subsidies.....	2,201.7	43.5	1,713.5	38.7	903.2	19.1	563.8	9.5
Total expenditures	5,056.9	100	4,416.9	100	4,720.2	100	5,945.8	100

Source: Kyiv City State Administration, Main Financial Office

Note:

(1) Figures reflect the planned City Budget as approved by the City Council, not the results of implementation.

Total expenditures from the City Budget increased from UAH 3.45 billion in 2000 to UAH 5.06 billion in 2001 and then decreased to UAH 4.42 billion in 2002 and subsequently increased to UAH 4.72 billion in 2003. Under the 2004 City Budget, budget expenditures in the current year are expected to increase to UAH 5.95 billion. The increase in expenditures from 2000 to 2001 was primarily due to an increase in the amount of funds transferred to the State Budget, which was in turn due to a change in 2002 in the method of determining the amount of funds to be transferred from the City

Budget to the State Budget. The decrease in expenditures from 2001 to 2002 was primarily due to a decrease in the amount of funds transferred to the State Budget, which was in turn due to a change in 2002 in the treatment of corporate income tax. See “– Funds Transferred to the State Budget” below. The increase in expenditures from 2002 to 2003 was primarily due to increased construction expenditures, which are in turn due to increased availability of funds in 2003 as a result of new borrowings. The increase from expenditures in 2003 to budgeted 2004 expenditures is primarily due to the increase in expected expenditures under primary activities, including education, health-care, welfare and housing and utilities, expenditures in support of small businesses and expenditures in support of debt service.

Education

Education expenditures include the funding of schools, boarding schools, extracurricular events, technical schools and colleges and certain municipal graduate institutions (academies and institutes). Expenditures on education were UAH 410.3 million in 2000, UAH 478.8 million in 2001, UAH 511.9 million in 2002 and UAH 592.7 million in 2003. According to the 2004 City Budget, the City is expected to spend UAH 678.1 million on education in 2004. The City expects the trend of increasing levels of expenditures on education to continue. The increase in expenditure over the period from 2000 to 2004 is principally attributable to increasing levels of staff salaries.

Health Care

Primary health and ambulatory care, hospitals and health education are funded from the City Budget. Expenditures on health care were UAH 386.9 million in 2000, UAH 482.2 million in 2001, UAH 508.5 million in 2002 and UAH 610.9 million in 2003. According to the 20034 City Budget, the City is expected to spend UAH 644.0 million on health care in 2004. The increase in expenditure over the period from 2000 to 2004 is principally attributable to increasing levels of staff salaries and partly due to increasing costs of medication and maintenance.

Welfare (Social Services)

Welfare (social services) expenditures include welfare payments and housing and utilities subsidies to certain categories of residents including senior citizens, veterans, disabled people, low income families, families with more than one child, young people and abandoned children. Expenditures on welfare (social services) were UAH 266.3 million in 2000, UAH 360.9 million in 2001, UAH 373.1 million in 2002 and UAH 442.7 million in 2003. According to the 2004 City Budget, the City is expected to spend UAH 563.8 million on welfare (social services) in 2004.

Housing and Utilities

Housing and utilities expenditures include expenditures for maintenance of the City’s residential housing and subsidies for housing and utilities for Kyiv residents generally. Expenditures on housing and utilities were UAH 275.2 million in 2000, UAH 354.2 million in 2001, UAH 282.7 million in 2002 and UAH 323.6 million in 2003. According to the 2004 City Budget, the City is expected to spend UAH 351.3 million on housing and utilities in 2004. The increase in expenditure from 2000 to 2001 and from 2002 to 2003 is principally attributable to increasing levels of population and maintenance costs, while the decrease from 2001 to 2002 was principally due to a reallocation of funds to cover the shortfall in revenues from corporate profit tax.

Construction

Construction expenditures include expenditures for construction and reconstruction projects in the areas of transport and infrastructure, public utilities, housing, health care facilities and educational and cultural facilities. Construction expenditures in a given year reflect actual amounts spent in that year. Expenditures on construction were UAH 314.7 million in 2000, UAH 347.1 million in 2001, UAH 227.6 million in 2002 and UAH 821.9 million in 2003. The large increase from 2002 to 2003 was attributable to the City’s expenditures on construction projects during 2003, principally expenditures on construction of part of the metro system. Part of the construction work was carried out in the years 2001-2002 but not paid for until 2003. Construction expenditures in 2003 were made using funds obtained from financing obtained in 2003, including the offering of the 8.75% loan participation notes due 2008 and domestic borrowings. According to the 2004 City Budget, the City is expected to spend UAH 1,768.2 million in 2004 on construction, including expenditures on the new Podilskiy bridge over the Dnipro River, a new cardiology centre, a new waste recycling plant, new metro lines, roads, sewage collectors and related infrastructure, the assembly of an aeration plant, certain construction projects to improve the quality of the water supply and other utility facilities.

Transport and Infrastructure

Transport and infrastructure is principally comprised of transport expenditures, which primarily include subsidies for reduced fares and public transport capital expenditures. Among the City's proposed investment projects in the transport area, the most significant are the purchase of additional buses, trams, metro trains and other passenger transport vehicles. Expenditures on transport and infrastructure were UAH 176.4 million in 2000, UAH 191.2 million in 2001, UAH 187.1 million in 2002 and UAH 212.8 million in 2003. According to the 2004 City Budget, the City is expected to spend UAH 198.3 million on transport and infrastructure in 2004.

Other Economic Services

Expenditures on other economic services principally include expenses for the promotion and encouragement of entrepreneurs and small and medium-size businesses, which were UAH 58.7 million in 2003 and are expected to be UAH 131.3 million in 2004.

Debt Service

Expenditures on debt service were nil in 2000, nil in 2001, UAH 25.4 million in 2002 and UAH 28.5 million in 2003. According to the 2004 City Budget, the City is expected to spend UAH 111.5 million on debt service in 2004. The increase in expenditures on debt service from 2003 to 2004 is attributable to interest payments on external and internal borrowings incurred during 2003. Expenditures on debt service are expected to increase further from 2004 due to interest payments on the Notes. See “– Indebtedness of the City of Kyiv”.

Public Administration

Public administration expenditures include expenditures for the Kyiv state executive authorities and for local self-government. Expenditures on public administration were UAH 62.3 million in 2000, UAH 24.4 million in 2001, UAH 106.9 million in 2002 and UAH 132.7 million in 2003. According to the 2004 City Budget, the City is expected to spend UAH 152.4 million on public administration in 2004.

Reserve Fund

The City is authorised to establish a reserve fund in the City Budget of not more than 1 per cent. of the total expenditures of the general fund of the City Budget. The funds allocated to the reserve fund cover unforeseen expenditures of a temporary nature. The reserve fund amounted to UAH 11.9 million, UAH 1.9 million and UAH 0.7 million in 2001, 2002 and 2003, respectively, and is budgeted to amount to UAH 4.9 million in 2004.

Funds Transferred to the State Budget

Funds transferred to the State Budget were UAH 1,235.4 million in 2000, UAH 2,201.7 million in 2001, UAH 1,713.5 million in 2002 and UAH 903.2 million, or 19.1 per cent. of total expenditures, in 2003. According to the 2004 City Budget, the City is expected to spend UAH 563.8 million, or 9.5 per cent. of total expenditures, on funds transferred to the State Budget in 2004. The amount of the City's funds transferred to the State Budget is calculated by reference to the amount of tax revenues estimated to be collected by the City in the relevant budget year. The decreases from 2001 to 2002 and from 2002 to 2003 are each largely attributable to the changes in treatment of corporate income tax over those years. Funds transferred to the State Budget decreased from 2003 to 2004 and are expected to decrease further from 2004 as a result of the introduction of the Personal Income Tax law with effect from 1 January 2004. See “– Budget Revenues – Tax Revenues” and “– City Budgetary System – Budgetary Relations between the State and Local Governments”.

Purpose Fund Expenditures

Annually, upon the approval of the City Budget for a particular year in accordance with the City's Social and Economic Development Programme for that particular year, the City Council determines the end purpose on which each Purpose Fund will be spent. In 2003, expenditures from Purpose Funds amounted to UAH 247.6 million. The 2004 City Budget provides for expenditures of UAH 321.8 million from Purpose Funds in 2004. Most of these expenditures are for the financing of various capital investment projects, including preparatory work in connection with such projects. Purpose funds are also used to finance environmental protection activities.

Results of Implementation of the Budget

Budget deficits in 1999 and 2001 reflect reserves from the previous budget year being used to make additional expenditures beyond budget revenues. Implementation of the budget in 2002 resulted in a

surplus of UAH 68.4 million. The deficit in 2003 and the deficit budgeted for 2004 principally reflect borrowings made in the relevant budget year to finance expenditures in excess of revenues.

Indebtedness of the City of Kyiv

General

The indebtedness of the City includes direct obligations of the City, such as loans and bonds, and indirect obligations such as guarantees granted by the City in relation to loans given by Ukrainian and international lenders to City-owned businesses.

The Ministry of Finance is the State body supervising the borrowing activities of the local governments in Ukraine. One of the functions of the Ministry of Finance is to ensure that the borrowings to the local budgets are carried out in compliance with all requirements of applicable budget legislation, including with respect to limits on levels of domestic and external debt and funds spent on debt service and debt repayment. The Budget Code, however, expressly provides that the State does not bear liability for borrowings made by local governments. The total debt of the City at 31 December 2001, 2002 and 2003 was UAH 13.4 million, UAH 171.5 million and UAH 1,011.9 million, respectively. The significant increase in total debt from 2002 to 2003 was principally due to the City's borrowing in 2003 of US\$150 million, funded by the proceeds of the offering of 8.75% loan participation notes due 2008 described below. Of these amounts, UAH 8.6 million, UAH 151.8 million and UAH 100.0 million, respectively, was denominated in hryvnia.

The Budget Code gives the City Council the authority to make domestic and external borrowings. Domestic debt is denominated in hryvnia, while external debt obligations may be denominated in a variety of foreign currencies. The size and composition of the borrowings to be made by the City Council during a budget year are specified in the City Budget for that budget year. Decisions on the level of municipal bond issues, municipal loans or other borrowing, whether in hryvnia or foreign currency, within the limits stipulated by the City Budget, are made by the City Council.

According to the Budget Code, borrowings under the City Budget may be made only for a designated purpose and must be repaid. Such borrowings must be allocated to the "development fund", which is a special fund of the City Budget. The Budget Code permits the City Council to borrow for the purpose of financing a City Budget deficit. However, a City Budget with a deficit may only be approved if the deficit is in the aforementioned "development fund", as opposed to the general fund. While indebtedness principal is paid from the special fund, expenditures for debt servicing (i.e., interest payments) are made from the general fund of the City Budget.

Parliament has recently passed amendments to the Budget Code which, upon becoming effective, will permit local budgets, including the City Budget, to be approved with a deficit in the general fund up to an amount equal to budget reserves from the previous fiscal year.

Pursuant to the Budget Code, in the course of the preparation of the City Budget for a particular budget year, the Kyiv City State Administration is required to submit to the City Council, together with its draft budget resolution, information on the servicing of the City's debt, including the amounts and terms and conditions of the City's borrowings. In practice, prior to a budget year, amounts necessary for the repayment of borrowings are allocated for the purpose of debt servicing in the City Budget for the relevant budget year.

Expenditures for debt servicing must be allocated in the City Budget for the relevant budget year and cannot exceed 10 per cent. of the aggregate expenditures of the general fund of the City Budget within that budget year. The City currently expects that its debt servicing expenditures through 2008 will not exceed 4.6 per cent. of the expenditures of the general fund in each respective budget year.

After a municipal bonds default by the City of Odessa in 1998, the President of Ukraine, by Decree No. 655/98 dated 18 June 1998 (the "Presidential Decree"), prohibited borrowings by local governments absent the approval of the Ministry of Finance. In furtherance of the Presidential Decree, the Ministry of Finance, by Order No. 19 dated 19 January 1999 ("Order No. 19"), introduced a procedure for obtaining consent to carry out domestic borrowings included in local budgets. In contrast to domestic borrowings, no external borrowings could be carried out by local governments until, on 24 February 2003, the Cabinet of Ministers of Ukraine, pursuant to the Budget Code, issued Regulation No. 207 "On Approval of the Procedure of Borrowings to Local Budgets" ("Regulation No. 207"), setting out the procedures for external borrowings made by local government bodies in Ukraine. Regulation No. 207 provides that any borrowings by a city council, either domestic or external, are subject to prior approval of the Ministry of Finance. Regulation No. 207 expressly provides that Ministry of Finance approval should not be construed as a guarantee by Ukraine or the

Ministry of Finance of the performance of obligations of a local government under the relevant borrowings or confirmation of the local government's solvency.

Indebtedness from 1998 to the Present

In 1998, pursuant to Decree No. 523 of the Cabinet of Ministers of Ukraine, dated 21 April 1998, the City received from the State Budget an interest-free loan of UAH 31.5 million, repayable in instalments, for the purpose of financing preparations for the annual meeting of the European Bank for Reconstruction and Development held in Kyiv in May 1998. The outstanding debt under such loan was repaid in full by 1 January 2004.

In 1998, the World Bank provided a loan of US\$18.29 million to the State through the Ministry of Finance to be further on-loaned by the State in order to finance the purchase and installation of energy-saving equipment in 1,300 social and cultural buildings in Kyiv. The funds are to be loaned by the Ministry of Finance to the City in several tranches, and, as of 1 April 2004, US\$9.8 million of such loans had been received by the City. The loans to the City have 12-year terms with a 1 per cent. interest rate and a five-year grace period on payments of principal. The City will begin to repay the principal under such loans in 2005. The aggregate amount loaned to the City is expected to increase to \$18.29 million by the end of 2004.

The City had no borrowings between 1998 and 2001.

In 2002, pursuant to Resolution No. 57/217 of the City Council dated 24 October 2002 on the Amendments to Resolution No. 162/1596 of the City Council of 20 December 2001 on the 2002 City Budget, and based on permission from the Ministry of Finance, the City borrowed an aggregate amount of UAH 150 million in the form of the following domestic loans from Ukrainian banks:

- a UAH 30 million loan from Prominvestbank, a Ukrainian commercial bank, at a 17.5 per cent. interest rate with a maturity of 20 November 2003;
- a UAH 106 million loan from Joint Stock Post Pension Bank "Aval" at a 17.5 per cent. interest rate with a maturity of 24 December 2003; and
- a UAH 14 million loan from the City-owned commercial bank "Khreschatyk" at a 17.5 per cent. interest rate with a maturity of 20 November 2003.

The proceeds of these loans were used for capital investments in the areas of transport infrastructure and housing and utilities and for the restoration of cultural monuments. These loans were repaid in full by 31 December 2003.

The original 2003 City Budget Resolution provided for the City Council to borrow up to UAH 120 million in domestic borrowings and UAH 577.5 million (approximately US\$110 million) in external borrowings. By Letter No. 022-03/57, dated 15 April 2003, the Ministry of Finance approved the initially budgeted borrowings of the City Council. On 26 June 2003, by its Resolution No. 513/673 on Amendments to Resolution No. 232/392 of the City Council on the 2003 City Budget of 28 December 2002, the City Council increased the amount of permitted external borrowings to up to UAH 1,066.6 million (approximately US\$200 million). The Ministry of Finance approved such increase by its Letter No. 03200-03/137 dated 25 June 2003.

In August 2003, pursuant to the 2003 City Budget Resolution, as amended by Resolution No. 513/673 and approved by Letter No. 03200-03/137 of the Ministry of Finance, each as described above, the City borrowed US\$150 million, which was funded from the proceeds of the offering of 8.75 per cent. loan participation notes due 2008 by Dresdner Bank Aktiengesellschaft. In November 2003, the City borrowed an additional UAH 100 million by way of a domestic offering of hryvnia-denominated bonds due 2008.

The 2004 City Budget Resolution, as amended on 15 April 2004 by Resolution No. 149/1359 of the City Council on Amendments to Resolution No. 267/1142 of the City Council on the 2004 City Budget of 18 December 2003, provides for the City Council to borrow up to US\$200 million in external borrowings. By Letter No. 31-05220-02-7/5705, dated 7 April 2004, the Ministry of Finance approved such budgeted external borrowings of the City Council.

Guarantees

The Law on Local Government and the Law on the Capital expressly provide that the City may only guarantee the obligations of City-owned businesses under their respective loan agreements, and the 2004 State Budget Law contains a prohibition on the issuance by the City of a guarantee for the debts of any third party, including City-owned businesses. The only exceptions to this prohibition are

guarantees securing loans granted or co-financed by an international financial institution or loans that are being repaid from the State Budget.

Prior to 2003, the City Council guaranteed loans obtained from Ukrainian and foreign banks and other obligations of various City-owned businesses to finance expenditures that the City considered to be a priority and in which the City had an interest. These guarantees are budget guarantees whereby the full taxing and borrowing power of the City and non-tax revenues are made available towards payment in the event that the City contractor fails to perform its obligations. The City has also provided hard currency guarantees, whereby the City has guaranteed payment of obligations denominated in various foreign currencies.

While the City is currently not permitted to issue guarantees, there can be no assurance that it will not be permitted to do so in the future.

Domestic Debt of the City of Kyiv

The following table sets out the domestic debt of the City as at 1 April 2004:

	<u>Amount, UAH millions</u>
Liability	
Domestic bonds	100.0
Total domestic debt	<u>100.0</u>

Source: Kyiv City State Administration, Main Financial Office

External Debt of the City of Kyiv

The following table sets out the external debt of the City as at 1 April 2004:

	<u>Currency</u>	<u>Amount, millions</u>
Liability		
Loans directly obtained from external sources.....	USD	150.0
	EURO	0.0
World Bank loan obtained via sub-loan from Ministry of Finance	USD	9.8
Total loans		<u>159.8</u>
Guarantees	USD	0.0
	EURO	9.7 ⁽¹⁾
Total guarantees		<u>9.7</u>
Total external debt	USD	<u>171.7⁽²⁾</u>

Source: Kyiv City State Administration, Main Financial Office

Notes:

(1) Guaranteeing obligations under a loan to Kyivvodokanal that is due to be repaid within 10.5 years after drawdown, with a 1.5 year grace period on repayment of principal. The ability of Kyivvodokanal to draw down on the loan is subject to the satisfaction of certain conditions precedent. No disbursements have been made under such loan to date and the City considers that the facility is likely to be terminated.

(2) Based on conversion of Euro amounts at an exchange rate of €1.00 = US\$1.2224 as at 1 April 2003.

Maturity of Debt of the City of Kyiv

	Principal payments due by period					After 5 years	
	Currency	Total	Less than one year	1-3 years	4-5 years		
			(millions)				
Liability							
Domestic debt:							
Domestic bonds.....	UAH	100.0	0.0	0.0	100.0	n/a	
Total domestic debt.....	UAH	100.0	0.0	0.0	100.0	n/a	
External debt:							
Loans directly obtained from							
external sources.....	USD	150.0	0.0	0.0	150.0	n/a	
	EURO	0.0	0.0	0.0	0.0	n/a	
World Bank loan on-loaned to City from Ministry of Finance	USD	9.8	0.0	6.8	5.4	6.1	
Guarantees	USD	0.0	0.0	0.0	0.0	0.0	
	EURO	9.7	0.0	0.0	0.0	0.0	
Total external debt.....	USD	171.7	0.0	6.8	155.4	6.1	

Source: Kyiv City State Administration, Main Financial Office

On 15 April 2004, the City Council, pursuant to Resolution No. 149/1359 on Amendments to Resolution No. 267/1142 of the City Council on the 2004 City Budget of 18 December 2003, decided to borrow up to US\$200 million in external borrowings, the proceeds of which are intended to be used for the implementation of major investment projects, including the construction of the new Podilskiy bridge over the Dnipro River and a waste recycling plant. The City currently anticipates that it will require further financing in the form of external and internal borrowings, including by way of debt offerings in the international capital markets, in 2005 and 2006.

City Debt Management

The Kyiv City State Administration's operating units, including the Main Financial Office and others, are responsible for external debt management and the efficient use of the City's borrowed funds. The principal functions of the Main Financial Office are as follows:

- to facilitate the obtaining of borrowings for the City Budget;
- to estimate the necessity of increasing the City's budget resources by means of various financial instruments;
- to maintain the co-operation of the Kyiv City State Administration with various banks and other financial institutions in the implementation of the City's programmes on social and economic development of the City;
- to maintain central recording of the City's borrowings;
- to monitor the service and discharge of the City's debts;
- to control the strict adherence of the use of borrowings to their specific purposes; and
- to approve loan documentation and confirm its compliance with the requirements of applicable legislation.

Debt Payment Record

Ukrainian legislation imposes strict requirements on the borrowing activity of the City Council. In the event of any failure by the City Council to comply with an agreed schedule of payments with respect to repayment of principal and/or interest under its borrowings, the Budget Code would prohibit the making of new borrowings for the City Budget during the following five years. As of 1 April 2003, the City has no overdue indebtedness with respect to the repayment of principal or interest under past or existing loans.

Assets of the City

The City's assets principally comprise real property holdings, shareholdings in newly established companies and shareholdings in privatised companies. These assets are held for and on behalf of the City by the City Council, which in turn may delegate certain management authority to the Kyiv City State Administration. For the year ended December 31, 2003, the City's assets generated estimated revenues of UAH 421.8 million for the City, compared with UAH 220.7 million in 2002.

Properties

The legal basis of the City's ownership to real estate is established by the Constitution of Ukraine, the Law of Ukraine "On Property", the Law on Local Self-Government and the Law on the Capital. The City Council's Standing Commission on City-owned Properties is the holder, manager and landlord of the City-owned property holdings on behalf of the City. The Standing Commission on City-owned Properties usually delegates the authority to sell the City's property holdings to the Main Office of Communal Property of the Kyiv City State Administration.

As at 31 December 2003, the City owned approximately 9.7 million square metres of non-residential real estate and approximately 45.5 million square metres of residential real estate.

Share Ownership

Of the 50 joint ventures and privatised companies in which the City is a shareholder or participant, the City currently holds shares in 28 open joint-stock companies whose shares are capable of being traded on the Ukrainian stock exchanges or trading systems. Only a portion of these shares trade with any degree of liquidity, however. The City participates in the management of these companies, including through representation on the companies' boards of directors. In addition, there are 470 municipal businesses in the City. The profits derived by municipal businesses either accrue to the City Budget or are used by such businesses for their own development.

The City received estimated dividends of UAH 12.9 million in 2003 from companies in which it is a shareholder or participant, as compared with dividends of UAH 10.7 million in 2002 and UAH 7.6 million in 2001. According to the 2004 City Budget, the City is expecting to receive dividends in an amount of UAH 14.0 million in 2004.

The City promotes and supports companies that are co-owned by the City through transferring some of the City's property holdings, maintaining City-owned property used by such companies, providing tax remissions and in some cases providing financial support for specific purposes, including as compensation for lost revenues resulting from City regulation of prices of the goods or services such companies produce or render. In 2003, the City provided an aggregate amount of UAH 45.8 million of such financial support to such companies.

The City's interests in privatised and commercial businesses include, among others, its ownership interests of 12.7 per cent. in JSEC "Kyivenergo" (an energy distributor), 50 per cent. plus one share in JSC Khib Kyiva (formed following the merger of OJSC "Kyivkhib" (a bread producer) and CJSC "Kyivmlyn" (a flour producer)), 51 per cent. in OJSC "Kyivspetstrans" (a public transport company), 80 per cent. in JSC "Kyivmiskbud" (a construction company), 92.5 per cent. in OJSC "Kyivvodokanal" (a water supply and waste management company), 100% in State Public Utility Gas Supply Enterprise "Kyivgas", 95.7 per cent. in OJSC "Kyivkhimvolokno" (a chemical producer), 53 per cent. in OJSC Commercial Bank "Khreschatyk" (a commercial bank) and 30 per cent. in OJSC "Kyivproekt" (an infrastructure and construction design company). See "The City of Kyiv – Privatisation".

UKRAINE

The following information relating to Ukraine is for background purposes only. The information presented in this subsection has been extracted from the offering circular dated 2 March 2004 for the issuance of Ukraine sovereign debt securities, which was prepared by the Cabinet of Ministers of Ukraine, represented by the Ministry of Finance for and on behalf of Ukraine, and was not prepared in connection with the preparation of this Offering Circular.

General

Ukraine occupies a land area of 603,700 square kilometres, which makes it the second largest country in Europe, after Russia. It is bordered by Russia to the east, Belarus to the north, Poland, Slovakia, Hungary, Moldova and Romania to the west and the Black Sea to the south. Ukraine is split into 24 oblasts (or regions) and has two major cities, Kyiv, the capital, and Sevastopol. The Crimean Peninsula constitutes an autonomous republic.

The population of Ukraine totaled approximately 47.6 million at 1 January 2004, of which about 73 per cent. were ethnic Ukrainians and 22 per cent. ethnic Russians. Other groups, including Byelorussians, Moldovans, Bulgarians, Crimean Tatars, Hungarians, Romanians, Greeks and Poles accounted for about 5 per cent. of the population. The official language is Ukrainian, although 80 per cent. of the population is bi-lingual, speaking both Ukrainian and Russian fluently.

Ukraine inherited a large heavy industrial sector from the Soviet era especially in iron and steel, aerospace and transport aircraft and other military equipment. Ukraine was traditionally viewed as the “bread basket” of the Soviet Union. Since independence, however, the agricultural sector has been hit by protectionist policies adopted by some of Ukraine’s trade partners. Ukraine also possesses a large mineral reserve base.

International Relations

Ukraine has established diplomatic relations with 169 countries and attaches high importance to developing relations with international organisations. Ukraine is a member of the United Nations (“UN”) and participates in the organisation’s activities in the areas of security, human rights, economic cooperation and environmental protection. Ukraine has signed and ratified the Non-Proliferation Treaty and other conventions banning weapons of mass destruction. Ukraine is a member of the IMF, the World Bank and a number of other international organisations, and it cooperates closely with the Organisation for Economic Cooperation and Development (“OECD”).

Ukraine applied to join the WTO in 1993. As at 13 February 2003, Ukraine had signed bilateral protocols on access to markets for goods and services with 23 of the WTO member countries that participate in the WTO working party for the negotiations with Ukraine, including an agreement with the EU signed in March 2003. Ukraine expects to finalise membership negotiations and become eligible for WTO membership in 2004. Achieving the target date of accession will be largely contingent on arriving at an agreement with the United States, in particular with respect to intellectual property protection measures in Ukraine, as well as on Ukraine’s ability to harmonise its legislation with WTO rules. Despite Ukraine’s efforts to improve its intellectual property protection legislation, at an annual review on 1 May 2003, the United States decided to keep in effect sanctions in the form of import tariffs imposed in January 2002 estimated to cost Ukraine U.S.\$75 million per year in lost trade for its failure to maintain adequate intellectual property rights protection.

Ukraine is a party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards and the Convention on the Settlement of Investment Disputes between States and Nationals of Other States. However, Ukraine has not entered into a treaty on the recognition and enforcement of judgments with the United States, Luxembourg, Germany or the United Kingdom.

Political Structure and Recent Developments

The Constitution and the President

The Constitution (the Fundamental Law of Ukraine) was adopted by Parliament on 28 June 1996. It defines Ukraine as a sovereign, independent, democratic, social, legal and unitary state. The Constitution guarantees, among other things, the principles of political, economic and ideological diversity; human and civil rights and freedoms; freedom of the press; the inviolability of private property and the right to conduct entrepreneurial activity. The state ensures the protection of competition and business activity.

The Constitution also stipulates the responsibilities of the Parliament, the President and the Government and outlines the system for the administration of justice and the functions of the judiciary of Ukraine. Under the Constitution, both the President and Parliament are directly elected by universal suffrage.

The Constitution envisages that the President is the head of Ukraine as a sovereign state and is authorized to act on behalf of Ukraine both within and outside of Ukraine. The President is elected for a term of five years and has the authority to appoint the Prime Minister, subject to parliamentary approval. The Prime Minister, in turn, appoints the Cabinet of Ministers, subject to presidential approval. The President has the right to initiate legislation, the power to veto Parliamentary bills and the right to revoke acts of the ministers. The President may also issue his own decrees and directives.

The Executive

The powers of the Government of Ukraine are vested in the Cabinet of Ministers of Ukraine, which is the highest body of executive power in Ukraine. The Cabinet of Ministers reports to the President and is accountable to the Parliament.

Ukraine continues to redefine the powers of the Executive but Parliament has yet to approve a law which will define the principal objectives of the Cabinet, principles of its organisation and other related issues. In line with the recommendations of the IMF and the World Bank, in December 1999, President Kuchma issued decrees providing for radical reform of the Cabinet of Ministers. In particular, as part of the ongoing administrative reform, the number of ministries was reduced from 24 to 15 and a number of other state committees and governmental departments were restructured to simplify administration and enhance accountability.

The Legislature

Legislative power in Ukraine is vested in the Parliament. The Parliament adopts laws, which have the highest authority in the hierarchy of normative acts in Ukraine after the Constitution itself. The Parliament is a unicameral body comprising 450 seats. Half of the seats are elected pursuant to a majority voting system from single-seat constituencies representing all regions of Ukraine and the other half are chosen from lists of political parties with not less than 4 per cent. of parliamentary representation, according to a system of proportional representation. Members of Parliament are elected for a term of four years. In a nationwide referendum held in April 2000, the introduction of a bicameral Parliament and measures to reduce the number of Parliamentary members to 300 were approved by the electorate. These measures have not yet been incorporated into the Constitution by Parliament. Draft Constitutional amendments which would address some of the results of the referendum have recently been proposed by certain members of Parliament and are currently before Parliament.

In addition to its legislative function, Parliament nominates the Governor of the NBU, confirms the President's appointment of the Prime Minister and the Chairman of the State Property Fund and decides on items such as the general Government agenda, including the State budget and the privatisation programme, granting and receiving loans from foreign countries, international organisations, banks and international financial institutions that are not otherwise envisioned in the State budget in any given year and the general structure, strength and functions of the Ukrainian armed forces.

The Judicial System and Legal Framework

The Constitutional Court of Ukraine is the highest judicial body in Ukraine. It has exclusive jurisdiction over the interpretation of the Constitution and laws of Ukraine and acts as final arbiter on constitutional issues. It consists of 18 judges, six nominated by the President, six nominated by Parliament and six nominated by the Congress of Judges. At the end of 2003, draft constitutional amendments providing for the nomination of judges to the Constitutional Court only by the President and Parliament were preliminarily agreed by Parliament. Judges of the Constitutional Court were chosen for the first time in 1996 as the late adoption of the Constitution hampered development of the judicial system before June 1996. In June 2002, the Law of Ukraine "On the Judicial System" came into force. This law aims to reform the Ukrainian judicial system and envisages the creation of new judicial institutions, as well as a system of specialised courts. However, the creation of specialized courts has been postponed because of insufficient funds in the State budget.

As a result of its relatively recent transition towards a market economy, Ukraine does not yet have a mature legal system comparable to the legal systems of most major European countries. Although new

laws have been introduced and amendments have been made to company, property, bankruptcy, securities, taxation, banking and foreign investment legislation, the legislation is undeveloped and contains many gaps, thereby failing to provide an adequate underpinning for sophisticated transactions. In order to facilitate implementation and enforcement of important legislation, such as tax legislation, Parliament has gradually been taking steps to adopt new legislation that consolidates the laws into unified codes.

On 1 January 2004, a number of new legislative acts came into force, the key ones comprising new editions of the Civil Code, the Economic Code, the Customs Code, the Family Code and the Criminal Enforcement Code.

In 2001, a new comprehensive tax code was proposed in Parliament and was adopted in the second reading but rejected in the third reading. Since then, Parliament has adopted several separate tax laws throughout 2002 and 2003 instead of implementing the proposed new tax code. In early January 2003, the President signed a new law which reforms corporate profit tax. The new law reduces the corporate profit tax rate from 30 per cent. to 25 per cent. effective from 1 January 2004. In May 2003, the President signed the Law of Ukraine "On Personal Income Tax" that became effective on 1 January 2004. This law reforms personal income tax by introducing a flat tax of 13 per cent. for all levels of income until 31 December 2006 and 15 per cent. starting from 1 January 2007. Before the introduction of this tax law, individuals were subject to personal income tax at rates ranging from 10 per cent. to 40 per cent. The new law also introduced a new tax on interest accrued on private deposits held by individuals in Ukrainian commercial banks, which tax will be withheld starting from 1 January 2005. On 19 June 2003, the Parliament passed a law under which the rate of VAT would be reduced from 20 per cent. to 17 per cent. to be effective from 1 January 2004 and which provided for the elimination of certain tax privileges. The President vetoed this law and redirected it to Parliament. On 12 December 2003, the President signed a law prolonging until 1 January 2005 VAT privileges, including zero-rate VAT, for certain kinds of agricultural producers. A new tax law was adopted by Parliament in February 2004 providing for comprehensive tax reform, including a reduction in the VAT rate from 20 per cent. to 17 per cent. beginning as of 1 January 2005 and to 15 per cent. beginning as of 1 January 2006, the elimination of certain tax privileges in publishing and in respect of sales of books, housing construction and sales of pharmaceutical products. The tax law also provides for a special VAT regime and reduced VAT rates for producers in the agricultural, forestry and fishing sectors beginning as of 1 January 2005. The President has vetoed this new tax law, but there remains a possibility that Parliament may override the veto.

Regional Administration

Each of Ukraine's 24 oblasts, cities (including Kyiv and Sevastopol) and rayons (or subdivisions) has a governor who is appointed by the President. Each of these governors heads the region's respective administrations (local executive bodies). In addition, municipal government is administered by a local Council of Deputies, a body made up of representatives elected from each of the regions' rayons. Crimea is an autonomous republic within Ukraine, with its own constitution, parliament and government, but remains subordinate to the central Government of Ukraine.

Political Parties and Elections

In October 1999, presidential elections were held and President Kuchma was re-elected for a second term of five years. President Kuchma won 36 per cent. of the votes in the first round of elections and 56.3 per cent. in the final round against the Communist leader Petro Symonenko, who obtained 37.8 per cent. of the votes. Following his re-election, President Kuchma appointed Mr Viktor Yushenko (the former governor of the NBU) as Prime Minister. In mid-2001, Mr Yushenko was dismissed and replaced with Mr Anatoliy Kinakh.

Between 1999 and 2001, the pace of reform was adversely affected by political deadlock in Parliament notwithstanding the re-election of President Kuchma in October 1999. In early 2000, Ukraine underwent a political crisis in Parliament revolving around attempts by a newly formed, largely pro-presidential centre-right majority to replace the incumbent Speaker and First Deputy Speaker. On 16 April 2000, the pro-presidential and centre-right majority survived a nationwide referendum that was called to vote on questions of the scope of parliamentary authority. The result of the referendum also supported the grant of additional powers to the President (particularly as regards the dissolution of Parliament and the calling of new elections) and the restructuring of Parliament. These measures have not yet been implemented into the Constitution by Parliament, although several constitutional amendments currently debated in Parliament address the results of the referendum.

On 16 November 2002, President Kuchma dismissed Prime Minister Kinakh and the then Cabinet of Ministers. President Kuchma nominated Viktor Yanukovich, the governor of the Donetsk region, as Prime Minister and the nomination was approved by Parliament on 21 November 2002. The new Cabinet of Ministers was appointed by President Kuchma at the end of November 2002. Also in December 2002, Mr Volodymyr Stelmakh, the head of the NBU, was replaced with Mr Serhiy Tyhypko. On 7 December 2002, the Prime Minister, the head of Parliament and leaders of Parliamentary factions comprising a majority in Parliament, signed a political agreement of cooperation and joint responsibility, which sets out the scope of activity in which the Cabinet of Ministers and Parliament will cooperate.

Currently, the parliamentary majority supporting the Government comprises approximately 234 seats (52 per cent. of the seats in Parliament). The larger factions which comprise the majority include the Social-Democratic Party (united), Regions of Ukraine, Democratic Initiatives and the Party of Manufacturers and Businessmen and Labour Ukraine Party. The larger factions which form the opposition include Our Ukraine, the Socialist Party, the Communist Party of Ukraine and the Yulia Tymoshenko bloc. The next presidential elections are due in October 2004.

Economic Background

Prior to commencing the transition to a market economy, Ukraine had a centrally planned economy that was geared towards Russia and the other countries in the CIS. While economic transition has begun to a considerable extent as policies of liberalisation, privatisation and financial stabilisation have been adopted by President Kuchma and his Government, the process remains incomplete in many substantial respects. Although the Government has generally been committed to economic reform, lack of political consensus in Parliament and controversies surrounding such issues as privatisations, subsidies to state-owned businesses and cooperation with international financial institutions have impeded reform. The pace of reform has also been adversely affected by various political problems and the emerging market crisis in 1998 as well as the more recent international economic slow-down. These delays, together with deteriorating conditions in the social sphere associated with substantial declines in income and high real unemployment, have exerted enormous pressure on limited state resources. Furthermore, the structural weaknesses in the economy that remain are likely to restrain economic growth and continue to impose substantial fiscal pressures on the Government over the coming years.

Gross Domestic Product

The following table sets forth certain information about Ukraine's GDP for the periods indicated.

	1999	2000	2001	2002	11 months ended 30 November 2003
GDP					
Nominal GDP (UAH millions).....	130,442.0	170,070.0	204,190.0	225,810.0	226,338.0
Nominal GDP (U.S.\$ millions) ⁽¹⁾	24,988.9	31,320.4	38,562.4	42,389.7	42,449.0
Real GDP (% change) ⁽²⁾	99.8	105.9	109.2	105.2	107.7 ⁽³⁾
Nominal per capita GDP (U.S.\$ millions).....	502.7	635.4	788.4	879.4	n/a ⁽⁴⁾

Notes:

- (1) Hryvnia amounts have been converted to dollar amounts using the period-end exchange rate specified under the heading "The Monetary System – Exchange Rates" and, for the eleven months ended 30 November 2003, the rate of UAH 5.33 = U.S.\$1.00.
- (2) The State Committee of Statistics calculates real GDP for a particular year by dividing nominal GDP for such year by the relevant consumer price index. The real GDP per cent. change for a particular year indicates the per cent. change from the previous year, where 100 = 0 per cent. growth.
- (3) As compared with the same period in 2002.
- (4) As full-year nominal GDP is not yet available, this figure does not offer a meaningful comparison with nominal per capita GDP for prior years.

Source: State Committee of Statistics

Privatisation

Ukraine began implementing a privatisation programme in 1992 with the objectives of increasing the private sector's share of the economy, generating foreign direct investment and contributing funds for the State budget. From 1992 to the end of 2003, Ukraine collected approximately UAH 10.7 billion in

privatisation receipts with approximately UAH 6.9 billion collected during the 2000-2003 Privatisation Programme.

Initially the privatisation programme focused on the sale of small scale enterprises (before 2000, enterprises with a book value of fixed assets worth no more than UAH 170 million; after 2000, enterprises with up to 100 employees) through auctions. According to figures published by the State Property Fund ("SPF"), 73,749 small scale entities were privatised by the end of 2003, including 20,090 since 1 January 2000. In addition, Ukraine implemented a privatization programme of medium to large scale enterprises (before 2000, enterprises with a book value of fixed assets over UAH 170 million; after 2000, enterprises with more than 100 employees). Companies identified as part of such privatisation programme are first converted into joint-stock companies and then sold to investors through commercial tenders, sales of privatisation certificates, auctions, preferential sales, leases and buyouts. Between 1992 and the end of 2003, 11,301 companies were converted into joint stock companies. More than 70 per cent. of these enterprises were transformed into municipal ownership and the remainder became private. From the beginning of privatisation 11,595 medium to large scale enterprises underwent a sale of at least 70 per cent. of their statutory capital.

During 2003, approximately UAH 2.2 billion in revenues from privatisations were received by the State Property Fund, against a target of UAH 2.1 billion. Of this amount, UAH 400 million was received from the sale in November 2002 of a 25 per cent. stake in Ukrainian Mobile Communications (payment for which was received in 2003) and UAH 410 million was received from the sale of a final 50 per cent. stake in a ferroalloy plant.

For 2004, target privatisation revenues have been set at UAH 2.14 billion. A draft law "On State Privatisation Programme" that would have provided for approval of the State Privatisation Programme for 2003-2008, further improvement of the privatisation process, the transition to large scale market transformation and preparation to privatise certain strategic sectors of the economy was rejected by the Parliament in September 2003. A revised draft privatisation programme for 2004-2006, which would permit the privatisation of certain regional and sector-specific enterprises, has been prepared and submitted to the Cabinet of Ministers for approval.

Unemployment

Since 1992, the number of people employed in the Ukrainian economy has declined significantly due to the restructuring of the economy. Based on figures calculated by the Ministry of Labour using an internationally accepted methodology of household surveys (the International Labour Organisation (ILO) methodology), which accounts for all persons capable of working between the ages of 15 and 70, the level of unemployment in Ukraine was 11.1 per cent. in 2001 and 10.2 per cent. in 2002. However, it is estimated that, as a result of the comparatively low level of unemployment benefits, less than half of those unemployed register with the National Employment Service. The National Employment Programme recently adopted by Parliament aims to reduce the rate of unemployment by creating incentives to open small businesses, supporting distressed regions and promoting temporary employment. The programme also aims to increase unemployment registration rates and provide retraining opportunities for the long-term unemployed.

Balance of Payments

The following table sets out Ukraine's balance of payments for the periods shown.

	1997	1998	1999	2000	2001	Nine months ended 30 September	
						2002	2003
	(in U.S.\$ millions)						
Current Account	(1,296)	932	1,207	1,402	3,173	2,207	2,489
Goods and Services (balance)	(1,207)	1,095	1,301	613	1,857	1,205	1,321
Export of Goods and Services	17,621	16,332	19,248	21,086	23,351	16,625	20,559
Import of Goods and Services	(18,828)	(15,237)	(17,947)	(20,473)	(21,494)	(15,375)	(19,238)
Goods (balance) ⁽¹⁾	(2,584)	(482)	505	198	710	485	124
Service (balance) ⁽²⁾	1,377	1,577	796	415	1,147	765	1,197
Revenues (balance).....	(871)	(869)	(942)	(667)	(606)	(445)	(373)
Transfers (balance) ⁽³⁾	782	706	848	1,456	1,922	1,402	1,541
Capital and Financial Account...	2,106	(22)	(1,057)	(1,171)	(2,288)	(1,609)	(12,254)
Financial account.....	2,109	32	(1,049)	(1,174)	2,303	(1,617)	2,240
Direct Investment.....	747	489	594	769	698	398	923
Portfolio Investment	47	(86)	(201)	(866)	(1,716)	(1,196)	(529)
Other Investment	(9)	(88)	(1,044)	529	(240)	898	560
Medium term and long term loans	130	5	(688)	169	266	181	219
Short term capital	(139)	(93)	(356)	360	(506)	253	(779)
Change in reserve assets ⁽⁴⁾	1,324	(283)	(398)	(1,606)	(1,045)	(809)	(2,074)
Net Errors and Omissions	(810)	(954)	(150)	(231)	(885)	(598)	(235)

Notes:

- (1) Not taking into account value of goods transferred into ownership of the Russian Federation towards payment of the following debt obligations:
 - in 1999 to the amount of U.S.\$726 million pursuant to the Agreement on Division of the Black Sea Fleet; and
 - in 2000 to the amount of U.S.\$274 million as repayment of NSC “Naftogaz Ukrainy” debt to OJSC “Gazprom”.
- (2) In 2000 without taking into account set-off of payments with the Russian Federation against repayment of state external debt of Ukraine pursuant to the agreement between the Government of Ukraine and the Government of Russian Federation of 28 May 1997.
- (3) Includes payments from Germany and Austria as compensation for World War II victims of U.S.\$150 million per year for each of 2002-2005.
- (4) Numbers in parentheses represent an increase in reserves.

Source: NBU

Public Finance and Fiscal Policy

Ukraine was confronted with a number of challenges to its fiscal policy after independence: a new fiscal structure had to be built, the tax system had to be re-designed in a market-oriented manner and the disruptions caused by the split from the Soviet Union led to new demands on the budget. In the early post-independence years expansionary fiscal policies were sometimes regarded as a useful tool to shelter the economy from adjustment shocks. Consequently, Ukraine's fiscal deficits increased rapidly in the first years following independence. The consolidated budget deficit (which includes the central and local budgets and most budgetary funds but excludes the pensions fund) amounted to 13.9 per cent. of GDP in 1992, 5.2 per cent. in 1993 and 8.9 per cent. in 1994. Fiscal accounting may, however, have been inaccurate in the early post-independence years with the result that the 1992 and 1993 deficits may have been even higher.

The deficits were financed from 1991 to 1995 predominantly by loans from the NBU and by accumulating arrears on energy imports from Russia and Turkmenistan. Only a relatively small part of the budget deficit was financed by foreign official loans and grants due to disagreements with Western donors over nuclear safety and disarmament. The Government's attempts to protect the economy from the impact of the separation from the Soviet Union through subsidies and social transfer payments meant that the percentage of GDP represented by budget expenditures remained at approximately 53 per cent. from 1992 to 1994 (even according to the official expenditure numbers which are probably understated) and the share of subsidies in budget expenditures rose from 14 per cent. in 1992 to 21 per cent. in 1994.

With the emergence of a domestic treasury bill market in March 1995, the Government continued to finance the deficit in part through the domestic debt markets. However, the domestic treasury bill market was characterised by short maturities and high real interest rates (which were necessary to protect the Ukrainian currency from devaluation). As a result, Ukraine increasingly relied upon

external sources of funding to cover the budget deficits, including official creditors, multilateral organisations and commercial debt. This resulted in a sharp rise in the aggregate external debt of Ukraine from 1994 to 1998. The lack of substantial progress in implementing needed structural reforms in the economy (including improved revenue collection), combined with the fall-out from the Russian and Asian economic crises of 1998/1999, made it increasingly difficult from mid-1998 for Ukraine to refinance its external obligations except on highly disadvantageous terms. During this period, loans from international organisations such as the IMF and the World Bank and from the EU were the only substantial new source of external financing for Ukraine.

The Government also used various payment arrears as a means of helping finance the budget deficit.

External Debt

Ukraine's external public debt was approximately U.S.\$12.5 billion in 1999, approximately U.S.\$10.3 billion in 2000, approximately U.S.\$10.1 billion in 2001 and approximately U.S.\$10.2 billion as at 31 December 2002. The debt reduction in 2000 resulted from the commercial restructuring undertaken in connection with the 2000 exchange offer and repayments of multilateral borrowings as well as the repayment of a certain portion of the gas debt owed to Turkmenistan. The total amount of State external debt as at 31 December 2003 was U.S.\$10.7 billion, including U.S.\$8.6 billion of State external debt (direct debt) and U.S.\$2.1 billion of State-guaranteed external debt (contingent liabilities). The limit for State external debt at the end of 2004 has been set by the 2004 State Budget Law at U.S.\$8.9 billion.

Monetary Policy

The NBU is charged with implementing monetary policy. Currently, the NBU implements monetary policy through instruments such as mandatory reserve requirements for banks, interest rates, open market transactions and lending to commercial banks.

With signs of the economy beginning to stabilise after the financial crisis in 1998, the NBU reduced the discount rate from 45 per cent. at the beginning of 2000 to 27 per cent. at the end of 2000, 12.5 per cent. by the end of 2001 and 7.0 per cent. in December 2002. As at 27 January 2004, the NBU's discount rate was 7.0 per cent. The Lombard rate was decreased from 50 per cent. at the beginning of 2000 to 30 per cent. at the end of 2000, 24 per cent. at the end of 2001 and 8.0 per cent. at the end of 2002. As at 27 January 2004, the Lombard rate was 8.5 per cent.

As of 1 August 2001, the NBU adopted new regulations relating to mandatory reserves of commercial banks, which provide that the NBU will use sanctions for failure to keep prescribed amounts of mandatory reserves which sanctions will be payable from banks' profits. Currently commercial banks are required to annually transfer to their reserves no less than 5 per cent. of their profits until and unless the reserves are equal to 25 per cent. of the regulatory capital.

In 2004, the main targets of NBU's monetary policy are to support macroeconomic stability by increasing, or at least maintaining, foreign currency reserves, staying within the forecasted inflation levels, ensuring the stability of the exchange rate and creating conditions that foster positive structural changes.

International Reserves

At the end of 2003, the international reserves of the NBU amounted to U.S.\$6,937.43 million, having increased by U.S.\$2,437.97 million, or 55 per cent. over the amount of international reserves in 2002. The amount of international reserves at year-end 2003 was equivalent to approximately 2.8 months of import coverage and reflected the continued strength of the current account.

Dynamics of the NBU international reserves for the period 1999-2003

	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>
	(by current exchange rate, U.S.\$ millions)				
International Reserves of the NBU ⁽¹⁾					
including:	1,095.37	1,475.47	3,089.47	4,417.00	6,937.43
Monetary Gold ⁽²⁾	47.21	123.67	134.11	175.42	206.51
Reserves in SDR and Reserve					
Position in IMF	65.56	248.11	251.10	28.29	21.21
Foreign Currency	980.69	1,103.64	2,704.25	4,213.12	6,709.71
Import Coverage (month) ⁽³⁾	0.7	0.9	1.7	2.0	2.8

Notes:

(1) International reserves are equal to the sum of foreign currency, SDR and monetary gold.

(2) Cost of gold is calculated on the basis of the price for one ounce of gold in U.S. dollars at the London Precious Metal Exchange.

(3) Import of goods and services of the future periods is used for calculation.

Source: NBU

FORM OF NOTES AND TRANSFER RESTRICTIONS

The following information relates to the form and transfer of the Notes. Terms defined in the section of this Offering Circular entitled "Terms and Conditions of the Notes" have the same meanings in the paragraphs below where not otherwise defined below.

Form of Notes

All Notes will be in fully registered form, without interest coupons attached. Notes offered and sold outside the United States in reliance on Regulation S will be represented by an interest in a Regulation S Global Note Certificate. The Regulation S Global Note Certificate will be deposited on or about the closing date with a common depository for Euroclear and Clearstream, Luxembourg, and registered in the name of BT Globenet Nominees Limited, as nominee for such common depository in respect of interests held through Euroclear or Clearstream, Luxembourg. By acquisition of a beneficial interest in the Regulation S Global Note Certificate, the purchaser thereof will be subject to certain restrictions on transfer contained in a legend appearing on the face of such Regulation S Global Note Certificate as set forth below. Beneficial interests in the Regulation S Global Note Certificate may at all times be held only through Euroclear or Clearstream, Luxembourg.

Notes offered and sold in reliance on Rule 144A will be represented by interests in a Rule 144A Global Note Certificate, which will be deposited on or about the closing date with a custodian for, and registered in the name of Cede & Co. as nominee for, DTC. The Rule 144A Global Note Certificate (and any note certificates in individual form issued in exchange therefor) will be subject to certain restrictions on transfer contained in a legend appearing on the face of each such note as set forth below. Beneficial interests in the Rule 144A Global Note Certificate may be held through DTC, or indirectly through Euroclear or Clearstream, Luxembourg.

The Regulation S Global Note Certificate will have a Common Code and an ISIN, and the Rule 144A Global Note Certificate will have a CUSIP number and an ISIN.

Transfer Restrictions

According to Chapter VI, Article 3, point A/II/2 of the Rules and Regulations of the Luxembourg Stock Exchange, the Notes shall be freely transferable and therefore no transaction made on the Luxembourg Stock Exchange with respect to the Notes shall be cancelled.

A beneficial interest in Notes represented by the Regulation S Global Note Certificate may be transferred to a person who wishes to take delivery of such beneficial interest in the form of a note represented by the Rule 144A Global Note Certificate only upon receipt by the Registrar or any of the Transfer Agents or Paying Agents of a written certification from the transferor (in the applicable form set out in the schedule to the Agency Agreement) to the effect that such transfer is being made to a person whom the transferor reasonably believes is purchasing for its own account or accounts as to which it exercises sole investment discretion, is a qualified institutional buyer within the meaning of Rule 144A in a transaction meeting the requirements of Rule 144A and in accordance with any applicable securities laws of any state of the United States or any other jurisdiction.

A beneficial interest in the Notes represented by the Rule 144A Global Note Certificate may also be transferred to a person who wishes to take delivery of such beneficial interest in the form of a Note represented by the Regulation S Global Note Certificate only upon receipt by the Registrar or any of the Transfer Agents or Paying Agents of a written certification from the transferor (in the form set out in the schedule to the Agency Agreement) to the effect that such transfer is being made in accordance with Regulation S or Rule 144 (if available) under the Securities Act.

Any beneficial interest in either the Notes represented by the Rule 144A Global Note Certificate or the Notes represented by the Regulation S Global Note Certificate that is transferred to a person who takes delivery in the form of a beneficial interest in the other Global Note Certificate will, upon transfer, cease to be a beneficial interest in such Global Note Certificate and become a beneficial interest in the other Global Note Certificate and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to a beneficial interest in such other Global Note Certificate for so long as such person retains such an interest.

The Notes are being offered and sold in the United States only to qualified institutional buyers within the meaning of and in reliance on Rule 144A. Because of the following restrictions, purchasers of Notes offered in the United States in reliance on Rule 144A are advised to consult legal counsel prior to making any offer, resale, pledge or transfer of such Notes.

Notes Sold Pursuant to Rule 144A

Each purchaser and beneficial owner of Notes offered hereby pursuant to Rule 144A will be deemed to have represented, agreed and acknowledged as follows (terms used herein that are defined in Rule 144A are used herein as defined therein):

- (i) it (A) is not an “affiliate” of the Bank or the Borrower or a person acting on behalf of such an affiliate, (B) is a qualified institutional buyer within the meaning of Rule 144A, (C) is acquiring the Notes for its own account or for the account of such a qualified institutional buyer and (D) such person is aware that the sale of the Notes to it is being made in reliance on Rule 144A;
- (ii) none of the Borrower, the Bank, the Managers or any person representing any such entity has made any representation to it with respect to any such entity or the offering or sale of any Notes, other than the information in this Offering Circular;
- (iii) the Notes are being offered only in a transaction not involving any public offering in the United States within the meaning of the Securities Act, and the Notes offered hereby have not been and will not be registered under the Securities Act and may not be reoffered, resold, pledged, or otherwise transferred except in accordance with the legend set forth below; and
- (iv) Rule 144A Individual Note Certificates (if any) issued in exchange for an interest in the Rule 144A Global Note Certificate will bear a legend to the following effect, unless the Borrower, the Bank and the Trustee determine otherwise in accordance with applicable law:

THE NOTES REPRESENTED HEREBY HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933 (THE “SECURITIES ACT”) OR ANY SECURITIES LAW OF ANY STATE OF THE UNITED STATES. THE HOLDER HEREOF, BY PURCHASING THE NOTES REPRESENTED HEREBY, AGREES FOR THE BENEFIT OF BAYERISCHE HYPO-UND VEREINSBANK A.G. (THE “ISSUER”) THAT THE NOTES REPRESENTED HEREBY MAY BE REOFFERED, RESOLD, PLEDGED OR OTHERWISE TRANSFERRED ONLY IN COMPLIANCE WITH THE SECURITIES ACT AND OTHER APPLICABLE LAWS AND ONLY (1) PURSUANT TO RULE 144A UNDER THE SECURITIES ACT TO A PERSON THAT THE HOLDER REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER WITHIN THE MEANING OF RULE 144A PURCHASING FOR ITS OWN ACCOUNT OR A PERSON PURCHASING FOR THE ACCOUNT OF A QUALIFIED INSTITUTIONAL BUYER WHOM THE HOLDER HAS INFORMED, IN EACH CASE, THAT THE REOFFER, RESALE, PLEDGE OR OTHER TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A UNDER THE SECURITIES ACT, (2) IN AN OFFSHORE TRANSACTION IN ACCORDANCE WITH RULE 903 OR 904 OF REGULATIONS UNDER THE SECURITIES ACT OR (3) PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT PROVIDED BY RULE 144 THEREUNDER (IF AVAILABLE).

IF THIS NOTE CERTIFICATE IS REGISTERED IN THE NAME OF CEDE & CO. (OR SUCH OTHER PERSON AS MAY BE NOMINATED BY THE DEPOSITORY TRUST COMPANY (“DTC”) FOR THE PURPOSE) (COLLECTIVELY, “CEDE & CO.”) AS NOMINEE FOR DTC, THEN, UNLESS THIS NOTE CERTIFICATE IS PRESENTED BY AN AUTHORIZED REPRESENTATIVE OF DTC TO THE ISSUER OR ITS AGENT FOR REGISTRATION OR TRANSFER, EXCHANGE OR PAYMENT AND ANY NOTE CERTIFICATE ISSUED UPON REGISTRATION OF TRANSFER OR EXCHANGE OF THIS NOTE CERTIFICATE IS REGISTERED IN THE NAME OF CEDE & CO. (OR SUCH OTHER NAME AS MAY BE REQUESTED BY AN AUTHORIZED REPRESENTATIVE OF DTC) AND ANY PAYMENT HEREUNDER IS MADE TO CEDE & CO. (OR, AS THE CASE MAY BE, SUCH OTHER PERSON), ANY TRANSFER, PLEDGE OR OTHER USE HEREOF FOR VALUE OR OTHERWISE BY OR TO ANY PERSON IS WRONGFUL, SINCE THE REGISTERED OWNER HEREOF, CEDE & CO. (OR, AS THE CASE MAY BE, SUCH OTHER PERSON), HAS AN INTEREST HEREIN.

The Borrower, the Bank, the Trustee, the Managers and their affiliates and others will rely on the truth and accuracy of the foregoing acknowledgements, representations and agreements. If it is acquiring any Notes for the account of one or more qualified institutional buyers, the purchaser represents that it has sole investment discretion with respect to each such account and that it has full

power to make the foregoing acknowledgements, representations and agreements on behalf of each such account.

Each purchaser and beneficial owner understands and acknowledges that its purchase and holding of such Notes constitutes a representation and agreement by it that for so long as it holds the Note or any interest therein either (a) it is not and will not be a benefit plan investor (as defined in 29 C.F.R. Section 2510.3-101) or any entity whose assets are treated as assets of a benefit plan investor or (b) it is a benefit plan investor and (i) its purchase and holding of the Note (or any interest in the Note) will not result in any prohibited transaction under Section 406 of the U.S. Employee Retirement Income Security Act of 1974, as amended (“ERISA”), or Section 4975 of the U.S. Internal Revenue Code of 1986, as amended (the “Code”), or a violation of any similar Federal, State or local law, (ii) if it is subject to Title I of ERISA or Section 4975 of the Code, the relief provided under one or more of Prohibited Transaction Class Exemption 84-14, 96-23, 95-60, 91-38 or 90-1 will apply to the acquisition and holding of the Note (or any interest in the Note), and (iii) if it is subject to ERISA, its purchase and holding of the Note (or any interest in the Note) will not cause the Issuer to be in violation of Section 412 of ERISA. Further, each purchaser and beneficial owner understands and acknowledges that it will not sell or otherwise transfer the Note or any interest therein to any person without first obtaining these same foregoing representations, warranties and covenants from that person.

Notes Sold Pursuant to Regulation S

Each purchaser (not including the Managers who are the initial purchasers) of Notes outside the United States pursuant to Regulation S, and each subsequent purchaser of such Notes in resales during the period which expires on and includes the 40th day after the later of the commencement of the offering of the Notes and the closing date (the “Distribution Compliance Period”), as certified by the Joint Lead Managers, will be deemed to have represented, agreed and acknowledged as follows:

- (i) it understands that the Notes, while represented by the Regulation S Global Note Certificate or if issued in exchange for an interest in the Regulation S Global Note Certificate or for Individual Note Certificates so issued, will bear a legend to the following effect:

THIS NOTE HAS NOT BEEN AND WILL NOT BE REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933 (THE “SECURITIES ACT”). THIS NOTE MAY NOT BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED WITHIN THE UNITED STATES OR TO OR FOR THE ACCOUNT OR BENEFIT OF ANY U.S. PERSON EXCEPT PURSUANT TO AN EXEMPTION FROM, OR IN A TRANSACTION NOT SUBJECT TO, THE REGISTRATION REQUIREMENTS OF THE U.S. SECURITIES ACT OF 1933, AS AMENDED.
- (ii) it is, or at the time the Notes are purchased will be, the beneficial owner of such Notes and (A) it is not a U.S. Person and it is purchasing such Notes in an offshore transaction (within the meaning of Regulation S) and (B) it is not an affiliate of the Bank or the Borrower or a person acting on behalf of such an affiliate;
- (iii) none of the Borrower, the Bank, the managers or any person representing any such entity has made any representation to it with respect to any such entity or the offering or sale of any Notes, other than the information in this Offering Circular;
- (iv) it understands that such Notes have not been and will not be registered under the Securities Act and that, prior to the expiration of the Distribution Compliance Period, it will not offer, sell, pledge or otherwise transfer such Notes except outside the United States in accordance with Rule 903 or Rule 904 of Regulation S;
- (v) the Borrower, the Bank, the Trustee, the Registrar, the Managers and their affiliates and others will rely upon the truth and accuracy of the foregoing acknowledgements, representations and agreements; and
- (vi) it understands and acknowledges that its purchase and holding of such Notes constitutes a representation and agreement by it that by its purchase and holding of such Notes or any interest therein, the purchaser and/or holder thereof and each transferee will be deemed to have represented and warranted at the time of its purchase and throughout the period that it holds the Note or any interest therein that either (a) it is not a benefit plan investor (as defined in 29 C.F.R. Section 2510.3-101) or any entity whose assets are treated as assets of any benefit plan investor or (b) it is a benefit plan investor and (i) its purchase and holding

of the Note (or any interest in the Note) will not result in any prohibited transaction under Section 406 of ERISA or Section 4975 of the Code or a violation of any Federal, State or local law, (ii) if it is subject to ERISA or Section 4975 of the Code, the relief provided under one or more of Prohibited Transaction Class Exemption 84-14, 96-23, 95-60, 91-38 or 90-1 will apply to the acquisition and holding of the Note (or any interest in the Note), and (iii) if it is subject to ERISA, its purchase and holding of the Note (or any interest in the Note) will not cause the Issuer to be in violation of Section 412 of ERISA. Further, each purchaser and/or holder and each transferee will be deemed to have represented and warranted that it will not sell or otherwise transfer the Note or interest therein to any person without first obtaining these same foregoing representations, warranties and covenants from that person.

Exchange of Interests in Global Note Certificates for Individual Note Certificates

Exchange of interests in Notes represented by the Rule 144A Global Note Certificate, in whole but not in part, for Notes represented by individual note certificates in individual form (the “Rule 144A Individual Note Certificates”) will not be permitted unless (i) DTC or a successor depository notifies the Bank that it is no longer willing or able to discharge properly its responsibilities as depository with respect to the Rule 144A Global Note Certificate or ceases to be a “clearing agency” registered under the Exchange Act, or is at any time no longer eligible to act as such, and the Bank is unable to locate a qualified successor within 90 days of receiving notice of such ineligibility or cessation on the part of such depository, (ii) following a failure to pay an amount in respect of any Notes within five days of the date on which such amount became due and payable in accordance with the Conditions or (iii) the Borrower or the Bank would suffer a material disadvantage in respect of the Notes as a result of a change in the laws or regulations which would not be suffered were the Notes evidenced by Restricted Note Certificates.

Exchange of interests in Notes represented by the Regulation S Global Note Certificate, in whole but not in part, for Notes represented by individual note certificates in individual form (the “Regulation S Individual Note Certificates”, and, together with the Rule 144A Individual Note Certificates, the “Individual Note Certificates”) will not be permitted unless (i) Euroclear or Clearstream, Luxembourg is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business or does in fact do so, (ii) following a failure to pay an amount in respect of any Notes within five days of the date on which such amount became due and payable in accordance with the Conditions or (iii) we or the Bank would suffer a material disadvantage in respect of the Notes as a result of a change in the laws or regulations which would not be suffered were the Notes evidenced by Regulation S Individual Note Certificates.

Exchange of interests in a Global Note Certificate, in whole or in part, for Individual Note Certificates may be made if instructions have been given for the transfer of an interest in such Global Note Certificate to a person who would otherwise take delivery thereof in the form of an interest in the other Global Note Certificate where such other Global Note Certificate has been exchanged for Note Certificates.

In such circumstances, the relevant Global Note Certificate shall be exchanged for Individual Note Certificates and the Bank will, at the cost of the Bank (to the extent reimbursed by us and against such indemnity as the Registrar or any relevant Transfer Agent or Paying Agent may require in respect of any tax or other duty of whatever nature which may be levied or imposed in connection with such exchange), cause sufficient Individual Note Certificates to be executed and delivered to the Registrar for completion, authentication and dispatch to the relevant noteholders in accordance with the Conditions. A person having an interest in a Global Note Certificate must provide the Bank and the Registrar with (i) a written order containing instructions and such other information as the Bank and the Registrar may require to complete, execute and deliver such Individual Note Certificates, and (ii) in the case of the Rule 144A Global Note Certificate only, a fully completed, signed certificate substantially to the effect that the exchanging holder is not transferring its interest at the time of such exchange or, in the case of a simultaneous sale pursuant to Rule 144A or Regulation S that the transfer is being made in compliance with the provisions of Rule 144A or Regulation S. Subject to the provisions of the Agency Agreement, Individual Note Certificates issued in exchange for a beneficial interest in the Rule 144A Global Note Certificate shall bear the legends as set out above under “– Transfer Restrictions”.

The beneficial owner of a Note, represented by an Individual Note Certificate, may transfer such Note in accordance with the provisions of the Trust Deed.

Upon the transfer, exchange or replacement of a Rule 144A Individual Note Certificate bearing the legend referred to under “–Transfer Restrictions,” or upon specific request for removal of the legend on a Rule 144A Individual Note Certificate, the Bank will deliver only Rule 144A Individual Note Certificates that bear such legend, or will refuse to remove such legend, as the case may be unless there is delivered to any Transfer Agents or Paying Agents a fully completed, signed certificate substantially to the effect that the transfer is being made in compliance with the provisions of Regulation S or Rule 144 (if applicable) or such evidence, which may include an opinion of counsel, as may reasonably be required by the Bank, that neither the legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the Securities Act.

Euroclear, Clearstream, Luxembourg and DTC Arrangements

So long as DTC or its nominee or Euroclear, Clearstream, Luxembourg or the nominee of their common depository is the registered holder of a Global Note Certificate, DTC, Euroclear, Clearstream, Luxembourg or such nominee, as the case may be, will be considered the sole owner or holder of the Notes represented by such Global Note Certificate for all purposes under the Agency Agreement and the Notes. Payments of principal, interest and Additional Amounts (if any) in respect of Global Note Certificates will be made to DTC, Euroclear, Clearstream, Luxembourg or such nominee, as the case may be, as the registered holder thereof. None of the Bank, us, the Trustee, any Transfer Agent or Paying Agent or any manager or any affiliate of any of them or any person by whom any of them is controlled for the purposes of the Securities Act will have any responsibility or liability for any aspect of the records relating to or payments made on account of beneficial ownership interests in Global Note Certificates or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.

Distributions of principal and interest with respect to book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg will be credited, to the extent received by Euroclear or Clearstream, Luxembourg from the Principal Paying Agent, to the cash accounts of Euroclear or Clearstream, Luxembourg customers in accordance with the relevant system’s rules and procedures.

Holders of book-entry interests in the Notes through DTC will receive, to the extent received by DTC from the Principal Paying Agent, all distributions of principal and interest with respect to book entry interests in the Notes from the Principal Paying Agent through DTC. Distribution in the United States will be subject to relevant United States tax laws and regulations.

Payments on the Notes will be paid to the holder shown on the Register on the fifteenth day before the due date for such payment so long as the Notes are represented by a Global Note Certificate, and on the fifteenth day before the due date for such payment if the Notes are in the form of Note Certificates (the “Record Date”).

The laws of some states of the United States require that certain persons take physical delivery of securities in individual form. Consequently, the ability to transfer interests in a Global Note Certificate to such persons may be limited. Because DTC, Euroclear and Clearstream, Luxembourg can only act on behalf of indirect participants, the ability of a person having an interest in a Global Note Certificate to pledge such interest to persons or entities which do not participate in the relevant clearing system, or otherwise take actions in respect of such interest, may be affected by the lack of a physical certificate in respect of such interest.

The holdings of book-entry interests in the Notes through DTC, Euroclear and Clearstream, Luxembourg will be reflected in the book-entry accounts of each such institution. As necessary, the Registrar will adjust the amounts of Notes on the Register for the accounts of (i) BT Globenet Nominees Limited, as common depository, and (ii) Cede & Co., to reflect the amounts of Notes held through Euroclear, Clearstream, Luxembourg and DTC, respectively. Beneficial ownership in the Notes will be held through financial institutions as direct and indirect participants in DTC, Euroclear and Clearstream, Luxembourg.

Beneficial interests in the Regulation S Global Note Certificate and the Rule 144A Global Note Certificate will be in uncertificated book-entry form.

Trading between Euroclear and Clearstream, Luxembourg Accountholders

Secondary market sales of book-entry interests in the Notes held through Euroclear or Clearstream, Luxembourg to purchasers of book-entry interests in the Notes through Euroclear or Clearstream, Luxembourg will be conducted in accordance with the normal rules and operating procedures of

Euroclear and Clearstream, Luxembourg and will be settled using the procedures applicable to conventional eurobonds.

Trading between DTC Participants

Secondary market sales of book-entry interests in the Notes between DTC participants will occur in the ordinary way in accordance with DTC rules and will be settled using the procedures applicable to United States corporate debt obligations in DTC's Same Day Funds Settlement System.

Trading between DTC Seller and Euroclear or Clearstream, Luxembourg Purchaser

When book-entry interests in Notes are to be transferred from the account of a DTC participant holding a beneficial interest in the Rule 144A Global Note Certificate to the account of a Euroclear or Clearstream, Luxembourg accountholder wishing to purchase a beneficial interest in the Regulation S Global Note Certificate (subject to such certification procedures as are provided in the Agency Agreement), the DTC participant will deliver instructions for delivery to the relevant Euroclear or Clearstream, Luxembourg accountholder to DTC by 12:00 noon, New York time, on the settlement date. Separate payment arrangements are required to be made between the DTC participant and the relevant Euroclear or Clearstream, Luxembourg accountholder, as the case may be. On the settlement date, the custodian will instruct the Registrar to (i) decrease the amount of Notes registered in the name of Cede & Co. and evidenced by the Rule 144A Global Note Certificate and (ii) increase the amount of Notes registered in the name of BT Globenet Nominees Limited, as common depositary, and evidenced by the Regulation S Global Note Certificate. Book-entry interests will be delivered free of payment to Euroclear or Clearstream, Luxembourg, as the case may be, for credit to the relevant accountholder on the first business day following the settlement date.

Trading between Euroclear or Clearstream, Luxembourg Seller and DTC Purchaser

When book-entry interests in Notes are to be transferred from the account of a Euroclear or Clearstream, Luxembourg accountholder holding a beneficial interest in the Regulation S Global Note Certificate to the account of a DTC participant wishing to purchase a beneficial interest in the Rule 144A Global Note Certificate (subject to such certification procedures as are provided in the Agency Agreement), the Euroclear or Clearstream, Luxembourg accountholder must send to Euroclear or Clearstream, Luxembourg delivery free of payment instructions by 7:45 p.m., Brussels or Luxembourg time, one business day prior to the settlement date. Euroclear or Clearstream, Luxembourg, as the case may be, will in turn transmit appropriate instructions to the common depositary for Euroclear and Clearstream, Luxembourg and the Registrar to arrange delivery to the DTC participant on the settlement date. Separate payment arrangements are required to be made between the DTC participant and the relevant Euroclear or Clearstream, Luxembourg accountholder, as the case may be. On the settlement date, the common depositary for Euroclear and Clearstream, Luxembourg will (i) transmit appropriate instructions to the custodian who will in turn deliver such book-entry interests in the Notes free of payment to the relevant account of the DTC participant and (ii) instruct the Registrar to (a) decrease the amount of Notes registered in the name of BT Globenet Nominees Limited, as common depositary, and evidenced by the Regulation S Global Note Certificate and (b) increase the amount of Notes registered in the name of Cede & Co. and evidenced by the Rule 144A Global Note Certificate.

Although the foregoing sets out the procedures of DTC, Euroclear and Clearstream, Luxembourg in order to facilitate the transfers of interests in the Notes among the participants of DTC, Euroclear and Clearstream, Luxembourg, none of DTC, Euroclear or Clearstream, Luxembourg is under any obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time. None of the Bank, us, the Trustee, any Agent or manager or any affiliate of any of them or any person by whom any of them is controlled for the purposes of the Securities Act, will have any responsibility for the performance by DTC, Euroclear or Clearstream, Luxembourg or their respective direct or indirect participants or accountholders of their respective obligations under the rules and procedures governing their operations or for the sufficiency for any purpose of the arrangements described above.

TAXATION

The following is a general description of certain tax considerations relating to the Notes. It does not purport to be a complete analysis of all tax considerations relating to the Notes. Prospective purchasers of Notes should consult their tax advisers as to the consequences, under the tax laws of the country of which they are resident for tax purposes, of a purchase of Notes, including but not limited to the consequences of receipt of interest and of sale or redemption of the Notes. This summary is based upon the law in effect on the date of this document and is subject to any change in law that may take effect after such date.

Ukrainian Tax Considerations

General

The following summary is included for general information only. Potential investors in and holders of the Notes should consult their own tax advisor as to the tax consequences under the laws of Ukraine of the acquisition, ownership and disposition of the Notes. This summary is based upon the Ukrainian tax laws and regulations as in effect on the date of this Offering Circular. Such laws and regulations are subject to change or varying interpretations, possibly with retroactive effect. As with other areas of Ukrainian legislation, tax law and practice in Ukraine is not as clearly established as that of more developed jurisdictions. It is possible, therefore, that the current interpretation of the law or understanding of the practice may change or that the law may be amended with retroactive effect. Accordingly, it is possible that payments to be made to holders of the Notes could become subject to taxation or that rates currently in effect with respect to such payments could be increased in ways that cannot be anticipated as of the date of this Offering Circular.

Withholding Tax on Interest Payments and Principal Repayments under the Loan

The Law of Ukraine “On Taxation of Profits of Enterprises”, dated 28 December 1994, as amended and restated (the “Profits Tax Law”), envisages that income of non-residents of Ukraine which are legal entities derived from sources in Ukraine in the form of interest payments is subject to 15 per cent. withholding tax. At the same time, paragraph 13.2 of Article 13 of the Profits Tax Law envisages that this withholding tax may be reduced or exempted by the provisions of an applicable effective tax treaty of Ukraine on the avoidance of double taxation.

Germany and Ukraine have entered into such a treaty, signed on July 3, 1995, effective on October 4, 1996 (the “Double Taxation Treaty”), pursuant to which interest payments are subject to a 2 per cent. withholding tax on the gross amount of interest payments made by a Ukrainian borrower to a German bank or any other German financial institution on any loan of whatever kind, provided that such bank or financial institution is the beneficial owner of the interest payments being received in Germany.

While the City believes the Bank will be treated as the beneficial owner of the income in question under Article 11 of the Double Taxation Treaty, the notion of beneficial ownership is not well defined, either in Ukrainian or international law. As a consequence, different interpretations are possible and the position could be taken that the Bank should not be viewed as the beneficial owner of the interest payments being received in Germany. However, the City believes that it is unlikely that the Ukrainian authorities will adopt this view. See “Risk Factors—Risks Associated with the Notes—Interest payments under the Loan may not qualify for the reduced rate of withholding tax under the applicable double taxation treaty”.

Applicable Ukrainian legislation allows upfront relief under the Double Taxation Treaty when the German recipient provides the Ukrainian borrower with a tax residence certificate in the prescribed form, confirming the fact that the recipient of interest is a resident of Germany for purposes of the Double Taxation Treaty. The obtaining of this upfront relief does not require the payee or payor to apply for and/or obtain any transaction-specific prior clearance from the Ukrainian tax authorities. Instead, the Ukrainian payor directly applies the reduced rate of withholding tax under the Double Taxation Treaty, provided that it has received the necessary documentation from the recipient on or prior to the date of payment of the Ukrainian source income. Therefore, when making interest payments to the Bank under the Loan Agreement, the City will directly apply the 2 per cent. withholding tax rate under the Double Taxation Treaty, provided that the City has received from the Bank the tax residency certificate, renewable on an annual basis, on or prior to the date of payment, subject to the reservation mentioned above.

The Profits Tax Law does not expressly exempt principal repayments from Ukrainian withholding tax. More specifically, paragraph 13.1 of Article 13 of the Profits Tax Law contains a “catch-all” provision, under which “other income of a non-resident (a permanent establishment of such or other non-resident) from carrying out business activity on the territory of Ukraine” is subject to a 15 per cent. withholding tax, established by paragraph 13.2 of Article 13 of the Profits Tax Law. Absent a definition of “income” in the Profits Tax Law, there is a remote risk that the repayment of principal under the Loan Agreement may be regarded as Ukrainian-source income of the Bank and, as such, subject to Ukrainian withholding tax at the rate of 15 per cent. Based on the professional advice it has received, the City is unaware of any situation in which the Ukrainian tax authorities have ever attempted to levy Ukrainian withholding tax on repayments of principal under a loan or credit transaction.

Consequences of Ukrainian Withholding

If any payments (including payments of interest) under the Loan Agreement are subject to any withholding tax (as a result of which the Bank would reduce payments under the Notes in the amount of such withholding), the City may, in certain circumstances specified in the Loan Agreement and subject to certain exceptions relating to the maintenance by the Bank of its residence in a qualifying jurisdiction, become obliged to pay such additional amounts as may be necessary so that the net payments received by the Bank will not be less than the amount the Bank would have received in the absence of such withholding tax.

The payment of gross up amount of 2 per cent. above the interest payments as a compensation for the withholding tax paid in Ukraine can be viewed as a payment not equivalent to interest payment under the Double Taxation Treaty and the applicable Ukrainian tax law. As a result, it can be argued that a different tax rate should be applied for the payment of the withholding tax on such gross up amount. The Ukrainian tax authorities have not challenged this position so far, but it is not clear how such payments will be viewed in the future.

While there is doubt as to whether the tax gross-up clause contained in the Loan Agreement is enforceable under Ukrainian law, a failure by the City to pay additional amounts due under the Loan Agreement would be a default under the Loan Agreement. Also, in the event that the City would become obliged to pay such additional amounts (other than in respect of applicable withholding tax at a rate of up to 2 per cent.), the City may prepay the Loan at its principal amount, together with accrued interest, and thereupon (subject to receipt of the relevant funds from the City) all outstanding Notes will be prepaid by the Bank.

Notwithstanding the foregoing, Articles 16.14 and 18.2 of the Profit Tax Law prohibit contractual provisions requiring one party to pay tax on behalf of another party. Absent any official interpretations or guidance on whether such restriction would apply to the City’s tax gross-up obligations, the tax gross-up provisions of the Loan Agreement and of other financing documents to which the City is a party may be deemed invalid and unenforceable under Ukrainian law.

Tax on Issue of and Interest Payments under the Notes

No Ukrainian withholding tax will be applicable to the issue of the Notes or interest payments on the Notes because the Notes will not be issued by the City or from Ukraine and interest payments on the Notes will not be made by the City or from Ukraine.

Tax on Payment of Instalments of Principal and on Redemption of Notes

The amount received by a non-resident as the result of the repayment of principal under a loan is not treated as the non-resident’s income derived from any sources in Ukraine. Therefore, it should not be subject to taxation in Ukraine and, consequently, no withholding tax shall be applied.

Principal payments on redemption of the Notes will not be subject to Ukrainian taxation because such payments will not be made either to or by a Ukrainian borrower (i.e., the City), nor will there be any guarantee of any payments under the Notes by a Ukrainian borrower (i.e., the City).

Ukrainian Holders

A Ukrainian resident Noteholder, i.e., an individual resident in Ukraine for a period of 183 days and more in a given calendar year or qualifying as a Ukrainian tax resident individual on any other ground, or a legal entity established under Ukrainian law, is subject to all applicable Ukrainian taxes. Interest from the holding of debt securities is included into the taxable income of a resident taxpayer, while the principal amount generally is not treated as a taxable income of such persons.

Transfers of Notes by Non-Ukrainian Investors to Ukrainian Investors

Ukrainian-source profits of non-residents derived from trading securities are generally subject to 15 per cent. withholding tax, as may be reduced by an applicable treaty on the avoidance of double taxation. Under the Ukrainian personal income tax legislation, Ukrainian-source income of non-resident physical persons will, subject to certain exceptions, be subject to withholding tax at a rate which is twice the then applicable rate of individual income tax, i.e., 26% for non-resident physical persons. However, the general rate of 13% personal income tax will apply to such Ukrainian-source income of a non-resident individual received as interest income.

Non-resident Noteholders are, therefore, likely to be subject to Ukrainian withholding tax on any gain (or the gross amount of the proceeds if the gain cannot be quantified) on the disposal of Notes where the proceeds of such disposal are received from a source within Ukraine.

Finally, there is some uncertainty as to whether the Notes would be considered “securities” under the Law of Ukraine “On Securities and Stock Exchange”, dated 18 June 1991, as amended and restated. An interpretation that the Notes are not securities under such legislation would, in principle, exempt the Notes from Ukrainian withholding tax by virtue of an applicable exemption in the Profits Tax Law.

German Tax Considerations

General

The following is a general discussion of certain German income tax consequences of the acquisition, ownership and disposition of the Notes to original purchasers of the Notes. This summary is based on the laws currently in force and as applied in practice on the date of this offering circular, which are subject to change, possibly with retroactive effect.

The information provided below does not purport to be a complete, exhaustive or final summary of the tax law and practice currently applicable in the Federal Republic of Germany. Prospective purchasers of the Notes are advised to consult their own tax advisors as to the German or other tax consequences of the purchase, ownership and disposition of the Notes in light of their particular circumstances, including the effect of any state, local or other national laws.

Resident Holders

Noteholders whose residence, customary place of abode or, in case the Noteholder is a corporation, seat or place of management is in Germany (resident holders) are subject to an unlimited tax liability in Germany. Interest income (including “Accrued Interest” (*Stückzinsen*) stemming from a sale or a redemption of the Notes) earned by resident holders from the Notes is taxable as income from capital investment pursuant to section 20 of the German Income Tax Act (*Einkommensteuergesetz – EStG*). In case the Notes are held as business assets, however, the interest income is taxable as business income according to section 20 para. 3 and 15 para. 1 EStG.

The interest income from the Notes is, in principle, subject to German income tax (*Einkommensteuer*) or German corporate income tax (*Körperschaftsteuer*), both plus solidarity surcharge thereon (*Solidaritätszuschlag*). Additionally trade tax (*Gewerbesteuer*) will become due if the Notes are held by a trade business (including partnerships which run a trade business) located in Germany.

If the Notes are held in custodial account by a German credit institution or financial services institution (“Disbursing Agent”) (which term includes a German branch of a foreign credit or financial services institution (including the Issuer but excludes a foreign branch of a German credit or financial services institution)), interest payments and Accrued Interest in respect of the Notes is subject to a 30.0 per cent. withholding tax (*Zinsabschlagsteuer*) and a 5.5 per cent. solidarity surcharge thereon. As a result, such payments are subject to a total withholding tax charge of 31.65 per cent.

If interest is paid by a Disbursing Agent upon physical presentation of the Notes or coupons, if any (so-called “over-the-counter” (OTC) transaction), the withholding tax rate is 35.0 per cent. plus 5.5 per cent. solidarity surcharge thereon, leading to an aggregate tax burden of 36.93 per cent. The withholding tax and solidarity surcharge withheld from such payments is credited as prepayment against the personal income tax or corporate income tax bill (including the respective solidarity surcharge) of the Noteholder.

Individuals are entitled to a tax-free allowance for investment income not resulting from business assets according to section 20 para. 4 *EStG*. The amount of interest received that can be excluded from taxable income is EUR 1,370 (EUR 2,740 for married couples) for all investment income (interest on bonds, interest on bank deposits, dividends etc.). In combination with the lump-sum

deduction for investment expenses (section 9a sentence 1 no. 2 *ESiG*), the amount excludible from taxable income amounts to EUR 1,421 (EUR 2,842 for married couples). However, these allowances only apply to investment income not resulting from business assets. For commercial corporate taxpayers income from the interest on the Notes does not qualify as investment income but as business income; thus the allowances for investment income are not granted.

In case Notes do not qualify as business assets, capital gains, if any, realised in respect of the Notes are not subject to income tax unless the Notes are sold within one year of acquisition or issuance. The German tax authorities might take the view that a capital gain realised from a redemption of the Notes within a period of one year after acquisition or issuance is subject to tax. Capital gains realised in respect of Notes held as business assets are, however, subject to income or corporate income tax (plus solidarity surcharge thereon) and trade tax. The capital gain on any disposal of the Notes is, in principle, calculated as the difference between the disposal price of the relevant Note and its acquisition cost.

German withholding tax will not be levied on capital gains deriving from the sale or redemption of the Notes.

However, if the Notes should be classified as a financial innovation (*Finanzinnovation*) within the meaning of the German Income Tax Act (which term includes, *inter alia*, discount notes, zero-coupon notes and floating rate notes), an amount equal to the difference between the issue or purchase price and the sales price or redemption amount to the extent attributable to the period over which the Noteholder has held such Notes (*Emissionsrendite*) or, alternatively, the difference between the proceeds from a sale or redemption and the purchase price or issue price of the notes (*Marktrendite*) will be subject to personal income tax or corporate income tax (in both cases plus solidarity surcharge thereon) as deemed interest income (“Deemed Interest”). In addition, where the Notes are held in custodial account by a Disbursing Agent an amount equal to the difference between issue or purchase price and the redemption amount or sales proceeds will be subject to withholding tax (plus solidarity surcharge thereon, i.e. 31.65 per cent. respectively 36.93 per cent. in aggregate as described above) if the Notes have been held in custodial account by such Disbursing Agent since the time of acquisition or issuance, respectively. Otherwise withholding tax and solidarity surcharge will apply at the rate described above calculated on a lump-sum basis of 30.0 per cent. of the proceeds received for partial or final redemption or sale of the Notes.

Non-Resident Holders

Noteholders whose residence, customary place of abode or, in case the Noteholder is a corporation, seat or place of management is outside Germany (non-resident holders) are subject to a limited tax liability in Germany with income deriving from German sources. In particular income earned through a German “Permanent Establishment” (which term shall include a fixed place of business in Germany or a German permanent representative) has to be considered as income from German sources. The same applies to income earned through a direct investment of non-resident holders in a German partnership, which carries out a trade business in Germany. As a result, interest income from the Notes is either subject to German income tax or (in case the Noteholder is established as a corporation) German corporate income tax, both plus solidarity surcharge thereon. Additionally, German trade tax will become due.

Interest payments earned by non-resident holders are in general exempt from German withholding tax (and solidarity surcharge thereon). An exemption applies if either the Notes form part of a German Permanent Establishment or the interest payments, including Accrued Interest and Deemed Interest, are effected upon an OTC transaction.

Capital gains realised by non-resident holders from a sale or other disposal or redemption of Notes that are not held as business assets of a Permanent Establishment in Germany are not subject to tax in Germany.

Inheritance and Gift Tax

A transfer of the Notes as a gift or by reason of death is subject to German inheritance or gift tax (*Erbschaftoder Schenkungsteuer*), if the Noteholder, or the heir, donee or other beneficiary is a German resident (*Inländer*) for German inheritance or gift tax purposes. In particular, (i) individuals with a residence or customary place of abode in Germany, corporations with a seat or place of management in Germany and German citizens without a residence in Germany who have not permanently stayed outside Germany for more than five years, qualify as German residents for such purposes, while (ii) German citizens without a residence in Germany who have not permanently stayed outside Germany

for more than ten years are subject to an extended limited tax liability. A transfer of the Notes as a gift or by reason of death is not subject to German inheritance or gift tax, if neither the Noteholder nor the heir, donee or other beneficiary is a German resident and the Notes do not constitute German located property. If a transfer of Notes triggers inheritance or gift tax, personal allowances are granted, among other things to spouses (EUR 307,000) and to children (EUR 205,000). The tax rate depends, among other things, on the degree of the relationship between the decedent/donor and the heir, donee or other beneficiary and on the tax value of the transferred assets.

Other Taxes

No stamp, issue, registration, or similar taxes or duties will be payable in Germany in connection with the issuance, delivery or execution of the Notes.

United States Federal Income Taxation Considerations

The following is a summary of the material U.S. federal income tax consequences of the acquisition, ownership and retirement or other disposition of Notes by a holder thereof and payments under the Loan. This summary applies only to Notes held as capital assets and does not address aspects of U.S. federal income taxation that may be applicable to holders that are subject to special tax rules, such as financial institutions, insurance companies, real estate investment trusts, regulated investment companies, grantor trusts, tax-exempt organisations, dealers or traders in securities or currencies or to holders that will hold a Note as part of a position in a “straddle” or as part of a “hedging,” “conversion” or “integrated” transaction for U.S. federal income tax purposes or that have a “functional currency” other than the U.S. dollar. Moreover, this summary does not address the U.S. federal estate and gift or alternative minimum tax consequences of the acquisition, ownership or retiring of Notes and does not address the U.S. federal income tax treatment of holders that do not acquire Notes as part of the initial distribution at the initial issue price. Each prospective purchaser should consult its tax advisor with respect to the U.S. federal, state, local and foreign tax consequences of acquiring, holding and retiring of Notes.

This summary is based on the U.S. Internal Revenue Code of 1986, as amended, administrative pronouncements, judicial decisions and existing and proposed U.S. Treasury Regulations, in each case, as available and in effect on the date hereof. All of the foregoing are subject to change or differing interpretation, which could apply retroactively and affect the tax consequences described herein.

For purposes of this summary, a “U.S. Holder” is a beneficial owner of Notes who, for U.S. federal income tax purposes, is (i) a citizen or resident of the United States; (ii) a corporation or partnership organised in or under the laws of the United States or any state or political subdivision thereof (including the District of Columbia); (iii) an estate the income of which is subject to U.S. federal income taxation regardless of its source; or (iv) a trust (1) that validly elects to be treated as a United States person for U.S. federal income tax purposes or (2) (a) over the administration of which a U.S. court can exercise primary supervision and (b) all of the substantial decisions of which one or more United States persons have the authority to control. If a partnership (or any other entity treated as a partnership for U.S. federal income tax purposes) holds Notes, the tax treatment of the partnership and a partner in such partnership will generally depend on the status of the partner and the activities of the partnership. Such a partner or partnership should consult its own tax advisor as to its consequences. A “Non-U.S. Holder” is a beneficial owner of Notes other than a U.S. Holder.

Interest

Interest paid on a Note or under the Loan (including any Additional Amounts) will be included in a U.S. Holder’s gross income as ordinary interest income in accordance with the U.S. Holder’s usual method of tax accounting. In addition, interest on the Notes or under the Loan will be treated as foreign source income for U.S. federal income tax purposes. Prospective purchasers should consult their tax advisers concerning the applicability of the foreign tax credit and source of income rules to income attributable to the Notes.

Subject to the discussion below under the caption “U.S. Backup Withholding Tax and Information Reporting,” payments of interest on a Note or under the Loan to a Non-U.S. Holder generally will not be subject to U.S. federal income tax unless such income is effectively connected with the conduct by such Non-U.S. Holder of a trade or business in the United States.

Sale, Exchange or Retirement

Upon the sale, exchange or retirement of a Note, a U.S. Holder will recognise taxable gain or loss equal to the difference, if any, between the amount realised on the sale, exchange or retirement (other than amounts attributable to accrued but unpaid interest, which will be taxable as such) and the U.S.

Holder's adjusted tax basis in such Note. A U.S. Holder's adjusted tax basis in a Note generally will equal the U.S. dollar cost of such Note to the U.S. Holder. Any such gain or loss will be capital gain or loss and will be long-term capital gain or loss if such U.S. Holder's holding period for such Notes exceeds one year. Any gain or loss realized on the sale, exchange or retirement of a Note generally will be treated as U.S. source gain or loss, as the case may be. The deductibility of capital losses is subject to limitations. Prospective purchasers should consult their tax advisers as to the foreign tax credit implications of the sale or retirement of the Notes.

Subject to the discussion below under "—U.S. Backup Withholding Tax and Information Reporting," any gain realized by a Non-U.S. Holder upon the sale, exchange or retirement of a Note generally will not be subject to U.S. federal income tax, unless (i) such gain is effectively connected with the conduct by such Non-U.S. Holder of a trade or business in the United States or (ii) in the case of any gain realized by an individual Non-U.S. Holder, such holder is present in the United States for 183 days or more in the taxable year of such sale, exchange or retirement and certain other conditions are met.

U.S. Backup Withholding Tax and Information Reporting

Backup withholding tax and information reporting requirements apply to certain payments of principal of, and interest on, an obligation and to proceeds of the sale or redemption of an obligation, to certain non-corporate holders of Notes that are United States persons. Information reporting generally will apply to payments by a U.S. paying agent or other U.S. intermediary of principal of, and interest on, an obligation, and to proceeds from the sale or redemption of, an obligation made within the United States to a holder (other than an exempt recipient, including a corporation, a payee that is not a United States person that provides an appropriate certification and certain other persons). The payor will be required to withhold backup withholding tax from any such payment within the United States on a Note or under the Loan to a holder of a Note that is a United States person (other than an "exempt recipient," such as a corporation) if such holder fails to furnish its correct taxpayer identification number or otherwise fails to comply with, or establish an exemption from, such backup withholding requirements. Payments within the United States of principal and interest to a holder of a Note that is not a United States person will not be subject to backup withholding tax and information reporting requirements if an appropriate certification is provided by the holder to the payor and the payor does not have actual knowledge or a reason to know that the certificate is incorrect. The backup withholding tax rate is 28 per cent. for years 2004 through 2010. Holders should consult their tax advisers as to their qualification for exemption from backup withholding and the procedure for obtaining an exemption.

In the case of payments to a foreign simple trust, a foreign grantor trust or a foreign partnership, other than payments to a foreign simple trust, a foreign grantor trust or foreign partnership that qualifies as a withholding foreign trust or a withholding foreign partnership within the meaning of the applicable U.S. Treasury Regulations and payments to a foreign simple trust, a foreign grantor trust or a foreign partnership that are effectively connected with the conduct of a trade or business in the United States, the beneficiaries of the foreign simple trust, the persons treated as the owners of the foreign grantor trust or the partners of the foreign partnership, as the case may be, will be required to provide the certification discussed above in order to establish an exemption from backup withholding tax and information reporting requirements. Moreover, a payor may rely on a certification provided by a payee that is not a United States person only if the payor does not have actual knowledge or a reason to know that any information or certification stated in the certificate is incorrect.

SUBSCRIPTION AND SALE

Deutsche Bank Securities Inc. and Morgan Stanley & Co. International Limited (the “Joint Lead Managers”), Open Joint Stock Company Commercial Bank “Khreschatyk”, Bayerische Hypo- und Vereinsbank AG and Parex Bank (the “Managers”) have, in a subscription agreement dated 15 July 2004 (the “Subscription Agreement”) and made between the Issuer, the Borrower and the Managers upon the terms and subject to the conditions contained therein, jointly and severally agreed to subscribe and pay for the Notes at their issue price of 100 per cent. of their principal amount. The Borrower will pay to the Joint Lead Managers, for the account of the Managers, a combined management and underwriting commission and selling concession of 0.475 per cent. of their principal amount. The Borrower has also agreed to reimburse the Joint Lead Managers for certain of their expenses incurred in connection with the management of the issue of the Notes. The Managers are entitled in certain circumstances to be released and discharged from their obligations under the Subscription Agreement prior to the closing of the issue of the Notes.

United States of America

The Notes and Loan have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in certain transactions exempt from or not subject to the registration requirements of the Securities Act. Accordingly, the Managers have agreed to offer the Notes for resale initially only to persons they reasonably believe to be qualified institutional buyers in reliance on Rule 144A under the Securities Act and outside the United States in offshore transactions in reliance on Regulation S under the Securities Act. See “Form of Notes and Transfer Restrictions”.

Each Manager has represented, warranted and agreed that, except as permitted by the Subscription Agreement, it will not offer, sell or deliver the Notes, (a) as part of their distribution at any time or (b) otherwise until 40 days after the later of the commencement of the offering and the issue date of the Notes, within the United States or to, or for the account or benefit of, U.S. persons, and that it will have sent to each dealer to which it sells Notes in reliance on Regulation S during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Notes within the United States or to, or for the account or benefit of, U.S. persons. Terms used in this and the preceding paragraph have the meanings given to them by Regulation S.

Notes offered and sold outside the United States to non-U.S. persons may be sold in reliance on Regulation S. The Subscription Agreement provides that the Managers may directly or through their respective U.S. broker-dealer affiliates arrange for the offer and resale of Notes in the United States only to persons whom they reasonably believe are QIBs within the meaning of Rule 144A.

In addition, until 40 days after commencement of the offering, an offer or sale of Notes within the United States by a dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act if such offer or sale is made other than in accordance with Rule 144A under the Securities Act.

This Offering Circular has been prepared by the Issuer for use in connection with the offer and sale of the Notes outside the United States, the resale of the Notes in the United States and for the admission of Notes to the Luxembourg Stock Exchange. The Issuer and the Managers reserve the right to reject any offer to purchase the Notes, in whole or in part, for any reason. This Offering Circular does not constitute an offer to any person in the United States or to any U.S. person (other than a QIB) and to whom an offer has been made directly by one of the Managers or its U.S. broker-affiliate. Distribution of this Offering Circular by any non-U.S. person outside the United States or by any QIB in the United States to any person other than a QIB and other than to those persons, if any, retained to advise such non-U.S. person or QIB with respect thereto, is unauthorised and any disclosure without the prior written consent of the Issuer of any of its contents to any such person is prohibited.

United Kingdom

Each Manager has further represented, warranted and undertaken that:

- (a) *No offer to public*: It has not offered or sold and will not offer or sell any Notes to persons in the United Kingdom prior to the expiry of a period of six months from the issue date of such Notes except to persons whose ordinary activities involve them in acquiring, holding, managing

or disposing of investments (as principal or agent) for the purposes of their businesses or otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995;

- (b) *Financial Promotion*: It has only communicated or caused to be communicated, and will only communicate or cause to be communicated, any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 (the “FSMA”)) received by it in connection with the issue or sale of any Notes in circumstances in which section 21(1) of the FSMA does not apply to the Issuer; and
- (c) *General compliance*: It has complied with all applicable provisions of the FSMA with respect to anything done by it in relation to any Notes in, from or otherwise involving the United Kingdom.

Ukraine

Each Manager has agreed that the Notes shall not be offered by any of them for circulation, distribution, placement, sale, purchase or other transfer in the territory of Ukraine. Accordingly, nothing in this Offering Circular or any other documents, information or communications related to the Notes shall be interpreted as containing any offer or invitation to, or solicitation of, any such circulation, distribution, placement, sale, purchase or other transfer in the territory of Ukraine.

Germany

Each Manager has confirmed that it is aware of the fact that no German sales prospectus (*Verkaufsprospekt*) within the meaning of the Securities Sales Prospectus Act (*Wertpapier-Verkaufsprospektgesetz*, the “Act”) of the Federal Republic of Germany has been or will be published with respect to the Notes and that it will comply with the Act and any other laws and legal and regulatory requirements applicable in the Federal Republic of Germany with respect to the issue, sale and offering of securities, whether as part of their initial distribution or as part of any resale of the Notes in the secondary market. In particular, each of the Managers has represented that it has not engaged and has agreed that it will not engage in a public offering (*öffentliches Angebot*) within the meaning of the Act with respect to any Notes otherwise than in accordance with the Act.

Republic of Italy

Each Manager has agreed that no action has been or will be taken which would allow an offering of the Notes to the public in the Republic of Italy and that individual sales of the Notes to any person in the Republic of Italy have only been and will only be made in accordance with Italian securities, tax and other applicable laws and regulations. The Notes will not be registered with the *Commissione Nazionale per le Società e la Borsa* (“CONSOB”) (the Italian Securities Exchange Commission) pursuant to the Italian securities legislation and, accordingly, each Manager has represented and agreed that no Notes may be offered, sold or delivered, nor may copies of the Offering Circular or of any other document relating to the Notes be distributed in the Republic of Italy, except:

- (a) to professional investors (*operatori qualificati*) as defined in Article 31.2, second paragraph, of CONSOB Regulation No. 11522 of 1 July 1998, as amended; or
- (b) in circumstances which are exempted from the Rules on Solicitation of Investments pursuant to Article 100 of Legislative Decree No. 58 of 24 February 1998, (the “Financial Services Act”) and Article 33, first paragraph, of CONSOB Regulation No. 11971 of 14 May 1999, as amended.

Accordingly, each of the Managers has represented and agreed that any offer, sale or delivery of Notes or distribution of copies of the Offering Circular or of any other document relating to the Notes in the Republic of Italy under (a) or (b) above must be:

- (i) made by an investment firm, bank or financial intermediary permitted to conduct such activities in Italy in accordance with the Financial Services Act and Legislative Decree No. 385 of 1 September 1993 (the “Banking Act”);
- (ii) in compliance with Article 129 of the Banking Act and the implementing guidelines of the Bank of Italy, amended from time to time, pursuant to which the issue or the offer of securities in Italy may need to be preceded and followed by an appropriate notice to be filed with the Bank of Italy depending, *inter alia*, on the aggregate value of the securities issued or offered in the Republic of Italy and their characteristics; and
- (iii) in compliance with any other applicable laws and regulations.

In each case, each of the Managers has represented and agreed that the Notes will not be placed, sold or delivered, either in the primary or secondary market, to Italian resident individuals.

No action has been or will be taken in any jurisdiction by the Issuer, the Borrower or any Manager that would, or is intended to, permit a public offering of the Notes, or possession or distribution of this Offering Circular or any other offering material, in any country or jurisdiction where action for that purpose is required. Persons into whose hands this Offering Circular comes are required by the Issuer, the Borrower and the Managers to comply with all applicable laws and regulations in each country or jurisdiction in which they purchase, offer, sell or deliver Notes or have in their possession, distribute or publish this Offering Circular or any other offering material relating to the Notes, in all cases at their own expense.

CERTAIN ERISA AND OTHER CONSIDERATIONS

The U.S. Employee Retirement Income Security Act of 1974, as amended (“ERISA”) and the U.S. Internal Revenue Code of 1986, as amended (the “Code”) set forth certain restrictions on (a) an employee benefit plan (as defined in section 3(3) of ERISA), (b) a plan described in Section 4975(e)(1) of the Code, including an individual retirement account and a Keogh plan, (C) any entity whose underlying assets include plan assets by reason of a plan’s investment in such entity (each of (a), (b) and (c) hereinafter referred to as a “Plan” or “Benefit Plan”) and (d) a person who has certain specified relationships to such Plan (a “Party-in-Interest” under ERISA and a “Disqualified Person” under the Code). ERISA also imposes specific requirements on a fiduciary of a Benefit Plan subject to ERISA, namely, that he make prudent investments, that he diversify investments, and that he make investments in accordance with the Plan documents and in the best interests of participants and their beneficiaries. Each fiduciary of a plan should consider the fiduciary standards of ERISA in the context of the Plan’s particular circumstances before authorising an investment in the Notes. Accordingly, among other factors, the fiduciary should consider whether the investment would satisfy the prudence and diversification requirement of ERISA and would be consistent with the documents and instruments governing the Plan.

Further, Section 406 of ERISA and Section 4975 of the Code prohibit a Plan from engaging in certain transactions involving the Plan or Plan assets with Parties in Interest under ERISA or Disqualified Persons under the Code with respect to such Plan (a “Prohibited Transaction”). A violation of these Prohibited Transaction rules could occur upon the acquisition or holding of a Note by a Benefit Plan if the Bank, the Managers, the Trustee, the Principal Paying Agent, Registrar and Transfer Agent, the Borrower or the Listing Agent and Luxembourg paying and Transfer Agent, or any of their respective affiliates were a Party-in-Interest or a Disqualified Person with respect to such Plan.

Certain transactions contemplated in connection with the offering of the Notes could be deemed to constitute direct or indirect Prohibited Transactions under Section 406 of ERISA and Section 4975 of the Code with respect to a Benefit Plan. For example, if either the Bank or the City is a Party in Interest with respect of an investing Plan (either directly or indirectly by reason of its ownership of or its being owned by a Party in Interest to such Plan), extensions of credit either between the investing Plan and the Bank (as represented by the Notes) or between the Bank and the City (as evidenced by the Further Loan Agreement) may be deemed to constitute Prohibited Transactions under Section 406(a)(1)(B) of ERISA and Section 4975(c)(1)(B) of the Code, unless exemptive relief were available under an applicable Prohibited Transaction exemption. In addition, the purchase of Notes from a Manager by an investing Plan may constitute a prohibited sale or exchange between such Plan and such Manager by reason of Section 406(a)(1)(A) of ERISA and Section 4975(c)(1)(A) of the Code, unless exemptive relief were available under an applicable Prohibited Transaction exemption.

A Prohibited Transaction may result in an excise tax, penalty or other liabilities under ERISA and/or Section 4975 of the Code for such persons, unless exemptive relief is available under an applicable statutory, regulatory or administrative Prohibited Transaction exemption. Benefit Plans that are non-U.S. plans or governmental plans (as defined in Section 3(32) of ERISA) or certain church plans (as defined in Section 3(33) of ERISA) are not subject to the requirements of Title I of ERISA or Section 4975 of the Code. However, a governmental plan may be subject to federal, state or local laws that are similar to the provisions of Title I of ERISA or Section 4975 of the Code.

Any insurance company proposing to invest assets of its general account in the Notes should consider the implications of the U.S. Supreme Court’s decision in *John Hancock Mutual Life Insurance Co. v. Harris Trust and Savings Bank*, 510 U.S. 86 (1993), which, in certain circumstances, treats the assets of an insurance company’s general account as assets of Plans that own policies or other contracts with the insurance company, as well as the effect of Section 401(c) of ERISA as interpreted by a regulation issued by the U.S. Department of Labor (the “DOL”) in January 2000 (29 C.F.R. Section 2550.401c-1) and the extent to which exemptive relief under PTCE 95-60 will apply to such investment.

The Notes purchased and held by a Benefit Plan would be considered assets of that Benefit Plan. Fiduciaries of a Benefit Plan should also consider, however, whether a Benefit Plan investing in Notes is deemed to own also an undivided interest in the underlying Loan. Certain transactions involving the Loan might be deemed to constitute Prohibited Transactions with respect to a Benefit Plan if the underlying Loan were deemed to be “plan assets” of such Benefit Plan. In that case, those persons or entities providing services related to the Loan could be deemed to be “fiduciaries” under ERISA with respect to such Benefit Plan and could be required to comply with the ERISA fiduciary rules. Further,

certain transactions involving those persons or entities, and other transactions involving a Benefit Plan which acquires or holds Notes, could be deemed to be Prohibited Transactions.

The DOL has issued a regulation (the “Plan Assets Regulation”) setting forth the standards it will apply for determining what constitutes the assets of a Plan. Under the Plan Assets Regulation, if a Plan acquires an equity interest in an entity that is neither a “publicly offered security” (defined by reference to U.S. securities laws) nor a security issued by an investment company registered under the U.S. Investment Company Act of 1940, the Plan’s assets will include both the equity interest and an undivided interest in each of the underlying assets of the entity, unless it is established that: (i) the entity is an “operating company,” or (ii) equity participation in the entity by “Benefit Plan Investors” (as defined below) is not “significant”.

For these purposes, an “equity interest” is any interest in an entity other than an instrument that is treated as indebtedness under applicable local law and has no substantial equity features. Further, an “operating company” is an entity that is primarily engaged, directly or through a majority owned subsidiary or subsidiaries, in the production or sale of a product or service other than the investment of capital. The term “operating company” includes an entity which is a “venture capital operating company” and a “real estate operating company”, as such terms are defined in the Plan Assets Regulation. Equity participation by Benefit Plan Investors is “significant” on any date if, immediately after the most recent acquisition of any equity interest in the entity, 25 per cent. or more of the value of any class of equity interests in the entity is held by Benefit Plan Investors. For these purposes, a “Benefit Plan Investor” is defined to include: (a) any employee benefit plan (as defined in Section 3(3) of ERISA), whether or not it is subject to Title I of ERISA (including any non-U.S. plan), (b) any plan described in Section 4975(e)(1) of the Code, and (c) any entity whose underlying assets include plan assets by reason of a plan’s investment in the entity.

Because the Notes entitle the holder to a participation interest in the Loan, under the Plan Assets Regulation the Notes would likely be viewed as equity interests, not debt interests. As a result, unless an exception applies, a Benefit Plan’s investment will be deemed to include not only the Notes but also an undivided interest in the Loan. There can be no assurance that any of the exceptions set forth in the Plan Assets Regulation will apply to the purchase of Notes offered hereby.

Section 412 of ERISA requires that every fiduciary of an employee benefit plan and every person who handles funds or other property of such a plan be bonded at levels required under ERISA. Each purchaser of a Note (or any interest therein) that is a Benefit Plan will, by its purchase of such Note (or interest therein), be deemed to have represented and agreed that the transactions hereunder will not cause the issuer to be in violation of Section 412 of ERISA (either by coverage of the issuer under such investor’s applicable bond or otherwise). The Bank will not be procuring its own bond for these purposes.

Fiduciaries of Benefit Plans should also take into account the ERISA requirements set forth in 29 C.F.R. Section 2550.404b-1 (the “Indicia of Ownership Rules”), which provide that no fiduciary under ERISA may maintain the indicia of ownership of assets of a Benefit Plan outside the jurisdiction of the Federal district courts of the United States, except in certain cases involving non-U.S. securities and non-U.S. currency. In the event that the Loan is deemed to be a “plan asset” of a Benefit Plan, the fiduciaries of that Benefit Plan should consult with their legal advisors regarding whether the indicia of ownership of the Loan will satisfy the conditions set forth in the Indicia of Ownership Rules. Executed originals of the Loan Agreement will be held in the United States.

Because of the considerations discussed above, Notes may not be purchased or held by any Benefit Plan that is subject to Title I of ERISA or Section 4975 of the Code unless such purchaser or holder is eligible for the exemptive relief available under PTCE 96-23, 95-60, 91-38, 90-1 or 84-14. Any purchaser or holder of the Notes (or interest therein) and any subsequent transferee of a Note (or interest therein) will have or will be deemed to have represented that it either (a) is not a Benefit Plan and is not purchasing such Notes (or interest therein) on behalf of or with “plan assets” of any Benefit Plan and it will not be a Benefit Plan for so long as it holds such Notes (or interest therein) or (b) is a Benefit Plan or is purchasing the Notes (or interest therein) on behalf of or with “plan assets” of any Benefit Plan and (i) its purchase and holding of the Notes (or any interest therein) will not result in any prohibited transaction under Section 406 of ERISA or Section 4975 of the Code or a violation of any similar Federal, state or local law or (ii) it is eligible for the exemptive relief available under PTCE 96-23, 95-60, 91-38, 90-1 or 84-14 with respect to such purchase, holding, disposition or transfer and will continue to be eligible for such exemptive relief throughout the period

that it holds the Notes (or interest therein). For more information, see the section of this Offering Circular entitled “Form of Notes and Transfer Restrictions”.

Due to the complexity of these rules and the penalties that may be imposed upon persons involved in non-exempt Prohibited Transactions, it is particularly important that fiduciaries or other persons considering the acquisition of Notes by or on behalf of any Benefit Plan consult with their counsel regarding the potential consequences under ERISA or the Code of making an investment in the Notes. Further, each Benefit Plan fiduciary should determine that the acquisition and holding of a Note is consistent with its fiduciary duties under ERISA. The fiduciary of a Benefit Plan that is not subject to ERISA or Section 4975 of the Code proposing to invest in the Notes must make its own determination that such investment is permitted under applicable law.

GENERAL INFORMATION

1. The Notes represented by the Global Note Certificates have been accepted for clearance through DTC and Euroclear and Clearstream, Luxembourg. The International Securities Identification Number of the Regulation S Notes is XS0197093965 and the Common Code of the Regulation S Notes is 019709396. The International Securities Identification Number for the Rule 144A Notes is US072735AA17 and the CUSIP for the Rule 144A Notes is 072735AA1. In addition, application has been made for the Rule 144A Notes represented by the Rule 144A Global Note Certificate to be designated as eligible for trading on PORTAL.
2. In connection with the application for the Notes to be listed on the Luxembourg Stock Exchange, a copy of a legal notice relating to the issue of the Notes will be deposited prior to listing with the *Registre de Commerce et des Sociétés Luxembourg*, where it may be inspected and copies obtained upon request. So long as any of the Notes are listed on the Luxembourg Stock Exchange and the rules of the Luxembourg Stock Exchange shall so require, the Issuer will maintain a paying agent and transfer agent in Luxembourg. Copies (and English translations where the documents in question are not in English) of the following documents may be inspected at and are available from the Specified Offices of the Transfer Agent and the Paying Agent during normal business hours on any week day (Saturdays, Sundays and public holidays excepted) so long as any of the Notes are listed on the Luxembourg Stock Exchange:
 - (a) the Agency Agreement;
 - (b) the Trust Deed, which includes the forms of Global Note Certificates and Individual Note Certificates;
 - (c) copies in English of the latest annual City Budget, including the report on the execution of the 2003 City Budget and the preliminary report on the execution of the 2004 City Budget, together with any further amendments thereto;
 - (d) copies (with an English translation) of the authorisations listed in 3. below; and
 - (e) the Loan Agreement.
3. The Loan has been authorised and approved by the 2004 City Budget Resolution, as approved by the City Council's Resolution No. 267/1142 of 18 December 2003 and as amended by the City Council's Resolution No. 149/1359 of 15 April 2004 on Amendments to Resolution No. 267/1142 of the City Council on the 2004 City Budget of 18 December 2003. By Letter No. 31-05220-02-7/5705 dated 7 April 2004 and Letter No. 31-03220-03-21/12345 dated 9 July 2004, the Ministry of Finance approved the Loan. The City Council will adopt further resolutions approving certain amendments to Resolution No. 267/1142 of 18 December 2003 and ratifying the execution of the Loan Agreement by the City and the Loan Agreement will be registered with the NBU prior to the closing of the issue of the Notes.
4. The Issuer has obtained all necessary consents, approvals and authorisations in connection with the issue of the Notes. Specifically, the Issuer obtained the approval of its Head of EEMEA Origination and Corporate Sales on 23 June 2004.
5. Save as disclosed in this Offering Circular, since 31 December 2003 there has been no material adverse change or any development involving a prospective material adverse change in the sources and amounts of revenue of the City or in the proposed expenditure of the City, each as set out in the Budget Accounts, that is material in the context of the issue of the Notes. The 2004 City Budget consists of revenues and expenditures planned for 2004 as reflected in the 2004 City Budget Resolution.
6. Save for the adoption of the further resolutions of the City Council and the registration of the Loan Agreement with the NBU prior to the closing of the issue of the Notes as described in 3. above, the City has obtained all necessary consents, approvals and authorisations in Ukraine in connection with the Loan.
7. No consents, approvals, authorisations or orders of any regulatory authorities are required by the Issuer under the laws of the Federal Republic of Germany for the maintaining of the Loan or for the issue and performance of the Notes.
8. There are no lawsuits, litigation or other legal or administrative or arbitration proceedings current or pending or, to the best of the knowledge and belief of the City, threatened before any court, tribunal, arbitration panel or agency which might be material in the context of the offering of the Notes.

9. Under current Ukrainian law, a filing fee will be payable upon the initiation of any action or proceedings (including any proceedings for enforcement) arising out of the Notes in any court of Ukraine.
10. Each of the City and the Issuer has agreed that, for so long as any Notes are “restricted securities” within the meaning of Rule 144(a)(3) under the Securities Act, the City or the Issuer will, during any period in which it is neither subject to Section 13 or 15(d) of the Exchange Act nor exempt from reporting pursuant to Rule 12g3-2(b) thereunder, provide to any holder or Beneficial owner of such restricted securities or to any prospective purchaser of such restricted securities designated by such holder or beneficial owner or to the Trustee for delivery to such holder, beneficial owner or prospective purchaser, in each case upon the request of such holder, beneficial owner, prospective purchaser or Trustee, the information required to be provided by Rule 144A(d)(4) under the Securities Act.

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