

RAPAPORT

Special Report November 2014



Honest Grading

The truth, the whole truth and nothing but the truth
By Martin Rapaport

Lawsuit: Nathaniel Averitt vs. Genesis Diamonds, LLC Nashville, Tennessee. August 18, 2014		
	Diamond Cuff Link 1	Diamond Cuff Link 2
Genesis Claimed		
EGL International		
Carat	3.04	3.01
Color	G	G
Clarity	SI1	SI1
Cut	Very Good	Excellent
Value		\$135,000.00
Actual		
Characteristics		
Carat	3.04	3.01
Color	N	M
Clarity	SI1	SI1
Cut	Good	Very Good
Value		\$22,500.00

Honest GRADING

Overgrading is not just a legal issue, it is an ethical issue facing the diamond and retail industry.

BY MARTIN RAPAPORT

*I*s it okay to sell a diamond as a G color when the color is really an N? How about if the G is really an L? Shockingly, a lot of the people in the diamond trade think that it's perfectly okay to use third-party diamond grading reports to overstate the color and clarity of the diamonds they sell.

Diamond grading reports labeled EGLI International (EGLI) commonly use Gemological Institute of America (GIA) terminology to describe diamonds as four or more color/clarity combination grades higher than what the GIA would give the same stones. Overgrading has become institutionalized. Hundreds of thousands of diamonds worth billions of dollars have been sold to consumers with overgraded reports in the past few years.

Remarkably, the dealers selling overgraded reports are not ashamed of their actions. Some buy diamonds with GIA grading reports conditioned on the seller's obtaining three, four or even five color/clarity combination upgrades from EGLI. Retailers seeking greater profits are active buyers of overgraded reports. After all, it's easier to sell an EGLI G at a low price than a GIA G at a much higher price. It's also easier to sell an EGLI G at the same price as a GIA K color. Consumers don't understand the nuances of color grading or the differences between GIA and EGLI reports, but they can certainly tell the

74 percent difference in cost from \$4,200 to \$7,300 for a 1-carat SI1 diamond. From dealers to retailers, an entire industry has emerged based on overgrading.

While the profit motivations are easy to understand, the cynical justifications for the unethical behavior are often just as crooked as the sellers themselves. The obvious negative ramifications of overgrading and misrepresenting diamond quality to hundreds of thousands of consumers are clear. The damage to the diamond industry by the establishment, acceptance and support of a culture that promotes systematic misrepresentation of diamond quality and the outright cheating of consumers destroys the diamond trade from within. It is as insidious as an undetected cancer eating away at the essential moral fiber of the diamond trade.

Frankly, are we an industry of liars and cheaters? And if not, what are the good people in our trade doing about the gross misrepresentations of diamond quality going on right under our noses? I believe that most of the people in our industry are honest and reputable. But I now question all of these good people, as well as our important trade organizations: Why are you turning a blind eye to the large-scale rampant misrepresentation and cheating that is going on? Hundreds of thousands of diamond consumers have been and are being cheated. Why are you not speaking up against this injustice?

CROOKED JUSTIFICATIONS

1 No Grading Standards,

say the gemological anarchists. EGLI, a primary source of overgraded diamond reports, states in its press release of September 18, 2014, “there is no single, international standard for diamond grading that has national or international status or acceptance.” According to them, it’s okay to call an N color a G color, since anybody can say anything they want in a world with no standards.

The GIA created its gemological standards and related terminology in 1953 and began issuing diamond grading reports in 1955. Ever since, it has continuously and consistently supported its standards by issuing grading reports for millions of diamonds. This directly counters the false EGLI claim. Let us be perfectly clear on this: The GIA is the global diamond grading standard accepted by the international trade and the legal systems of the United States and other countries.

One has to question the integrity and honesty of EGLI’s claim. After all, if there are no internationally recognized GIA standards and EGLI maintains different non-GIA standards, then why is EGLI using GIA terminology on its grading reports? Why is its best color a D and not an A? Could it be that EGLI is using GIA terminology in a way that is designed to fool consumers into thinking that they are getting a better grade of diamond than they are actually getting?

Furthermore, consider the ramifications of such gemological anarchy. If the trade accepts EGLI’s claim and allows it to destroy our industry’s internationally accepted GIA standard, then how will we honestly communicate diamond quality to consumers and to each other? If we can’t differentiate quality, we can’t differentiate price, and this will result in a collapse of diamond prices.

The false claim that there are no grading standards is a frontal attack on the very foundation of our industry. It is an attempt to destroy the language of our trade and the life’s work of great people like GIA’s Richard Liddicoat and others who have created standards that honest people live by.

I am shocked that industry leaders have not publicly spoken out against this brazen attempt to destroy the credibility of our industry. I call upon the leaders of our industry to issue public statements confirming the existence of GIA standards. I also urge our trade organizations to condemn and expel from our legitimate trade those who grade and sell diamonds using GIA terminology while applying alternative grading standards that willfully and consistently overstate the quality of diamonds.

MARTIN RAPAPORT STATEMENT REGARDING OVERGRADING OF DIAMONDS

“The Rapaport Group is opposed to the misrepresentation of diamond quality. The overgrading of diamonds is an unfair practice that destroys consumer confidence and the legitimacy of the diamond industry. Retailers who sell overgraded diamonds using GIA terminology and non-GIA grading standards are at great risk. When consumers try to resell their diamonds or send them to the GIA for regrading and discover significant quality differences, there will be hell to pay. The diamond trade must prioritize the protection of consumers above profits,” said Martin Rapaport, Chairman of the Rapaport Group.

RAPNET ANNOUNCEMENT

Effective October 1, 2014, EGL will no longer be listed as a diamond grading report on RapNet. This notice applies to all EGL grading reports, including EGL International, as stated in our previous notice.

BACKGROUND STATEMENT

RapNet is concerned about the misrepresentation of diamond quality through the abuse of the GIA grading standard. We oppose the misuse of GIA terminology by applying alternative grading standards that overstate the quality of diamonds. We support the GIA standards as defined by the GIA grading laboratory to its diamond grading reports.

RapNet recognizes that some EGL grading reports are more consistent with GIA grading standards than others. In our opinion, there is confusion and inconsistency among the various EGL grading reports and we have therefore decided not to list any EGL grading reports on RapNet.

RapNet recognizes that GIA and other laboratory diamond grading is based on human evaluation and is therefore subjective. We recognize that a difference of one color and one clarity between diamond grading reports from the same or different laboratories is within a reasonable tolerance range. We reject the idea that there is no diamond grading standard and caution RapNet members not to use GIA grading terminology to describe diamonds that are below a reasonable tolerance range of the GIA standard.

RapNet members using GIA terminology are required to honestly communicate diamond quality based on the GIA standard.

2 Diamond Grading Is Subjective. Since diamond grading is subjective, there are no standards, say the overgraders. This is false. Diamond grading is only subjective to a degree. For example, 100 out of 100 trained gemologists can tell the difference between a G and a J color. The systematic grading of a diamond by multiple gemologists yields diamond grading results that are almost always consistent within a one color or one clarity range. At the very most, in rare, exceptional circumstances, there might be an error with a gemological difference of two colors or two clarities. In any case, when using GIA standards, there is no justification for the consistent overgrading of diamonds by more than one color or clarity grade.

3 It's Not Me, It's EGLI. Many sellers of overgraded EGLI reports think that they are not personally responsible for overstating the quality of diamonds. Some make the claim that they never said the diamond was a G, it was EGLI, not them, who overgraded. Essentially, they believe they can hide behind the EGLI report.

When we examined prices on RapNet, we found that diamonds graded independently by sellers without any third-party grading report were offered at higher prices than EGLI graded diamonds of the same quality. It appears that RapNet members did not want to personally lie about the quality of the diamonds they were offering for sale but did feel comfortable offering EGLI diamonds for sale at lower prices because they were of lower qualities. The takeaway is that overgrading reports have become a license to lie about quality.

So what will happen when consumers try to resell their diamonds or send them to the GIA for regrading and then find out that their Gs are really Ks or worse? Who will be held responsible for the overgrading misrepresentation? Will it be the EGLI laboratory in Hong Kong or Israel? The dealer who sold the diamond to the retailer? The retailer who sold the diamond to the consumer?

While there may be uncertainty about the legal responsibility of EGLI and dealers who sell overgraded diamonds to retailers, one thing is for sure: Retailers will be held 100 percent accountable for any and all misrepresentations of diamond quality to consumers. U.S. law differentiates between transactions between “experts” such as dealers or jewelers and the sale of products to consumers. Experts are expected to have a high level of product knowledge. They are expected to look at the diamond and know that their EGLI G is in fact a GIA K. Therefore, it is unlikely that retailers will be able to make any claims against dealers when the consumer returns

the diamond and demands a refund. Essentially, the retailer will be 100 percent solely responsible for the refund with no legal recourse to the supplier.

It will get even more interesting when consumers demand triple the damages they are entitled to from retailers who have sold them misrepresented overgraded diamonds. It appears that retailers are the ultimate suckers in this game. The financial and reputational risk is all theirs.

Some dealers take the position that if they are not legally responsible for selling overgraded diamonds to retailers, then there is no problem in doing so. After all, if it's legal, why shouldn't they do it?

This raises the important question of ethics in our industry. Most ethical people would agree that it is wrong to sell overgraded diamonds to consumers. They would also agree that it's wrong to institutionalize a business that sells overgraded diamonds to retailers who may end up going bankrupt when consumers find out about the misrepresentation. Do we or should we have any ethical constraints? Or are we only bound by legalities? Is our trade ethical?

DEFINITION: OVERGRADED DIAMOND

An overgraded diamond is a diamond graded using GIA terminology that when verified by the GIA is more than one color or one clarity lower than the original grade.

In my view, it is important to separate ethical products and people from unethical products and people. While we can't stop companies from legal unethical activities, we can decide who to do business with. And if our industry does not have a sufficient critical mass of ethical companies, then at the very least we should refuse to trade legal but unethical products that are used to mislead people.

The bottom line is that overgraded diamond reports are poison. Ethical people should not deal in them.

4 But The Price Was Low. Some suppliers think that it is okay to misrepresent quality as long as the price is low. They further maintain that the consumer somehow knows that the quality is overstated because the price is so low. In fact, there is no ethical or legal justification for such misrepresentation. Consumers are incentivized to buy because they think they are getting a “good deal” when in fact they are not getting a “good deal” as they think because the quality has been exaggerated more than they realize. It's illegal.

Consider the case of Rick Chotin, a St. Louis retailer with a 40-year-old store. In the early 1990s, he was one of the first U.S. jewelers to offer Yehuda-treated fracture-filled diamonds for sale to consumers. He charged significantly lower prices than prices for similar nontreated stones, but he failed to tell his customers that the diamonds were fracture-fill treated. He thought he was simply giving them a “good deal.”

One day one of his customers visited the local appraiser, who upon observing the telltale rainbow effect, informed the consumer that her engagement ring was treated. She was shocked. A local TV station picked up the story and soon there were hundreds of consumers lining up outside the appraiser's office determined to find out if their diamonds were also treated. According to the appraiser, some 90 percent were indeed treated.

In spite of the low prices Chotin charged, he was investigated and ordered by the Missouri attorney general to refund money to his customers and pay penalties. Chotin tried to do what was right and used his life savings of \$1,000,000 to provide refunds to his customers. But there wasn't enough money. Finally on March 7, 1994, Rick Chotin killed himself by drinking a dose of “jeweler's cocktail”—a cyanide solution used for cleaning gold. He was 44 years old.

Is there nothing for us to learn from Rick Chotin's death? Did he die for nothing?

Does anyone still think it's okay to misrepresent quality if you are selling at a low price?

5 Salespeople Make Full Disclosure. Some people say salespeople always tell the customer that EGLI uses a non-GIA standard that overgrades diamonds. In fact, if all salespeople honestly tell the customer that EGLI diamonds are overgraded compared to GIA standards, then that might be a good retailer defense. However, given the use and abuse of GIA terminology on the EGLI grading reports, there must be honest communication about the extent of overgrading. If EGLI calls a diamond a G, what is it really? Is it a GIA K, GIA N or what? It's hard to believe the salesperson will know the true GIA grade, let alone communicate it.

Here is a quote from the James Wells v. Genesis Diamonds LLC lawsuit filed on July 22, 2014, in Nashville, Tennessee. The quote is from a TV station undercover report on the sale of EGLI diamonds by Genesis:

“Back at Genesis at least one dissatisfied customer was told that there was only one difference separating GIA stones from EGL International: the price.... The Genesis employee goes on to tell Michael the difference in GIA and EGL certification wouldn't be the quality of the stone, but rather its price.”

Frankly, I do not believe that it is standard industry practice for retailers to show an EGLI grading report and then fully disclose to the consumer what the actual GIA grades are. Even if consumers are told different standards are used, they still do not know the extent of the overgrading.

CONSEQUENCES

The rampant misrepresentation of diamond quality by those selling overgraded diamonds has ramifications well beyond specific fraudulent transactions. The continuation of such unfair business practices undermines the integrity and legitimacy of the diamond industry as it destroys consumer confidence in diamonds and the diamond trade. Diamond quality misrepresentation threatens the sustainability of the entire diamond industry and must be stopped.

The following are some of the consequences.

6 The Unlevel Playing Field. What about ethical jewelers who refuse to sell overgraded diamonds? How are they to compete with the jeweler across the street who is selling EGLI Fs at \$4,200 against GIA Fs at \$7,300? How much time and money can be spent trying to educate consumers about the differences in grading standards? What about consumers who are more interested in shopping than education? Over time, ethical jewelers will lose price-sensitive customers to competitors who use unfair business practices. Should being ethical mean that you have to go out of business?

The sad fact is that many jewelers feel that they have no choice but to offer diamonds with overgraded reports. If everybody is doing it they believe they have to do it to stay in business. The introduction of overgraded diamonds into a consumer market forces other jewelers to compete with their own overgraded diamonds. And so a culture that promotes the systematic misrepresentation of diamond quality grows.

The insidious thing about overgrading is that it promotes more overgrading until the extent of unethical activity overwhelms the reputation of the entire industry. The solution is for the diamond trade to bifurcate. Separate the good products from the bad products, the good labs from the bad labs. That is what the GIA was designed to do (see “GIA Grading System Background,” page 57).

Those who seek to maintain an all-inclusive diamond trade that mixes ethical and unethical people, good and bad standards, honest and dishonest products, are destroying our industry by creating an unlevel playing field that rewards bad at the expense of good.

The lesson here is that the diamond industry cannot survive without a level playing field. The good people in our industry can, should and must create their own level playing field with ethical, honest standards.

7 What About Christmas? Some retailers are concerned that the disclosure of the overgrading problem to consumers may have a negative impact on the upcoming holiday season. Upon learning of overgrading, some consumers may not want to buy any diamonds at all.

The rampant misrepresentation of diamond quality to hundreds of thousands of consumers poses a significant threat to the sale of legitimately graded diamonds. Until such time as there is clearly communicated differentiation between honestly graded and overgraded diamonds, the industry faces catastrophic reputational risk. Yet if disclosure is made and consumer alerts are issued, legitimate retailers may suffer. It looks like a lose-lose situation. What to do?

Whenever I don't know what to do, I err on the side of truth and transparency. In this case, there is even greater reason to broadcast the situation. Consider the position of the consumers who buy an overgraded diamond. What about the terrible feeling they will get when they learn that the quality of their diamond is lower than they thought? Should they be buying overgraded diamonds this holiday season because we failed to warn them? As an industry, should we be more concerned about the lost sales and profits of diamond dealers and jewelers than the lost money and trust of consumers?

Our industry is facing exponentially increasing reputational risk as well as an important ethical challenge, which demands that we tell consumers the truth. As an industry, we must embrace the values of truth and honesty and make them more meaningful than short-term gains. The bottom line is that our trade must prioritize the protection of consumers above profits.

As an industry, I don't think we can or should hide the truth about overgrading. Aside from the more important ethical obligation, we must recognize that this elephant is much too large to sweep under the rug. Consumers must be warned about grading reports that overgrade diamonds and the legitimate market of diamonds graded to GIA standards must be protected.

8 Show Me The Money. What will happen when consumers find out about the massive overgrading situation? Will consumers say, "Oh, I knew that EGLI was using a different lower grading standard and I paid a fair price, so no problem?" Or will EGLIs become the new Yehuda fracture-filled diamonds of the twenty-first century? Will consumers who have been sold diamonds without fair disclosure line up waiting for appraisers to tell them the GIA quality of their diamonds? Will the eager beaver, class action lawyers smell opportunity? Will consumers and attorneys general demand refunds? If so, who will pay?

We are not just talking about theoretical abstract reputational risk. No, we are talking about cold, hard cash. Something tangible that everyone in our trade understands.

While I don't want to create panic, I do want to warn everyone about the serious risk we are facing. Well over a billion dollars of overgraded diamonds are out there and some of them will come back to retailers from consumers demanding a full retail refund. If retailers take back the diamonds and provide a full refund, things may not get too messy. However, if retailers do not take back the diamonds, they will be offered for resale on the open market and/or sent to the GIA for regrading. Consumers will find out that they have been taken for a ride.

If a critical mass of consumers is made aware of the overgrading of their diamonds and they are unable to get their money back, things may get frighteningly interesting. We can expect a publicly driven social media blast against diamonds, the likes of which we have never seen or can barely imagine.

If you are a retailer trading in overgraded diamonds, you had best be prepared to buy them back or go out of business. Considering the possibility that your legally minded supplier may not back you on purely ethical grounds, you should probably get a written guarantee from your supplier that he will take back any overgraded diamonds sold to you. You should also consider that even if you agree to buy back the diamonds from consumers, an enterprising lawyer might still claim that you defrauded clients by not providing full disclosure of quality and subject you to a lawsuit demanding triple damages. Consider that you will be expected to refund the full retail price rather than wholesale price.

ISSUES

9 What About The Good EGLs? While I am not sure about how "good" the good EGLs are, there is a clear difference between two types of laboratories.

There are the good laboratories that use GIA terminology and declare that they grade according to GIA standards, producing diamond grading reports that are reasonably consistent within one color and one clarity grade of GIA. And then there are the overgrading

We
reject the
idea
that there
is no
diamond
grading
standard.

laboratories that use GIA terminology and grade according to different standards that regularly overstate the quality of the diamonds and produce grading reports that are more than one color or one clarity grade higher than GIA's grades.

Rapaport policy is to not work with overgrading laboratories and work with good laboratories. RapNet lists GIA, AGS, HRD, IGI and other grading reports that we believe meet our good laboratory description. In the case of GIA and HRD, we operate take-in windows that assist clients in obtaining their reports.

We recognize that some EGL grading reports are more consistent with GIA grading standards than others.

The problem with EGL is that the brand is out of control, lacking any common ownership or standards. There is great confusion and inconsistency among the various EGL laboratory standards and reports. Every EGL does what it wants with different yet similarly named grading reports scattered across the globe. EGLI is an overgrading laboratory while EGL USA subscribes to GIA standards and claims not to overgrade. Yet they both carry the EGL brand name.

A huge problem is that each EGL laboratory promotes its brand name under the same EGL banner. They all tell the world they are good labs, while some clearly are not. Consumers, jewelers and even dealers cannot be expected to tell the difference between the grading standards of EGL International, EGL Israel, EGL USA, EGL Hong Kong, EGL China, EGL India, EGL Israel, EGL Turkey, EGL Canada, EGL Miami, EGL Platinum and EGL Antwerp. Furthermore, new EGLs pop up like mushrooms, some of which have outrageous standards or even no standards at all. All of this amid reports that some clients at some EGLs get highly preferential grading results, blank grading reports and can even provide labs with suggestions of what the color and clarity should be. With all due respect to the good EGLs, this hodgepodge mixed brand of good, not good and who-knows-what labs is entirely unacceptable.

An even greater problem is the way branding works. EGLI gets a free ride on EGL USA's branding. The more EGL USA promotes its brand as a good laboratory, the more opportunities there are for unethical jewelers to mislead consumers with EGLI reports. EGLI would not be as large and successful as it is in the U.S. today without EGL USA's better reputation.

We have to ask how many consumers have been sold overgraded EGLI reports due to EGL USA? Do the good EGLs share responsibility for supporting the overgrading EGLs? In my view, it is time for the good EGLs to stop aiding and abetting the not-good EGLs with their brand confusion. The ethical thing for the good EGLs to do is to change their name.

Finally, let us consider the confusion that consumers are being subjected to. First, they must confront multiple grading standards. One lab's G color is another's N color. But that's not enough. Let's also confuse them with the brand name of laboratories all under the same EGL name but using different standards. A consumer doesn't know the difference between EGLI, EGL USA and EGL Turkey. Buying diamonds should not be like buying an EGL lottery ticket. The idea that if you can't beat consumers out of their money, you can confuse them out of it, is over.

10 If GIA Is The Standard, What About SI3s And Other Gemological Information?

We define SI3 as an intermediate grade between SI2 and I1. Many in the trade, including this writer, believe that the clarity and price spread between SI2 and I1 is too large. Furthermore, the diamond trade commonly sorts diamonds into SI2, SI3 and I1 grades.

GIA GRADING SYSTEM BACKGROUND

An additional issue related to the SI3 grade is the inability of the current GIA diamond grading system to differentiate between eye-clean and not-eye-clean diamonds. The eye-clean issue is important because it has great relevance when selling a diamond to a consumer. There is also concern that the GIA is much too lenient when grading black imperfections and much too strict when grading feathers and nonblack inclusions.

And then there are numerous higher-level technical aspects that are often provided by companies listing diamonds on RapNet but not provided in the GIA grading report. This might include the color tint, inclusion size, color and location of inclusions, photos of diamonds and other items.

In general, the trend is for RapNet to provide as much information as possible so that buyers can trade online without seeing the stone. Or if buyers require inspection, sufficient information is provided so as to significantly limit returns. Furthermore, diamond manufacturers commonly sort diamonds to higher levels of differentiation so as to optimize pricing.

Since we have made a strong argument in this article that GIA is the standard and that if you use GIA terminology you must use the GIA grading standards, there is an obvious question about why the Rapaport Price List quotes SI3 prices.

The issue before us is if it is okay to add to GIA standards without replacing them. Obviously there is no problem with a lab or dealer describing a diamond using GIA standards and adding information such as the color of the inclusion or if the diamond is eye-clean. Also, it's not a problem if someone does not use GIA terminology such as TLB (top light brown) or PQ2 (imperfection 2) to describe a diamond. A lab or company might also want to grade a diamond as an F- or VVS2+.

The question regarding SI3 is interesting. While we are not technically using GIA terminology, I would hate to see companies using SI3 to describe I2 diamonds. Therefore, our RapNet policy will be that if you grade a diamond as SI3, it will have the same overgrading condition as if you graded it SI2. In other words, an SI3, like an SI2, should not come back from the GIA as an I2. If it does, it is overgraded.

We are communicating with the GIA regarding the need for an SI3 grade as well as about other gemological grading concerns described above. At some stage, we hope that the GIA will extend its grading system to modify or add additional information to its reports.

We must recognize that while the GIA grading system is not perfect or all-inclusive, it is the standard that must be used when using GIA terminology.

When was the Gemological Institute of America (GIA) created? Who created it? And why?

GIA was created in 1931 by Robert M. Shipley, Sr. to "professionalize the jewelry trade through education." Through his personal experience in the jewelry business, Shipley realized how little he actually knew about gems. He got the idea for GIA after enrolling in correspondence courses at Britain's National Association of Goldsmiths while studying in Europe and decided to bring that same type of education back to the states.

What about the American Gem Society (AGS)?

The AGS was also founded by Shipley in 1934 as a professional guild of knowledgeable jewelers. The goal of the AGS was to create an organization that could help protect consumers from fraud and false advertising.

When was the GIA diamond grading system created? And who created it?

Prior to 1933, there were no instruments specifically used for diamond grading, so jewelers had to rely on tools, such as microscopes, from other fields to gauge the quality of diamonds. That's why Robert Shipley, Jr.'s invention of the "Diamond Eye Loupe," "Polariscope" and "DiamondScope" between 1934 and 1937 was so revolutionary.

Richard Liddicoat created the GIA diamond grading system in 1953, though he had been working on the system as early as the 1940s and was using it as a teaching tool at the GIA.

He introduced the International Diamond Grading System™, based on Robert Shipley, Sr.'s 4Cs — color, cut, clarity and carat weight.

Until then, there had not been a universal, objective standard of measurement in place for grading diamonds. Due to the inconsistency of descriptions used, dealers would often disagree among themselves about the quality of specific stones. Liddicoat wanted a consistent system of grading diamonds that dealers could agree on.

Liddicoat used the letters D-Z to describe color, with D as a starting point, because prior to the creation of the grading system, dealers were using A, AA, AAA to describe color and "A" had become misused and tarnished. He wanted a fresh perspective and starting point.

We must recognize that while the GIA grading system is not perfect or all-inclusive it is the standard that must be used when using GIA terminology.

11 Laboratory Competition. Our strong support of the GIA standard does not imply that we do not support competition among laboratories. While we believe that the GIA is the sole custodian of its diamond grading terminology and standards, we also believe that there should be healthy competition among companies and laboratories that use GIA terminology and standards to grade diamonds. The GIA does not have a monopoly on the use of its terminology or standards.

GIA has given the diamond industry a great gift of language, incorporating not just the terminology but also defining what the letters mean in the form of live standards provided by an active GIA grading laboratory. We must ensure the GIA has the exclusive right to manage the language it has given us so that we can maintain honest communication and standards in our trade.

The fact that GIA controls one set of terminology and associated grading standards does not prevent other companies or laboratories from establishing their own different standards using their own different terminology. It's a freely competitive market and likely to become more so as new technology enables diamond grading standardization and differentiation. Nothing stops anyone from creating a different or better grading system.

RAPAPORT SOLUTIONS

Having discussed the problem of overgrading, the key issue before us now is what to do about it. Specifically, what policies and procedures should the diamond industry adopt so as to ensure fair and honest communication regarding diamond quality? This can be accomplished by applying two rules and one definition.

RAPAPORT RULES

Rule 1: It is an unfair business practice to communicate the grade of a diamond using GIA terminology while applying non-GIA standards that systematically overgrade the quality of the diamond.

Definition: An overgraded diamond is a diamond graded using GIA terminology that when verified by the GIA is more than one color or one clarity point lower than the original grade.

Rule 2: Diamond suppliers are responsible for the quality of the diamonds they sell. If a supplier communicates the quality of a diamond using GIA terminology, the buyer may at his option and expense, within ten business days of receiving the diamond, send the diamond for grading verification to the GIA. Upon return, if the diamond is graded more than one color or one clarity grade lower than the quality represented by the seller, then the seller shall accept the return of the diamond and provide the buyer with a full refund as well as a refund of the GIA grading verification fee. In the event that the buyer is a consumer, the buyer shall have 30 business days to send the diamond for grading verification to the GIA.

DISCUSSION ABOUT RAPAPORT RULES FOR HONEST GRADING

12 Sellers Are Responsible For What They Sell.

The foundation of the diamond business is based on the honesty and integrity of diamond traders. The oldest rule in the business is that sellers have to stand behind the products they sell. Diamond reports that overgrade diamonds are now being used as an excuse by sellers to avoid their responsibility to buyers. It's time to shift responsibility for the accuracy of diamond grading back to the suppliers and away from the laboratories. Once sellers are forced to take full responsibility for what they sell, the overgrading misrepresentation game will end. Selling an overgraded diamond should be like selling a treated diamond requiring full disclosure. "Give me my money back" will become the new language of overgrading.

13 Buyer Beware. In the new world of seller responsibility, the buyer will have to get the supplier to commit to written quality assurances on the invoice. Some sellers might say, "I've got an EGLI, I do not guarantee any quality, buy it if you like." And so, indeed, if you buy it, everything is now the buyer's responsibility. The game now becomes about who is promising what to whom, not what some third-party lab is saying. It will be interesting to see how careful sellers become about what they promise when they have to put their money where their mouth is.

14 Laboratory Harmonization. The harmonization of laboratory standards is a good idea and deserves support. So does transparent testing. However, given the competitive market situation, the complexity of international law, antitrust issues and enforcement problems, I don't think our industry can wait around long enough for this to be a realistic solution for the current situation.

CONCLUSION

The misrepresentation of diamond quality by laboratories that overgrade diamonds poses a significant threat to the diamond industry. Hundreds of thousands of consumers have purchased more than one billion dollars of overgraded diamonds. While there does not appear to be any imminent threat of consumers returning these diamonds en masse, a few lawsuits have already commenced. Failure by jewelers and the diamond trade to provide fair refunds to consumers seeking to return overgraded diamonds could encourage other consumers to question the quality of their diamonds. Should consumers find that a significant number of diamonds have been overgraded, a run of refund requests to jewelers is possible. If this occurs, it is unlikely that retailers will have the necessary funds to provide refunds. In any case, there would be significant damage to overall consumer confidence for all diamonds.

The diamond trade must address the issue of overgraded diamonds in a timely manner. Consumers should be warned about overgrading and directed toward grading reports that provide fair grades. Trade organizations should implement rules that make suppliers responsible for the accuracy of the grading information they provide with the diamonds they sell. Use of third-party grading reports that overgrade diamonds should be discouraged with mandatory disclosure requirements to all buyers, including consumers. In all instances, jewelers should be fully informed of the risks they take when buying and selling overgraded diamonds. ♦

IMPORTANT RAPAPORT DISCLOSURE

The Rapaport Group provides a broad range of added-value services to the diamond trade. These services include GIA LabDirect service that provides take-in and delivery window access to GIA diamond grading laboratories for clients in Israel, Belgium and India. Similar services are provided to HRD Antwerp. Rapaport has worked with GIA for over 20 years and has handled millions of GIA diamonds for clients.

Additional Rapaport services include independent RapLab gemological services as well as *Rapaport Magazine* and *Diamonds.Net* editorial and information services, the RapNet diamond trading network and Rapaport Trading Services, which include Rapaport Auctions and Tenders.