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The Office of Foreign Assets Control and Marange Diamonds

The legal aspects of trade in diamonds from Marange in the US

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In recent weeks, a large quantity of rough diamonds extracted starting in May 2010 from the Marange region of Zimbabwe were sold to diamond trading companies and exported from Zimbabwe. These diamonds were approved by a monitor from the Kimberley Process, and declared to be fully compliant with all KP standards.

The mining companies that extracted the diamonds and exported them from Zimbabwe are believed to be 50% owned by one or more entities listed on the US Office of Foreign Assets Control list of "specially designated nationals" ("SDN"). According to US laws, because these listed companies are the subject of US sanctioning laws, or are suspected of supporting terrorism or engaging in money laundering, it is prohibited in the U.S. to engage in direct transactions with these companies or entities, or companies that may not be on the list but are 50% or more owned by a listed company. Such transactions may lead to transactions being blocked by US banks or in some circumstances, civil or criminal sanctions against the parties engaging in the transactions.

This leads to the question: Are US diamond dealers prevented by law in engaging in **indirect** transactions buying or selling these diamonds on the secondary market because they were first sold as rough by companies that are 50% or more owned by an OFAC listed Zimbabwe company?

Let's pose a hypothetical so we are all on the same page: Company Z (a 50% owned affiliate of an OFAC listed company in Zimbabwe) sells rough diamonds extracted after May 28, 2010[1] to a company located in India. The payment for the diamonds from the company in India to the affiliate in Zimbabwe is completed in a currency other than US dollars[2], and after payment, the diamonds are compliantly exported to the Indian company with authentic Zimbabwe KP certificates stamped and signed by the KP monitor, as required. The Indian company receives the rough diamonds, cuts and polishes them, and then offers them for sale. A US diamond manufacturing company seeks to purchase the polished diamonds for export from India to the U.S. and intends to pay for them by a wire transfer in US dollars to the company in India. The company in India on its invoice truthfully provides the relevant KP warranty that the diamonds invoiced were traded consistently with all KP requirements and any UN resolutions addressing conflict diamonds. In this scenario, is the U.S. entity buying the polished diamonds from the company in India risking violation of any US provision of law by accepting the imports, or by paying for these diamonds in US dollars? Could this transaction be blocked?

In general, the answer is no - there is no apparent violation of US law, and the transaction should not ordinarily be blocked. While any attorney would be very hesitant to answer questions based on hypothetical facts, JVC has been asked to answer this question so frequently in the past weeks we thought it would be advisable to provide some clarity on the subject - with one very strong caveat: if you have doubts, consult with your company's counsel before engaging in the transaction.

JVC does not provide legal advice. But here, we can provide some guidance based on our interpretation of the OFAC rules. The OFAC rules apply to direct U.S. company to OFAC listed company transactions, or transactions to an OFAC listed company using US dollars transmitted through US clearing banks. If the transaction is on the secondary market, not a transaction directly between a US company and a listed company (or a 50% owned affiliate of the listed company) then the transaction should not be blocked nor would it violate any US laws. It should be noted that the transaction between the listed company and the Indian company could have been blocked if the transaction used US dollars - since a US clearing bank would have to have been involved in a transaction. But the subsequent transaction between a US company and an unlisted Indian company reselling the polished diamonds should not ordinarily be blocked since there is no direct transaction with a listed company.

You will note that there is one issue that JVC has not addressed in this article - the ethical calculation one might apply generally to the purchase of diamonds from Marange. This is a subject for another day. JVC's focus and expertise is legal compliance, which is the subject of this article.

Any questions or comments? Please contact me at clg@jvclegal.org, or visit the JVC web site - www.jvclegal.org.

[1] May 28, 2010 is the date after which the KP monitor declared that diamond production by the two new producers in Marange were fully compliant with KP minimum standards.

[2] Under US banking law, if the payment transaction from India to the company in Zimbabwe were in US dollars, the transaction would have to be cleared by a US bank, and thus could have been subject to blocking.

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