

AFTER KIMBERLEY... NOW WHAT?

BY MARTIN RAPAPORT

By now it should be clear that a Kimberley Process (KP) certificate does not ensure a diamond is free of human rights violations or other serious ethical problems. In fact, a KP certificate does not even ensure that a diamond is legal for trade in the United States or European Union.

The recent release of over \$200 million dollars of KP-certified Marange diamonds opens a Pandora's Box of complex ethical, legal and financial issues that the diamond industry is struggling to address.

Questions abound. How does one deal with the fact that KP certificates are being issued for diamonds that violate U.S. sanction regulations and cannot be legally sold to U.S. companies? How do you know that the diamonds you are buying were not involved in severe human rights violations? What if diamonds are "only" involved in funding repressive regimes that murder and torture political opponents? What about "unknown" diamonds from Angola, the Congo and Cote d'Ivoire? Are they okay? If you don't buy "bad" diamonds – won't someone else buy them for low prices and then compete with you? If others are buying — why should you miss out?

One fundamental question is: Who is responsible for ensuring that the diamond industry is not promoting human rights violations through the purchase of diamonds?

Over the past few years, industry trade organizations have taken the position that it is the role of governments through the KP to ensure the legitimacy of the diamond trade. Millions of dollars have been spent promoting and proclaiming that KP certification and the "System of Warranties" guarantee that "diamonds have been obtained from legitimate sources." However, as evidenced by the recent KP certification of U.S.-banned Marange diamonds, that is a false and dishonest position.

The diamond trade can no longer get away with telling consumers and each other that having a KP certificate ensures diamonds are legitimate. Even a child can see that the KP emperor has no clothes.

GOVERNMENT LIMITATIONS

While governments are very powerful on a national level, their power is severely limited on an international level. This is particularly true when governments interfere with internal human rights issues of another nation. No government wants another government to tell it how to deal with its own people and their human rights. Absent a United Nations Security Council (UNSC) resolution or an act of war, no government has the legal right to force another government to do or not do anything.

It is important to understand that the KP is run by governments for governments and its purpose is to protect the self-interest of those governments, not the interests of the diamond trade. The governments running the KP have a broad range of competing interests, obligations and priorities. A solid majority of member governments, including China, Russia, South Africa and the other African producer nations never wanted and do not now want human rights to be part of the KP. Consider things from the African perspective. If you represented an African diamond-producing country, would you agree to a system whereby white people in America and Europe decide if you can sell your diamonds based on their human rights values? Would America agree to let Africans control their right to export products? If the KP voted, there is no question that a majority would support the immediate export of all Zimbabwean diamonds irrespective of any human rights violations. To most governments, the issue is not human rights; it is sovereignty — the right of governments to independently control their exports.

It's not the fault of governments or the KP that they are unable to solve the problem of human rights in the diamond industry. The KP was designed to respond to United Nations Security Council (UNSC) resolutions that embargo diamonds to stop wars — as was the case in Sierra Leone in the late 1990s. It was not designed and never had a consensus for the elimination of human rights violations.

So let's make it clear. The problem isn't the KP and the solution isn't the KP. The real problem is the fact that the diamond and jewelry industry refuses to take responsibility for the human rights violations that are taking place in the artisanal mining sectors. The dishonest attempt by trade organizations to lay human rights problems at the feet of the KP, which is incapable of dealing with them, is shameful, wrong and evil.

Perhaps it wouldn't be so bad if the political wrangling was just about money or jobs. But it isn't. Artisanal diggers and innocent civilians were murdered, raped and enslaved. We must be able to differentiate between business as usual and terrible unacceptable things happening in our supply chain. The diamond industry bought, sold and profited from the Marange blood diamonds of October 2008 as if nothing was wrong, as if people had not died. You have to wonder — where are these blood diamonds today? Are they in your safe? Is your customer wearing them? Consider the fact that no trade organization stopped the trade in these blood diamonds in 2009 because the diamonds were legitimized with KP certificates.

RESPONSIBILITY

So let's answer our first fundamental question: Who is responsible for ensuring that the diamond industry is not promoting human rights violations through the purchase of diamonds?

You are. Every single rough dealer, cutter, polished dealer, jewelry manufacturer, wholesaler, retailer and consumer is individually and personally responsible for what they buy. You can't rely on governments or trade organizations. You have to make a fair and honest effort to ensure your supplier is not selling you bad diamonds. And it's not just Marange diamonds. It's about Congo, Angola and other problematic artisanal diamond sources. And what about gold? What about colored gemstones?

Now it might seem irresponsible and unrealistic for us to place the responsibility for an ethical jewelry industry on hundreds of thousands of individual members of the jewelry trade scattered across the globe. After all, individuals do not have law enforcement powers. They do not control customs. How can we as individuals stop evil? How can we stop smuggling and bribing and governments in Africa that use their soldiers against their own people?

Let's get realistic and accept the fact that we can't stop evil. But let us also accept the fact that we can no longer go on supporting evil. Let's accept and support the fact that we have the ability and obligation to control who we give our money to. Let's recognize that sometimes our decision about what we buy and where we buy is a life-and-death decision for someone else.

U.S. POSITION

Consider the position taken by the U.S. government. President Bush banned U.S. entities from trading with the Zimbabwe Mining Development Corporation (ZMDC) on July 25, 2008. Since then, U.S. entities have not been allowed to buy ZMDC's diamonds, including diamonds from the Mbada and Canadile mines, even if they have KP certificates.

Now, why would the President do this? Didn't he know that Indian companies buy these diamonds and mix them with other diamonds making it difficult for

Excerpt: Letter from U.S. Office of Foreign Asset Control to Martin Rapaport

“You also seek guidance on whether a U.S. person may purchase diamonds from other foreign companies which have purchased diamonds from Mbada or Canadile. Please be advised that a U.S. person may not procure goods, services or technology, including diamonds, from a blocked person directly or indirectly (including

through a third-party intermediary). Please also be advised that the prohibitions on transactions involving blocked property apply to transactions by a U.S. person in a location outside the United States with respect to property in which the U.S. person knows, or has reason to know, a person whose property and interests in property

are blocked has or has had an interest since the effective date of the blocking. See ZSR, §541.406. Therefore, a U.S. person generally cannot purchase diamonds from a foreign company if the U.S. person knows, or has reason to know, that a blocked person has or has had an interest in the diamonds since the effective date of the blocking.”

A list of OFAC blocked entities is available at <http://www.treasury.gov/ofac/downloads/t11sdn.pdf>

U.S. retailers to know if they are buying Marange diamonds? Why was the President putting the responsibility and threat of jail sentences on company directors and individuals buying these diamonds?

The message here is that governments hold the private sector responsible for how they spend their money. It's the law. Whether your company buys goods that fund terrorism, supports governments that kill diggers or pays bribes, you are responsible. You can't get off the hook by claiming that other people do it. Your money is your responsibility, period.

It's interesting to note that the letter from the U.S. Office of Foreign Assets Control (OFAC) to Martin Rapaport (see page 31) clearly prohibits "indirect purchases of diamonds" if a person knows or "has reason to know" the diamonds are from ZMDC's Mbada or Canadile mines. Given the fact that well over \$300 million of these diamonds have been exported recently from the UAE and South African with KP certificates, buyers undoubtedly have "reason to know" that the diamonds they buy may originate from sanctioned ZMDC sources. It looks like the U.S. and probably EU diamond trade can't simply make believe that the diamonds they buy are okay because they have been mixed. The "if you can't beat the law, confuse the law" approach isn't going to work.

ETHICAL CERTIFICATION

So what do we do about this? It's obviously time to separate the good diamonds from the bad and unknown diamonds. We can no longer assume that a diamond purchased from an unknown source is good. We have to ask questions and get assurances from suppliers that are well beyond the "KP System of Warranties" statement on the invoice (see box this page).

Invoices

Rapaport suggests that the following text be required on all supplier diamond invoices in addition to the standard Kimberley Process notification.

Note bracketed items to be included as appropriate. We do not know or suggest that such notification is sufficient due diligence on the part of U.S. entities buying diamonds. Consult your attorney to ensure you are meeting your compliance requirements.

"The supplier hereby warrants that reasonable due diligence has taken place to ensure that the [natural, untreated] diamonds hereby invoiced [provided on memorandum] have not been sourced from entities blocked by the U.S. Office of Foreign Asset Control or other government agencies."

The fundamental solution to the ethical and legal problem of buying diamonds that are involved in or fund human rights violations is the establishment and support of Ethical Certification Systems. Such systems would address a broad range of social issues and offer a grading system (see page 33) that enables suppliers and their customers to price and trade a range of ethical products.

A Rapaport Ethical Certification (EC) system would accomplish the following:

- Identify the production process and producers from raw materials to certified product
- Rate and audit the ethical status of all the product production processes
- Confirm and audit all transformation processes and transition points to ensure product identity
- Physically identify the final certified product to enable reverse and progressive traceability
- Conduct independent third party audits of the auditing procedures and random spot checks of the production and auditing processes (without prior notification)
- Transparently communicate the certification processes and the limitations of the Ethical Certificate

It is important to recognize and support the efforts of the Responsible Jewellery Council (RJC). The RJC has established standards for the ethical certification of companies in the jewelry sector based on Organization for Economic Cooperation and Development (OECD) guidelines and a consultative process. The RJC is also in the process of establishing voluntary Chain of Custody (CoC) standards that will enable ethical certification of products. While the RJC is not perfect and has critical ethical limitations related to their reliance on KP certification and conflict diamond definitions as a basis for ethical conduct, their approach, intention and direction is improving and they are an important positive force for the development of ethical certification in the jewelry industry. Members of the trade are strongly encouraged to join and involve themselves with the RJC. At this stage it is the best way to learn about your ethical responsibilities and establish your ethical identity.

While the De Beers Forevermark and BHP Billiton's CanadaMark™ branding initiatives are primarily designed to increase the downstream value of their diamonds, they do provide a recognizable level of ethical certification based on the fact that the diamonds originate from known ethical sources and the production process is audited to conform to documented best practice principles.

The advent and intensification of additional diamond and jewelry branding initiatives will undoubtedly increase demand for ethical certification. While branding increases profits through the marketing of an added-value promise to the consumer, it also leaves a company susceptible to extreme damage in the event of ethical misbehavior.

In the late 1990's Nike experienced a branding crisis due to the discovery and disclosure by news organizations of exploitative employment practices. The negative impact on Nike was not limited to the reputation or social aspects of its brand. Profits fell by 49 percent and share prices plummeted by 57 percent. Fortunately, Nike recognized the problem and implemented strict supply chain controls. The message is clear — if you are going to brand your products, you had better get your ethical priorities in order. Efficient and transparent ethical certification is an optimal way to address this need.

THE ETHICAL PROCESS

While the ethical certification solution addresses the needs of downstream manufacturers and retailers, it does not solve the terrible human rights challenges confronting the artisanal mining community. While jewelers might find safety under the protection of ethical certification for good diamonds, the diggers of Marange will likely continue to be abused and violated as Zimbabwe turns to elections and diamond revenue is used to fund violence. Make no mistake about it, no one is going to throw Marange or other problematic diamonds down the toilet because responsible jewelers refuse to buy them. China and Russia are already bidding heavily for these diamonds and they will pay a high price given the state of the market. So other than protecting our own economic self-interests and operating in compliance with U.S. and EU legal requirements what good will our ethical certification systems do for others? Will they make any difference to the diggers? Will they save any lives?

Implementation of ethical certification will create a process of unintended sustainable consequences that are not obvious. The diamond and jewelry industry is undoubtedly on the slippery slope of legitimization. In spite of the “animal instincts” of our highly price-competitive dealer markets, our downstream trade is evolving. As mining companies absorb an ever increasing percentage of available manufacturing profits, cutters and dealers are forced downstream and are evolving into sophisticated added-value, brand-conscious, luxury merchants. We are not only repositioning our products; we are repositioning ourselves.

Change will only take place if it is driven by money and profits. While it is important for this writer to shout out about the terrible injustice in the artisanal sector, I have very little illusion that corporate titans will transform

RAPAPORT ETHICAL PRODUCT SCALE

Fair Trade



Recycled



Ethical



Unknown



Problematic



Sanctioned



**Human Rights
Violence**

themselves and their companies into sensitive altruistic entities. Positive change will only take place if it is supported and justified by sustainable economic incentive.

Given the hard unfortunate fact that we cannot eliminate evil, our next best option is to incentivize good with the intention that good will drive out evil. Ethical certification can accomplish this because it enables good behavior to be turned into profit. Without ethical certification, what is the economic benefit in being good? From a purely business perspective, why increase expenses to be good, if no one knows it and you can't get more money for it? On the other hand, if you can certify your goodness and get more money for it, then it pays for you to be good. That payment is the economic justification that will drive the shift to ethical behavior.

TRIPLE X ETHICAL CERTS

Consider what happened with excellent cut diamonds. The American Gem Society (AGS) came out with triple zero's and then Gemological Institute of America (GIA) came out with triple X's. Before the excellent cut certification game began, cutters didn't cut to such excellent standards. Only after excellent certification was established and communicated through certification did the quality of cutting levels significantly increase. That is because triple X certs brought a higher price, not because cutters altruistically enjoyed looking at their sparkly well cut diamonds. The certificate justified the higher price. Creating excellent cut diamonds not only became a legitimate way to add value, it became an integral part of the marketing and branding proposition of many companies. Tens of millions of dollars have been spent promoting it.

There is no reason we cannot accomplish the same thing with ethical certification. By separating good diamonds from "bad" or "unknown" diamonds through certification we are creating added-value product differentiation. If cutters naturally learned to compete with excellent cuts there is no reason they should not learn to compete with triple X certified fair trade diamonds that give artisanal diggers an excellent deal. When governments or companies that control diamond resources come to realize that they can get a better price for their diamonds if they observe human rights standards, they will be incentivized to do so.

The main idea is to recognize that the way to eliminate bad is to pay more for good. We must also appreciate the fact that innovators in the diamond and jewelry industry are constantly looking for ways to add value to their products. And here is a great opportunity to market and commercialize ethical behavior through certification. You can add value and increase your sales and profits by securing and certifying your ethical supply chain. You can add even more value by recycling gold and diamonds. And still more by trading fair trade gold and diamonds that empower impoverished artisanal diggers.

Best of all, it's not charity and it need not be altruistic. It's economically sustainable because with proper marketing consumers are willing to pay more for ethical jewelry. Free competitive market forces will ensure that suppliers and jewelers develop a correct cost-benefit ratio for ethical jewelry, and society will get the exact level of social and ethical responsibility that it is willing to pay for. In the end, business is about making money, and so is doing the right thing. ♦

RAPAPORT FAIR TRADE PRINCIPLES

- **Pay Fair Wages**
- **Community Benefit**
- **Do No Harm**
- **Independent Auditing**