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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

☒ **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended September 30, 2004

☐ **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the transition period from _____ to _____

Commission File Number: 000-23329

Charles & Colvard, Ltd.

(Exact name of Registrant as specified in its charter)

North Carolina	**56-1928817**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

300 Perimeter Park, Suite A, Morrisville, N.C. 27560
(Address of principal executive offices)

919-468-0399
(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule12b-2 of the Exchange Act). Yes ☐ No ☒

As of October 31, 2004 there were 13,458,589 shares of the Registrant's Common Stock, no par value per share, outstanding.

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Charles & Colvard, Ltd. and Subsidiary

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Part I. Financial Information

Item 1. Financial Statements

Charles & Colvard, Ltd. and Subsidiary
Condensed Consolidated Statements of Operations
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Net sales	$ 5,197,189	$ 3,776,592	$ 15,198,999	$ 12,461,441
Cost of goods sold	1,910,348	1,549,824	5,150,223	4,640,841
Gross profit	3,286,841	2,226,768	10,048,776	7,820,600
Operating expenses:				
Marketing and sales	1,895,329	1,418,890	5,410,027	4,011,734
General and administrative	730,048	664,867	2,174,790	1,851,068
Research and development	2,141	12,081	9,316	19,673
Total operating expenses	2,627,518	2,095,838	7,594,133	5,882,475
Operating income	659,323	130,930	2,454,643	1,938,125
Interest income	34,436	24,484	85,672	88,393
Income before income taxes	693,759	155,414	2,540,315	2,026,518
Income tax expense	390,684	151,208	1,393,392	987,630
Net income	$ 303,075	$ 4,206	$ 1,146,923	$ 1,038,888
Net income per share:				
Basic	$ 0.02	$ 0.00	$ 0.09	$ 0.08
Diluted	$ 0.02	$ 0.00	$ 0.08	$ 0.08
Weighted-average common shares:				
Basic	13,282,258	13,183,970	13,253,504	13,234,933
Diluted	13,728,583	13,482,930	13,607,174	13,550,188

See Notes to Condensed Consolidated Financial Statements.

Charles & Colvard, Ltd. and Subsidiary
Condensed Consolidated Balance Sheets
(Unaudited)

	September 30, 2004	December 31, 2003
Assets		
Current Assets:		
Cash and equivalents	$ 12,365,500	$ 11,559,123
Accounts receivable	4,297,695	3,702,095
Interest receivable	9,787	6,792
Inventories (Note 2)	22,197,386	24,065,992
Inventory on consignment (Note 3)	3,386,568	—
Prepaid expenses	251,719	499,442
Deferred income taxes	235,179	235,179
Total current assets	42,743,834	40,068,623
Long Term Assets:		
Furniture and equipment, net	532,730	453,836
Patent and license rights, net	328,718	274,890
Deferred income taxes	4,324,047	5,649,939
Total long term assets	5,185,495	6,378,665
Total assets	$ 47,929,329	$ 46,447,288
Liabilities and Shareholders' Equity		
Current Liabilities:		
Accounts payable:		
Cree, Inc.	$ 717,773	$ 778,516
Other	610,285	538,943
Accrued payroll	390,050	164,943
Accrued expenses and other liabilities	450,624	392,659
Deferred gross profit	—	448,270
Total current liabilities	2,168,732	2,323,331
Commitments (Note 5)		
Shareholders' Equity:		
Common stock (Note 4)	55,400,864	54,333,287
Additional paid-in capital – stock options	1,829,920	2,407,780
Accumulated deficit	(11,470,187)	(12,617,110)
Total shareholders' equity	45,760,597	44,123,957
Total liabilities and shareholders' equity	$ 47,929,329	$ 46,447,288

See Notes to Condensed Consolidated Financial Statements.

Charles & Colvard, Ltd. and Subsidiary
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Nine Months Ended September 30,	
	2004	2003
Operating Activities:		
Net income	$ 1,146,923	$ 1,038,888
Adjustments:		
Depreciation and amortization	140,520	119,724
Stock option compensation	2,177	24,087
Loss on disposal of long term assets	11,787	—
Provision for deferred income taxes	1,325,892	923,630
Change in operating assets and liabilities:		
Net change in assets	(1,868,834)	(2,612,303)
Net change in liabilities	(154,599)	385,417
Net cash provided by (used in) operating activities	603,866	(120,557)
Investing Activities:		
Purchase of furniture and equipment	(206,114)	(133,007)
Patent and license rights costs	(78,915)	(17,290)
Net cash used in investing activities	(285,029)	(150,297)
Financing Activities:		
Proceeds from exercise of stock options	722,474	55,559
Purchase of common stock	(234,934)	(748,003)
Net cash provided by (used in) financing activities	487,540	(692,444)
Net change in cash and equivalents	806,377	(963,298)
Cash and equivalents, beginning of period	11,559,123	13,282,245
Cash and equivalents, end of period	$ 12,365,500	$ 12,318,947

See Notes to Condensed Consolidated Financial Statements.

Charles & Colvard, Ltd. and Subsidiary
Notes to Condensed Consolidated Financial Statements
(Unaudited)

1. Basis of Presentation

The accompanying unaudited financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America for interim financial information. However, certain information or footnote disclosures normally included in complete financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed, or omitted, pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, the financial statements include all normal recurring adjustments which are necessary for the fair presentation of the results of the interim periods presented. Interim results are not necessarily indicative of results for the year. These financial statements should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2003, as set forth in the Company's Form 10-K, filed with the Securities and Exchange Commission on March 17, 2004.

In preparing financial statements that conform with accounting principles generally accepted in the United States of America, management must make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and amounts of revenues and expenses reflected during the reporting period. Actual results could differ from those estimates.

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary in Hong Kong, Charles & Colvard (HK) Ltd. These financial statements also include the accounts of a Charles & Colvard controlled company in China. All inter-company accounts have been eliminated.

All of the Company's activities are within a single business segment. The following tables present certain data by geographic area:

	Three Months Ended September 30,	
Net Sales (based on destinations of our shipments)	**2004**	**2003**
United States	$ 4,536,190	$ 3,032,212
International	660,999	744,380
Total	$ 5,197,189	$ 3,776,592

	Nine Months Ended September 30,	
Net Sales (based on destinations of our shipments)	**2004**	**2003**
United States	$ 13,102,024	$ 10,536,654
International	2,096,975	1,924,787
Total	$ 15,198,999	$ 12,461,441

Furniture and equipment, Net	**September 30, 2004**	**December 31, 2003**
United States	$ 409,944	$ 340,037
International (All in Asia)	122,786	113,799
Total	$ 532,730	$ 453,836

2. Inventories

Inventories are stated at the lower of cost or market determined on a first in, first out basis. Inventory costs include direct material and labor, inbound freight, purchasing and receiving costs, inspection costs and warehousing costs. A significant amount of inventory must be maintained at all times to be prepared to react to possible customer demand for large purchases and for a variety of jewel styles. In addition, the Company has entered into certain agreements to consign inventory for new or expanding retail opportunities. These consignments will require a significant amount of inventory to be maintained. On average, using historical results as a basis, finished jewels are held in inventory up to 36 months prior to being sold.

The Company currently sells one grade of jewel. The grade is classified as “very good” and consists of near colorless jewels that meet certain standards. Only “very good” jewels are valued in inventory. There is a substantial amount of jewels, including colored jewels, that have not met the quality standards and are not valued in inventory. As market conditions change, including the influences of customer demand, there may be a market for a portion of this unvalued inventory that management may pursue in the future.

Despite the significant amount of jewels in our inventory, obsolescence is not a factor in our inventory valuation. Our jewels do not degrade over time and our inventory consists of the cuts and sizes most commonly used in the jewelry industry. All inventories are carefully reviewed for quality standards before they are entered into finished goods. As the quality of our raw material has improved, so have the standards used to evaluate our finished goods. To ensure our inventory meets our current standards, we review the inventory on an ongoing basis. We established a reserve in 2002 to allow for certain jewels of a slightly lesser quality in our finished goods inventory to be re-cut to increase their quality and/or to satisfy certain cuts/sizes demanded by the customer. The need for adjustments to this reserve is evaluated on a period-by-period basis.

Finished goods are shown net of a reserve for excess jewelry inventory of $100,000 and $130,000 at September 30, 2004 and December 31, 2003, respectively. The Company does not actively market its jewelry inventory. Jewelry inventory value is determined as the amount we would obtain by melting the gold in the jewelry and putting the jewels back into loose stone inventory. In addition, finished goods are shown net of a lower of cost or market reserve of $400,000 at September 30, 2004 and December 31, 2003. This reserve was established to allow for the carat weight loss associated with the re-cutting of a portion of the finished goods inventory. There are certain shapes and sizes of jewels in inventory that will be re-cut to achieve higher quality standards. These jewels can be re-cut into shapes and sizes that have a higher demand without the purchase of additional raw material. The Company’s inventories consist of the following as of September 30, 2004 and December 31, 2003:

	September 30, 2004	December 31, 2003
Raw materials	$ 1,286,852	$ 1,133,805
Work-in-process	4,481,903	4,140,703
Finished goods	16,428,631	18,791,484
Total Inventory	$ 22,197,386	$ 24,065,992

3. Inventory on Consignment

Periodically, the Company sells product to customers on “memo” terms. For shipments on “memo” terms, the customer assumes the risk of loss and has an absolute right of return for a specified period. The Company does not recognize revenue on these transactions until the earlier of (1) the customer informing the Company that it will keep the product or (2) the expiration of the memo period. Prior to 2004, these types of sales have not been significant and the Company recorded them as accounts receivable and deferred gross profit at the time of shipment. In 2004, the Company experienced a significant increase in “memo” sales and determined that, effective January 1, 2004, product shipped to our customers on “memo” terms that do not meet all of the relevant criteria for recording as a sale would be classified as inventory on consignment on the Company’s consolidated balance sheets. The $3,387,000 of inventory on consignment at September 30, 2004 represents potential revenue of $10,666,000 and potential gross profit of $7,279,000.

4. Common Stock

In December 2003, the Board of Directors authorized a follow-on repurchase program for up to 900,000 shares of the Company's common stock. At the discretion of management, the repurchase program can be implemented through open market or privately negotiated transactions at prices at or below prevailing prices. This program will expire in December 2004. There were no shares repurchased during the three months ended September 30, 2004. During the nine months ended September 30, 2004, there were 46,377 shares repurchased at an average price of $5.07. Management will determine the time and extent of any future repurchases based on its evaluation of market conditions and other factors.

5. Commitments

Operating Lease

In March 2004, the Company entered into a seven year lease, beginning in August 2004, for approximately 16,500 square feet of mixed use space from an unaffiliated third party at a base cost of $11,727 per month, plus additional rentals based on the Company's proportionate share of the lessor's operating costs. Terms of the lease provide for escalations of the base monthly rent throughout the lease term, up to $13,546 at August 1, 2010. The lease also provides for twelve different months (August 2004-September 2004 and August 2005-May 2006) throughout the term where no rent will be payable and a $74,000 moving allowance to be paid to the Company. At the Company's discretion, the lease can be extended for three successive five year periods. Finally, the lease provides the Company the right to terminate the lease at the end of five years for $192,000.

The future minimum lease payments of the Company, including its Hong Kong subsidiary, are as follows: $64,000 for the remainder of 2004, $158,000 in 2005, $111,000 in 2006, $149,000 in 2007, $153,000 in 2008, $156,000 in 2009, $160,000 in 2010 and $95,000 in 2011, totaling $1,046,000. Rental expense incurred for operating leases and leases whose terms are less than one year in duration for the three and nine months ended September 30, 2004 was $69,000 and $220,000, respectively. For the three and nine months ended September 30, 2003, such expense was $57,000 and $164,000, respectively.

Purchase Commitment

On June 6, 1997, the Company entered into an Amended and Restated Exclusive Supply Agreement ("Exclusive Supply Agreement") with Cree, Inc. ("Cree"). The Exclusive Supply Agreement has an initial term of ten years which may be extended for an additional ten years by either party, if the Company orders in any 36-month period SiC crystals with an aggregate purchase price in excess of $1 million. The Company has met this order threshold and expects to extend the term of the Exclusive Supply Agreement. In connection with the Exclusive Supply Agreement, the Company has committed to purchase a minimum of 50% (by dollar volume) of its requirements for SiC crystals from Cree. If the Company's orders require Cree to expand beyond specified production levels, the Company must commit to purchase certain minimum quantities. In December 2003, the Company agreed with Cree on a framework for purchases for 2004. The Company is obligated to purchase a minimum quantity of usable material on a quarterly basis if Cree meets certain minimum quality levels. During the three and nine months ended September 30, 2004, we purchased $1.5 million and $4.2 million of raw material from Cree, respectively. We have committed to purchase approximately $2,000,000 of material from Cree during the three months ended December 31, 2004. We have not yet committed to a specific purchase amount for 2005.

6. Stock Based Compensation

The Company measures compensation costs related to employee stock options using the intrinsic value of the equity instrument granted (i.e., the excess of the market price of the stock to be issued over the exercise price of the equity instrument at the date of grant) rather than the fair value of the equity instrument.

In accordance with Accounting Principles Board (APB) Opinion No. 25, and the provision of Statement of Financial Accounting Standards (FAS) No. 123 as applicable to consultants, the Company recorded compensation expense relating to stock options granted with exercise prices less than market value or granted to consultants as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Stock based compensation cost, net of income tax, included in reported net income	$ —	$ 7,134	$ 1,338	$ 14,800

This compensation expense is included in general and administrative expenses in the accompanying Statements of Operations. Had compensation expense for all stock options been determined consistent with the provisions of FAS 123, rather than APB 25, the Company's net income and income per share for the three and nine months ended September 30, 2004 and 2003 would have been recorded to the pro forma amounts indicated below:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2004	2003	2004	2003
Net income:				
As reported	$ 303,075	$ 4,206	$ 1,146,923	$ 1,038,888
Deduct – total stock based compensation expense under fair value method for all awards, net of income tax	79,210	45,500	253,782	427,254
Pro forma net income (loss)	$ 223,865	$ (41,294)	$ 893,141	$ 611,634
Basic net income (loss) per share:				
As reported	$ 0.02	$ 0.00	$ 0.09	$ 0.08
Pro forma	$ 0.02	$ 0.00	$ 0.07	$ 0.05
Diluted net income (loss) per share:				
As reported	$ 0.02	$ 0.00	$ 0.08	$ 0.08
Pro Forma	$ 0.02	$ 0.00	$ 0.07	$ 0.05

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations

This report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended ("Exchange Act"). These forward-looking statements represent our judgment on future events. Our business is subject to business and economic risks and uncertainties that could cause our actual performance and results to differ materially from those expressed or implied by any of the forward-looking statements included herein. These risks and uncertainties include but are not limited to the Company's ability to manage growth effectively, dependence on Cree, Inc. ("Cree") for SiC crystals, dependence on a limited number of distributors such as K&G Creations, Reeves Park, and Stuller Settings, Inc., our limited operating history and dependence on continued growth and consumer acceptance of the Company's products, in addition to the other risks and uncertainties described under the heading "Business Risks" in our Form 10-K for the year ended December 31, 2003, which was filed with the Securities and Exchange Commission on March 17, 2004, and other filings with the Securities and Exchange Commission.

Overview

We manufacture, market and distribute Charles & Colvard created moissanite jewels (also called moissanite) for sale in the worldwide jewelry market. Moissanite, also known by its chemical name, silicon carbide (SiC), is a rare, naturally occurring mineral found primarily in meteorites. As the sole manufacturer of scientifically-made moissanite jewels, our strategy is to create a unique brand image which positions moissanite as a jewel in its own right, distinct from all other jewels based on its fire, brilliance, luster, durability and rarity. Moissanite is being marketed as a new product category and business opportunity for the jewelry trade.

We began shipping moissanite to domestic retail jewelers and international distributors during the second quarter of 1998. During the second quarter of 2000, we changed our domestic distribution model to sell through jewel distributors and jewelry manufacturers rather than directly to retail stores.

In March 2000, we entered into distribution agreements with Stuller Settings, Inc. (Stuller) and Rio Grande, two of the largest suppliers of jewelry-related products to the jewelry industry, for the North American distribution of moissanite. We have also entered into several agreements with domestic jewelry manufacturers, including K&G Creations and Reeves Park, which are two of our largest customers. Through these agreements with Stuller, Rio Grande and jewelry manufacturers and the brand awareness created by our marketing program, we have sought to rapidly increase the introduction of moissanite into the domestic jewelry market while maintaining average selling prices. Although these new distribution and marketing strategies enabled us to achieve profitability in each of the last three completed fiscal years, we have no assurance that these strategies will be successful in the long-term.

In October 2000, we established a wholly-owned subsidiary in Hong Kong, Charles & Colvard (HK) Ltd., for the purpose of gaining better access to the important Far Eastern markets. The importance of having a presence in this market is twofold; Hong Kong is the headquarters city for a very large number of jewelry manufacturing companies with sales and distribution worldwide, and Hong Kong is the gateway to the markets of Mainland China. To enhance our presence in this market, we established a Charles & Colvard controlled company in China in August 2003.

During 2002, we focused on the domestic market, while investing limited resources in certain international markets that management believes represent the most potential. Our 2002 sales were 44% higher than sales in 2001 with sustained profitability and positive cash flow. In 2003, we increased our sales and marketing expenses to expand product awareness and provide support to retailers, thereby accelerating sales growth. The majority of the increased expenses were focused on the domestic market, however we also increased our marketing and sales investment in Hong Kong and China. Our sales were 4% higher in 2003 over 2002. We believe that our increased investment in sales and marketing expenses will lead to an increased growth rate in 2004 and beyond. For the nine months ended September 30, 2004 our sales were 22% higher over the same period last year and we remained profitable. Although our goals for the remainder of 2004 are to continue increasing sales while sustaining profitability, we cannot be sure that either goal will be achieved.

In a joint effort with our direct customers, Quadamas of Los Angeles, and Reeves Park of Minneapolis, we launched a Charles & Colvard moissanite jewelry category at four hundred and sixty JCPenney retail locations on October 1, 2004. JCPenney also offers moissanite jewelry in its catalog and online at www.jcpenney.com. The program will be supported with extensive advertising and public relations activities, as well as by in-store events and promotions. The jewelry placed in this distribution will be on consignment with the retailer. Revenue will be recognized by the Company as the retailer reports to us on a bi-weekly basis the sales of our products to the consumer. As of September 30, 2004, $3.4 million of our inventory on consignment was concentrated primarily with two national retailers.

There are several other new retailers introducing moissanite jewelry during the fourth quarter of 2004, including a 10 store test in the 44 store Daniel's Jewelry, a 3 store test in the 16 store Alvin's Jewelry, a 14 store test in the 41 store Boscov's department stores and a 12 store test at the 40 store Migerobe leased department store chain. Our investment in advertising for the fourth quarter of 2004 to support the holiday promotions for our retail distribution partners is budgeted at approximately $2 million and could result in increased operating expenses as a percentage of sales. This increased investment in advertising and promotion expenses could occur in advance of our generating revenue from these new opportunities, resulting in short-term operating losses for the Company in a given quarter.

Results of Operations

The following tables are intended to illustrate a tabular analysis of certain Consolidated Statement of Operations data as a percentage of sales for both periods presented. A detailed explanation of our results of operations follows these tables:

	Three Months Ended September 30,			
	2004		2003	
Sales	100%	$ 5,197,189	100%	$ 3,776,592
Gross profit	63%	3,286,841	59%	2,226,768
Marketing and sales expenses	36%	1,895,329	38%	1,418,890
General and administrative expenses	14%	730,048	18%	664,867
Operating income	13%	659,323	3%	130,930

	Nine Months Ended September 30,			
	2004		2003	
Sales	100%	$15,198,999	100%	$12,461,441
Gross profit	66%	10,048,776	63%	7,820,600
Marketing and sales expenses	36%	5,410,027	32%	4,011,734
General and administrative expenses	14%	2,174,790	15%	1,851,068
Operating income	16%	2,454,643	16%	1,938,125

Three Months ended September 30, 2004 compared with Three Months ended September 30, 2003

Net sales were $5,197,189 for the three months ended September 30, 2004 compared to $3,776,592 for the three months ended September 30, 2003, an increase of $1,420,597 or 38%. Shipments of moissanite jewels increased 41% to approximately 30,100 carats from 21,400 carats in the same period of 2003. The average selling price per carat was relatively flat (increased by 1%) as we sold a comparable product mix in the same period last year. Domestic sales accounted for approximately 87% and 80% of sales during the three months ended September 30, 2004 and 2003, respectively.

Domestic net sales and carat shipments increased by 50% and 53%, respectively, for the three months ended September 30, 2004 as compared to the three months ended September 30, 2003. Increased domestic shipments are due primarily to a higher volume of sales to Stuller in anticipation of stronger holiday sales following their first release of a twenty page moissanite jewelry catalog for retailers. Our three largest customers, Stuller, K&G Creations, and Reeves Park, accounted for 44%, 27%, and 10%, respectively, of our sales during the three months ended September 30, 2004. K&G Creations and Reeves Park, domestic manufacturing customers, provide moissanite jewels and jewelry to a customer base that consists primarily of television shopping channels and traditional retail stores. Stuller, the largest supplier to domestic independent jewelers, provides both moissanite jewels and a limited line of moissanite jewelry to its customers. While we believe our current relationship with these customers is good, and alternate manufacturers and distributors are available to serve their customer base, a

loss of any of these customers could cause a material adverse effect on our results of operations in a particular period. Based on our inventory on consignment with Reeves Park for JCPenney and planned advertising and promotional support for this program, the Company expects its relationship with Reeves Park (and indirectly JCPenney) to become more significant in future periods and that the Company will become, at least in the short-term, more dependent on maintaining and enhancing its JCPenney program.

International net sales and carat shipments decreased by 11% and 10%, respectively, for the three months ended September 30, 2004 as compared to the three months ended September 30, 2003. Decreased shipments into Taiwan, Thailand, and India were partially offset by increased shipments into Singapore, England, and Australia.

Our gross profit margin was 63.2 % for the three months ended September 30, 2004 compared to 59.0% for the three months ended September 30, 2003. The increased gross margin percentage was primarily caused by lower cost inventory items being relieved from inventory under our first-in, first-out accounting policy. Future gross margins will fluctuate based upon our average selling price per carat and the costs being relieved from inventory under our first-in, first-out accounting policy. The costs being relieved from inventory should trend lower over time, with variations quarter to quarter, as we have achieved declining production costs per carat over the past three years.

Marketing and sales expenses were $1,895,329 for the three months ended September 30, 2004 compared to $1,418,890 for the three months ended September 30, 2003, an increase of $476,439 or 34%. As a percentage of sales, these expenses decreased to 36% from 38% in the same period of 2003. The primary reasons for the increased expenses are $310,000 of increased advertising expenses to promote customer sales opportunities at new and existing retailers, $101,000 of increased co-op advertising expense, $71,000 of increased costs associated with our offices in Hong Kong and China, partially offset by $185,000 of advertising production costs incurred during 2003, not present in 2004, associated with the redesign of our advertising message. Our investment in advertising for the fourth quarter of 2004 to support holiday promotions for our retail distribution partners is budgeted at approximately $2 million and could result in increased operating expenses as a percentage of sales. This increased investment in advertising and promotion expenses could occur in advance of our generating revenue from these new opportunities, resulting in short-term operating losses for the Company in a given quarter.

General and administrative expenses were $730,048 for the three months ended September 30, 2004 compared to $664,867 for the three months ended September 30, 2003, an increase of $65,181 or 10%. As a percentage of sales, these expenses decreased to 14% from 18% in the same period of 2003. The increase in expenses is primarily attributable to increased professional fees, partially offset by $187,000 of legal costs incurred during 2003, not present in 2004, associated with now settled litigation.

Interest income was $34,436 for the three months ended September 30, 2004 compared to $24,484 for the three months ended September 30, 2003, an increase of $9,952 or 41%. This increase resulted from a higher interest rate earned on our cash balances.

Our effective income tax rate for the three months ended September 30, 2004 was 56% compared to 97% for the three months ended September 30, 2003. Our statutory tax rate is 38.5% and consists of the Federal income tax rate of 34% and North Carolina income tax rate of 4.5%, net of the federal benefit. Our effective income tax rate is higher than our statutory rate primarily due to our inability to currently recognize an income tax benefit for our operating losses in Hong Kong and China. We cannot recognize this income tax benefit due to the uncertainty of generating sufficient future taxable income in these countries to offset the existing losses. Although the net losses in Hong Kong and China are comparable for 2003 and 2004, the 2003 effective rate is much higher than 2004 due to our lower US pretax income in 2003. Our 2004 effective rate is also negatively impacted by additional income tax expense associated with the profit on inter-company sales to our subsidiary that are eliminated in consolidation.

Nine Months ended September 30, 2004 compared with Nine Months ended September 30, 2003

Net sales were $15,198,999 for the nine months ended September 30, 2004 compared to $12,461,441 for the nine months ended September 30, 2003, an increase of $2,737,558 or 22%. Shipments of moissanite jewels also increased 23% to approximately 86,000 carats from 70,000 carats in the same period of 2003. The average selling price per carat was relatively flat (decreased by 1%) as we sold a comparable product mix in the same period last year. Domestic sales accounted for approximately 86% and 85% of sales during the nine months ended September 30, 2004 and 2003, respectively. Domestic carat shipments increased by 26% and international carat shipments increased by 6%.

Increased domestic shipments are due primarily to a higher volume of sales to Stuller in anticipation of stronger holiday sales following their first release of a moissanite jewelry catalog for retailers, as well as expanded distribution into a number of new retailers and increased volume with our existing retailers. Increased international shipments into Singapore and Korea were offset by decreased shipments into Thailand. Our three largest customers, K&G Creations, Stuller and Reeves Park, accounted for 34%, 31%, and 13%, respectively, of our sales during the nine months ended September 30, 2004. K&G Creations and Reeves Park, domestic manufacturing customers, provide moissanite jewels and jewelry to a customer base that consists primarily of, television shopping channels and traditional retail stores. Stuller, the largest supplier to domestic independent jewelers, provides both moissanite jewels and a limited line of moissanite jewelry to its customers. While we believe our current relationship with these customers is good, and alternate manufacturers and distributors are available to serve their customer base, a loss of any of these customers could cause a material adverse effect on our results of operations in a particular period. Based on our inventory on consignment with Reeves Park for JCPenney and planned advertising and promotional support for this program, the Company expects its relationship with Reeves Park (and indirectly JCPenney) to become more significant in future periods and that the Company will become, at least in the short-term, more dependent on maintaining and enhancing its JCPenney program.

Our gross profit margin was 66.1% for the nine months ended September 30, 2004 compared to 62.8% for the nine months ended September 30, 2003. The increased gross margin percentage was primarily caused by lower cost inventory items being relieved from inventory under our first-in, first-out accounting policy. Future gross margins will fluctuate based upon our average selling price per carat and the costs being relieved from inventory under our first-in, first-out accounting policy. The costs being relieved from inventory should trend lower over time, with variations quarter to quarter, as we have achieved declining production costs over the past three years.

Marketing and sales expenses were $5,410,027 for the nine months ended September 30, 2004 compared to $4,011,734 for the nine months ended September 30, 2003, an increase of $1,398,293 or 35%. As a percentage of sales, these expenses increased to 36% from 32% in the same period of 2003. The primary reasons for the increase are $942,000 of increased advertising expenses to promote customer sales opportunities at new and existing retailers and $228,000 of increased costs associated with our offices in Hong Kong and China, partially offset by $275,000 of advertising production costs in 2003 associated with the redesign of our advertising message. Our investment in advertising for the fourth quarter of 2004 to support holiday promotions for our retail distribution partners is budgeted at $2 million and could result in increased operating expenses as a percentage of sales. This increased investment in advertising and promotion expenses could occur in advance of our generating revenue from these new opportunities, resulting in short-term operating losses for the Company in a given quarter.

General and administrative expenses were $2,174,790 for the nine months ended September 30, 2004 compared to $1,851,068 for the nine months ended September 30, 2003, an increase of $323,722 or 17%. As a percentage of sales, these expenses decreased to 14% from 15% in the same period of 2003. The increase in expenses is primarily due to $246,000 of increased professional fees and $136,000 of accrued compensation cost in 2004 under our Executive Compensation Plan. There were no costs recorded in 2003 under the Executive Compensation Plan as the Company did not meet its 2003 internal sales and profit goals. The net increase in general and administrative expenses was reduced by a decrease in legal fees over the relevant period of $189,000 related to the now settled litigation.

Net interest income was $85,672 for the nine months ended September 30, 2004 compared to $88,393 for the nine months ended September 30, 2003, a decrease of $2,721 or 3%. This decrease resulted from a lower interest rate earned on our cash balances.

Our effective income tax rate for the nine months ended September 30, 2004 was 55% compared to 49% for the nine months ended September 30, 2003. Our statutory tax rate is 38.5% and consists of the Federal income tax rate of 34% and North Carolina income tax rate of 4.5%, net of the federal benefit. Our effective income tax rate is higher than our statutory rate primarily due to our inability to currently recognize an income tax benefit for our operating losses in Hong Kong and China. We cannot recognize this income tax benefit due to the uncertainty of generating sufficient future taxable income in these countries to offset the existing losses. The increase in our effective income tax rate from 49% to 55% is primarily due to additional income tax expense associated with the profit on inter-company sales to our subsidiary that are eliminated in consolidation.

Liquidity and Capital Resources

At September 30, 2004, we had $12.4 million of cash and cash equivalents and $40.6 million of working capital. Cash and inventory account for 89% of our current assets. Our principal sources of liquidity are cash on hand and cash generated by operations. During the nine months ended September 30, 2004, $603,866 of cash was provided by operations. The primary reason for the increase in cash was pretax income of $2,540,315, partially offset by a $1,517,962 increase in inventory and a $598,595 increase in receivables. In addition, we used $206,114 of cash for the purchase of furniture and equipment and $78,915 on patent and license rights costs (primarily for the issuance of our patents in the countries of the European Union).

Income tax payments for the nine months ended September 30, 2004 were limited to $67,500 due to the utilization of a portion of the Company's net operating loss ("NOL") carryforwards to offset the taxable income generated during that period by our US operations. As of December 31, 2003, we had a United States NOL carryforward of approximately $13.1 million, which expires between 2012 and 2020. Federal and state income tax payments will be limited in future periods to primarily alternative minimum tax payments until the NOL has been completely utilized.

Periodically, the Company sells product to customers on "memo" terms. For shipments on "memo" terms, the customer assumes the risk of loss and has an absolute right of return for a specified period. The Company does not recognize revenue on these transactions until the earlier of (1) the customer informing the Company that it will keep the product or (2) the expiration of the memo period. Prior to 2004, these types of sales have not been significant and the Company recorded them as accounts receivable and deferred gross profit at the time of shipment. At December 31, 2003, $889,000 of our receivables related to sales on "memo" terms and there was $448,000 of deferred gross profit on the balance sheet. In 2004, the Company experienced a significant increase in "memo" sales and determined that, effective January 1, 2004, product shipped to our customers on "memo" terms that do not meet all of the relevant criteria for recording as a sale would be classified as inventory on consignment on the Company's consolidated balance sheets. The $3,387,000 of inventory on consignment at September 30, 2004 represents potential revenue of $10,666,000 and potential gross profit of $7,279,000. Since "memo" transactions were not material prior to 2004, we have not reclassified our December 31, 2003 balance sheet to conform to the 2004 presentation.

On average, using historical results as a basis, finished jewels are held in inventory up to 36 months prior to being sold. As sales increase, we expect the number of months finished jewels are held in inventory to decrease. Prior to 2001 the buildup in the Company's inventory was a material use of the company's cash flow. Management considered this investment in inventory essential to be able to meet the orders of its expanding customer base and to fulfill the new and expanding requests from our customers for consigned inventory. It is management's opinion that total inventory should decrease slightly over time from current levels due to forecasted sales increases, and that inventory turnover should increase, thereby not requiring a significant use of working capital and providing a source of future cash flow. However, the Company will maintain inventories to support its forecasted increases in demand for its product.

In December 2003, we agreed with Cree on a framework for purchases for 2004. The Company is obligated to purchase a minimum quantity of usable material on a quarterly basis if Cree meets certain minimum quality levels. During the three and nine months ended September 30, 2004, we purchased $1.5 million and $4.2 million of raw material from Cree, respectively. We have committed to purchase approximately $2,000,000 of material from Cree during the three months ended December 31, 2004. We have not yet committed to a specific purchase amount for 2005.

In December 2003, the Board of Directors authorized a follow-on repurchase program for up to 900,000 shares of the Company's common stock. At the discretion of management, the repurchase program can be implemented through open market or privately negotiated transactions at prices at or below prevailing prices. This program will expire in December 2004. There were no shares repurchased during the three months ended September 30, 2004. During the nine months ended September 30, 2004, there were 46,377 shares repurchased at an average price of $5.07. Management will determine the time and extent of any future repurchases based on its evaluation of market conditions and other factors.

Based on our cash and cash equivalents and other working capital, management believes that our existing capital resources are adequate to satisfy our capital requirements for at least the next 12 months.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

We believe that our exposure to market risk for changes in interest rates is not significant because our investments are limited to highly liquid instruments with maturities of three months or less. At September 30, 2004, we had approximately $10.8 million of short-term investments, primarily money market funds, classified as cash and equivalents. All of our transactions with international customers and suppliers are denominated in U.S. dollars.

Item 4: Controls and Procedures

(a) Evaluation of disclosure controls and procedures

As of September 30, 2004, the Company's Chief Executive Officer and the Chief Financial Officer evaluated the effectiveness of the Company's disclosure controls and procedures in accordance with Rule 13a-15 under the Exchange Act. Based on their evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures enable the Company to record, summarize and report in a timely manner the information that the Company is required to disclose in its Exchange Act reports.

(b) Changes in internal control over financial reporting

There were no changes in the Company's internal control over financial reporting that occurred during the period covered by this report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Part II - Other Information

Item 2(e). Purchase of Equity Securities

Charles & Colvard did not make any purchases of its common stock during the three months ended September 30, 2004, however, there is an authorized repurchase program and the related activity in this program in 2004 was as follows:

Period	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly-Announced Plan	Maximum Number of Shares That May Yet be Purchased Under the Plan (1)
July 1, 2004 – July 31, 2004	—	—	—	853,623
August 1, 2004 – August 31, 2004	—	—	—	853,623
September 1, 2004 – September 30, 2004	—	—	—	853,623
Total for 2004	46,377	$ 5.07	46,377	

(1) In December 2003, the Board of Directors authorized the repurchase of up to 900,000 shares of the Company's common stock through open market or privately negotiated transactions at prices at or below prevailing prices. This plan expires in December 2004. On May 17, 2004, the Company announced that pursuant to this authority it had entered into a written stock repurchase agreement with Raymond James & Associates, Inc. to provide for the repurchase of certain amounts of the Company's stock in accordance with rules 10b5-1 and 10b5-18 of the Securities and Exchange Act of 1934. At current trading prices, no additional purchases are expected to be made pursuant to the Raymond James Agreement. However, management is still authorized to make additional share repurchases pursuant to the Board of Director's authority expiring December 2004.

Item 6: Exhibits

(a) Exhibits

Exhibit No.	Description
10.64	Manufacturing Agreement, dated August 12, 2004, between Reeves Park, Inc. and Charles & Colvard, Ltd.
10.65	Security Agreement, dated August 15, 2004, between Reeves Park, Inc. and Charles & Colvard, Ltd.
10.66	Consignment Agreement, dated August 16, 2004, between Reeves Park, Inc. and Charles & Colvard, Ltd.*
10.67	Amendment to Manufacturing Agreement, dated November 8, 2004, between Reeves Park and Charles & Colvard, Ltd.
10.68	First Amendment to Security Agreement, dated November 8, 2004, between Reeves Park and Charles & Colvard, Ltd.
31.1	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) or 15d-14(a) of the Exchange Act, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* The registrant has requested that certain portions of this exhibit be given confidential treatment.

Table of Contents

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Charles & Colvard, Ltd.

Date: November 9, 2004

/s/ Robert S. Thomas

Robert S. Thomas
President & Chief Executive Officer
(Principal Executive Officer)

Date: November 9, 2004

/s/ James R. Braun

James R. Braun
Vice President of Finance & Chief Financial Officer
(Principal Accounting Officer)

Exhibit 10.64

CHARLES & COLVARD®
Created
MOISSANITE

August 12, 2004

Mr. Klaus H. Jung
Reeves Park, Inc.
5050 Lincoln Drive
Suite 470
Edina, MN 55436

Re: Manufacturing Agreement

Dear Klaus:

This letter agreement sets forth the terms and conditions of the sale of Charles & Colvard created Moissanite by Charles & Colvard, Ltd. ("C&C"), to Reeves Park, Inc. ("Buyer"). This letter, together with the attached price list, terms and conditions, and License Agreement constitutes the entire agreement (the "Agreement") between our companies.

C&C hereby agrees to sell to Buyer commercially reasonable amounts of moissanite for use by Buyer in the manufacturing of fine jewelry, and C&C agrees to:

1. Provide the staff of Buyer with any required training concerning moissanite, C&C's marketing strategy and C&C's product positioning for moissanite.

Buyer hereby recognizes, and agrees to cooperate with C&C in the protection of, all C&C trademarks, copyrights and intellectual property. Further, Buyer agrees to include Charles & Colvard created Moissanite in its catalog and trade show presentations for the term of this Agreement. Buyer acknowledges receipt of the brand identity guidelines provided by C&C and agrees to market Charles & Colvard created Moissanite in a manner consistent with such guidelines. Additionally, Buyer shall use commercially reasonable efforts to ensure its customers abide by such guidelines.

Buyer specifically agrees to NOT sell C&C created moissanite as loose stones, and will sell moissanite only in jewelry mountings.

This Agreement shall terminate on August 11, 2005 pursuant to Section 7 under Terms and Conditions or notice by either party to the other party of its intent not to renew the Agreement at least 30 days prior to the end of the then current one-year term.

If the forgoing meets with your understanding of our agreement, please sign and return one copy of this letter for my files.

Charles & Colvard, Ltd.	Agreed and Accepted by "Buyer"
By: */s/ Robert S. Thomas*	By: */s/ Klaus Jung*
Name: Robert S. Thomas	Name: Klaus Jung
Title: President & CEO	Title: President

3800 Gateway Boulevard, Suite 310 Morrisville, NC 27560 Telephone 919.468.0399
Facsimile 919.468.0486 www.moissanite.com

TERMS AND CONDITIONS

1. ACCEPTANCE OF ORDERS. C&C's acceptance of all orders for Charles & Colvard created Moissanite (the "Product") and all offers and sales by C&C are subject to and expressly conditioned upon Buyer's acceptance of the terms and conditions of this Agreement, and Buyer's acceptance of any offer by C&C must be made on such terms and conditions exactly as offered by C&C. Any of Buyer's terms and conditions which are different from or in addition to those contained in this Agreement are objected to by C&C and shall be of no effect unless specifically agreed to in writing by C&C. Shipment of the Product shall not be construed as acceptance of any of Buyer's terms and conditions which are different from or in addition to those contained herein. Buyer's acceptance of the Product furnished by C&C pursuant hereto shall constitute Buyer's acceptance of the terms and conditions of this Agreement.

This Agreement shall be governed by and construed under the laws of the State of North Carolina as if made and to be performed entirely within such state.

2. PRICES. The prices stated in this Agreement are F.O.B. C&C's manufacturing facilities and do not include transportation, insurance or any sales, use, excise or other taxes, duties, fees or assessments imposed by any jurisdiction. All applicable taxes shall be paid by Buyer, unless Buyer provides C&C with appropriate tax exemption certificates. Buyer shall promptly reimburse C&C for any taxes paid by C&C which are the responsibility of Buyer hereunder. All prices and other terms are subject to correction for typographical or clerical errors. Prices are subject to change annually at the sole discretion of C&C.

3. TERMS OF SALE & PAYMENT. C&C shall provide the Product in the "very good" grade which includes slight possible color saturations and inclusions. Buyer shall pay for the Product in cash upon delivery, unless an earlier or later time for payment is specified in the Agreement (in which case payment shall be due at the time so specified). Each shipment shall be considered a separate and independent transaction and payment for each shipment shall be due accordingly.

C&C may, at its option, elect to extend credit to Buyer. If C&C extends credit to Buyer, invoices will be issued upon shipment and payment shall be due in full within thirty (30) days from the invoice date. C&C reserves the right to change the amount of or withdraw any credit extended to Buyer at any time without notice to Buyer.

Amounts not paid when due shall be subject to interest at the rate of one and one-half percent (1 ½%) per month or, if less, the maximum rate permitted by law.

In the event of the bankruptcy or insolvency of Buyer, or the filing of any proceeding by or against Buyer under any bankruptcy, insolvency or receivership law, or in the event Buyer makes an assignment for the benefit of creditors, C&C may, at its election and without prejudice to any other right or remedy, exercise all rights and remedies granted to C&C in Section 7 as in the case of a default by Buyer under this Agreement.

4. DELIVERY, TITLE AND RISK OF LOSS. All sales hereunder shall be F.O.B. C&C's manufacturing facilities, and the Product shall be deemed delivered to Buyer when delivered to the transportation company at the C&C's manufacturing facilities. Unless otherwise agreed in writing by C&C, all transportation charges and expenses shall be paid by Buyer, including the cost of any insurance against loss or damage in transit which C&C may obtain on Buyer's behalf. C&C reserves the right to ship the Product freight collect.

C&C hereby reserves, and Buyer hereby grants to C&C, a purchase money security interest in all Product purchased under this Agreement, together with all proceeds thereof, including insurance proceeds. Such security interest secures all of Buyer's obligations arising under this Agreement, and any other agreements between Buyer and C&C, until all amounts due C&C hereunder have been paid in full. Buyer agrees to promptly execute and deliver appropriate financing statements evidencing C&C's security interest upon C&C's request.

Subject to the security interest reserved to C&C, title and risk of loss and/or damage to the Product shall pass to Buyer upon delivery of the Product to the transportation company at C&C's manufacturing facilities. Confiscation or destruction of or damage to the Product shall not release, reduce or in any way affect the liability of Buyer hereunder. In the event Buyer rejects or revokes acceptance of any Product for any reason, all risk of loss and/or damage to such Product shall nonetheless remain with Buyer unless and until the same are returned at Buyer's expense to such place as C&C may designate in writing.

Buyer shall inspect all Product promptly upon receipt and file claims with the transportation company in the event there is evidence of shipping damage.

5. PERFORMANCE. C&C shall make a reasonable effort to observe the dates specified herein or such later dates as may be agreed to by Buyer for delivery or other performance, but C&C shall not be liable for any delay in delivery or failure to perform due to acceptance of prior orders, strike, lockout, riot, war, fire, act of God, accident, delays caused by any subcontractor or supplier or by Buyer, technical difficulties, failure or breakdown of machinery or components necessary to order completion, inability to obtain or substantial rises in the price of labor or materials or manufacturing facilities, or compliance with any law, regulation, order or direction, whether valid or invalid, of any governmental authority or instrumentality thereof, or due to any unforeseen

circumstances or any causes beyond its control, whether similar or dissimilar to the foregoing and whether or not foreseen. No penalty of any kind shall be effective against C&C for delay or failure; provided, however, that if the delay or failure extends beyond six (6) months from the originally scheduled date either party may, with written notice to the other, terminate this Agreement without further liability.

6. ACCEPTANCE. All Product delivered hereunder shall be deemed accepted by Buyer as conforming to this Agreement, and Buyer shall have no right to revoke any acceptance, unless written notice of the claimed nonconformity is received by C&C within twenty (20) days of delivery thereof. Notwithstanding the foregoing, any use of the Product by Buyer, its agents, employees, contractors or licensees, for any purpose, after delivery thereof, shall constitute acceptance of that product by Buyer.

7. DEFAULT AND TERMINATION. Buyer may terminate this Agreement if C&C materially defaults in the performance of its obligations hereunder and fails to cure such default within sixty (60) days after written notice thereof from Buyer. Such termination shall be Buyer's sole remedy in the event of a default by C&C.

Buyer shall be deemed in material default under this Agreement if Buyer fails to pay any amounts when due hereunder, cancels or attempts to cancel this Agreement prior to delivery or refuses delivery or otherwise fails to perform its obligations hereunder or fails to pay C&C any sums due under any other agreement or otherwise. In the event of a material default by Buyer, C&C may, upon written notice to Buyer, (1) suspend its performance and withhold shipments, in whole or in part, (2) terminate this Agreement, (3) declare all sums owing to C&C immediately due and payable and/or (4) recall Product in transit, retake same and repossess any Product held by C&C for Buyer's account, without the necessity of any other proceedings, and Buyer agrees that all Product so recalled, taken or repossessed shall be the property of C&C, provided that Buyer is given credit therefore. Exercise of any of the foregoing remedies shall not be construed as limiting, in any manner, any of the rights or remedies available to C&C under the Uniform Commercial Code or other laws.

8. PATENTS AND OTHER INTELLECTUAL PROPERTY RIGHTS. The sale of the Product hereunder does not convey any expressed or implied license under any patent, copyright, trademark or other proprietary rights owned or controlled by C&C, whether relating to the Product sold or any manufacturing process or other matter. All rights under any such patent, copyright, trademark or other proprietary rights are expressly reserved by C&C.

9. MANUFACTURING PRACTICES. When engaged in the design, production or distribution of any jewelry containing the Product, Buyer and its agents, sub-manufacturers, or contractors involved in the design, production, or distribution of jewelry containing the Product shall not engage in the use of child labor, prison or any type of forced labor, or any other labor practices that may violate the sensibilities of the American public. Buyer shall certify to C&C from time to time, upon C&C's demand, that it, as well as its agents, sub-manufacturers, or contractors involved in the design, production, or distribution of the Product does not engage in such labor practices. Upon C&C's demand, Buyer shall also certify that all rules and regulations, as well as all measures of safety, health, and labor practices, recommended or requested by the relevant authorities of Buyer's governing municipalities, as well as the governing municipalities of Buyer's agents, sub-manufacturers, or contractors involved in the design, production or distribution of the Product have been complied with. Buyer shall indemnify C&C for, and hold C&C harmless from, all claims, actions or demands arising from any action or omission that occurs on Buyer's, its agent's, sub-manufacturer's or contractor's premises. Furthermore, C&C guarantees that no radioactive process has been utilized in the manufacturing process of the Product.

10. LIMITED WARRANTY. Other than as set out herein, C&C makes no warranty or other representation concerning the Product; and, other than as specifically provided in this Agreement, C&C's liability is limited to replacement of any Product not conforming to the specifications set out in Section 3 of this Agreement upon their return to C&C. Buyer reserves the right to return any Product not conforming to the specifications set out herein to C&C. C&C shall pay return shipping, handling and insurance on the replacements for the Product that does not meet the specifications in Section 3. All returned Product must be accompanied by a return authorization number that should be displayed prominently on the outside of the package. All other shipping, handling and insurance for returns shall be paid by Buyer. The warranty set forth in this Section 10 is intended solely for the benefit of Buyer. All claims hereunder shall be made by Buyer and may not be made by Buyer's customers. ***THE WARRANTY SET FORTH ABOVE IS IN LIEU OF ALL OTHER WARRANTIES, EXPRESSED OR IMPLIED, WHICH ARE HEREBY DISCLAIMED AND EXCLUDED BY C&C, INCLUDING, WITHOUT LIMITATION, ANY WARRANTY OF MERCHANTABILITY OF FITNESS FOR A PARTICULAR PURPOSE OF USE.***

Exhibit A

LICENSING AGREEMENT

This Agreement is by and between Charles & Colvard, Ltd., having its principal office at 3800 Gateway Boulevard, Suite 310, Morrisville, North Carolina ("Licensor") and Reeves Park, Inc. and 5050 Lincoln Drive, Suite 470, Edina, MN 55436 ("Licensee"):

A. Licensor desires to license certain of its trademarks, which are set forth on the attached Schedule 13 (a), Exhibit 1 ("Trademarks") and certain copyrights in works, which are set forth in the attached Schedule 13 (a) Exhibit 2 ("Copyright Works").

B. The Trademarks and Copyright Works are valuable rights of the Licensor. Licensor desires to and Licensee agrees to protect the integrity of the Trademarks and Copyright Works so as to avoid consumer confusion and to distinguish Licensor's products from those of its competitors. Licensee shall exercise this protection by conforming to certain guidelines concerning the use of the Trademarks and Copyright Works, as described on the attached Exhibit 3 ("Brand Identity Guidelines").

C. Licensee wishes to use the Trademarks and Copyright Works in connection with the advertising, promotion and sale of Licensee's products which incorporate Charles & Colvard created Moissanite jewels.

Now, therefore, in consideration of the mutual promises of the Agreement, the parties agree as follows:

1. **GRANT OF LICENSE**

Licensor grants to Licensee, subject to the terms and conditions of this Agreement, the non-exclusive right to use the Trademarks and Copyright Works listed in Exhibits 1 & 2, in connection with Licensee's advertisement, promotion and sale of Licensee's products which incorporate Charles & Colvard created Moissanite jewels. Licensee may use the Trademarks and Copyright Works: (i) only in the United States of America without reasonable prior written notice to Licensor; (ii) only in connection with Licensee's advertisements, promotional and sales materials (including but not limited to online advertising and promotion) (collectively "Advertisements"); and (iii) only as permitted by this Agreement. Licensee may make no other use of the Trademarks and Copyright Works and Licensor reserves any rights, benefits and opportunities not expressly granted to Licensee under this Agreement.

2. **TERM AND TERMINATION**

The term of this Agreement shall begin on the date of this Agreement and end simultaneously with the termination of the Manufacturing Agreement of even date hereof between Licensor and Licensee concerning manufacture of jewelry incorporating Charles & Colvard created Moissanite Jewels, unless sooner terminated. Licensor may terminate this Agreement at any time and for any reason.

3. **ROYALTIES**

Licensee is not obligated to pay Licensor any royalties for the use of the Trademarks or Copyright Works under the terms of this agreement.

4. **QUALITY AND APPROVAL**

(a) Purpose of Quality Control. In order to maintain the quality and reputation of the Trademarks and the rights in the Copyright Works, all Advertisements must have Licensor's prior approval.

(b) Pre-approved Materials. All advertising, promotional and sales material bearing or incorporating the Trademarks and/or Copyright Works which are supplied to Licensee directly by Licensor, without change or alteration of any kind, shall be considered approved.

(c) Materials Requiring Prior Approval. Licensor and Licensee shall cooperate in the development by Licensee of Advertisements containing the Trademarks and/or Copyright Works which are not pre-approved to facilitate the timely approval of such materials. Licensee shall submit to Licensor for prior approval any and all Advertisements containing or bearing the Trademarks and/or Copyright Works which are not pre-approved. Licensee shall not use the Trademarks and/or Copyright Works in connection with Advertisements before obtaining Licensor's approval. Licensor may withhold its approval for any reason. If Licensor fails to approve a submittal within twenty (20) days after receipt of Licensee's submission, such failure shall constitute a disapproval of the submittal.

(d) Changes. If during the term of this Agreement there is to be any change to Advertisements bearing or incorporating the Trademarks and/or Copyright Works (even if such changes do not relate to a change in the display of Trademarks and Copyright Works) after the initial approval, the changed Advertisements shall be considered new proposed Advertisements and Licensee must comply with the provisions of Section 4(b) prior to using the changed Advertisements.

5. **TRADEMARK AND COPYRIGHT OWNERSHIP AND NOTICES**

(a) Licensee's use of the Trademarks shall, depending upon the directions provided by Licensor, in every instance be combined with one of the following notices: (i) Reg. U.S. Pat. & TM. Off.; (ii) ®; (iii) Trademark of Charles & Colvard; (iv) TM; or (v) such other similar language as shall have Licensor's prior approval.

(b) Licensor and Licensee agree and intend that all material, including without limitation all artwork and designs, created by Licensee or any other person or entity retained or employed by Licensee bearing, displaying or containing the Trademarks or Copyright Works ("Copyright Materials") are works made for hire within the meaning of the United States Copyright Act and shall be the property of Licensor, unencumbered by moral rights. As owner, Licensor shall be entitled to use and license others to use the Copyright Materials. To the extent the Copyright Materials are not works made for hire, Licensee hereby irrevocably assigns to Licensor, its successors and assigns, the entire right, title and interest in perpetuity throughout the world in and to any and all rights, including all copyrights and related rights in such Copyright Materials. Licensee warrants and represents that: (i) the Copyright Materials are completely original and are not based on or derived from the work or works of any third party; (ii) only Licensee created or contributed to the Copyright Materials; (iii) the Copyright Materials are an original work of authorship, and no royalties, honorariums or fees were, are or will be payable to other persons by reason of Licensor's use of the Copyright Materials; and (iv) the Copyright Materials do not infringe the rights of others. If Licensee wishes to retain a third party to assist Licensee in the creation of the Copyright Materials, Licensee shall obtain Licensor's prior approval and shall obtain and provide to Licensor an original assignment from the third party to Licensor of the third party's rights in the Copyright Materials.

(c) The following notice (or such other notice as shall have Licensor's prior approval) shall appear in connection with the Copyright Works and/or Copyright Materials at least once on Advertisements using Copyright Works and/or Copyright Materials: © **(year of first publication) Charles & Colvard® All Rights Reserved.**

(d) Licensee shall not use any language or display the Trademarks, Copyright Works and Copyright Materials in such a way as to create the impression that the Trademarks, Copyright Works and Copyright Materials belong to Licensee. Licensee shall not use any Trademark, any trademark incorporating all or any part of the Trademarks, the Copyright Works or the Copyright Materials on any business sign, business cards, stationery or forms (except as licensed herein), or as the name of Licensee's corporation or business or any division thereof, unless otherwise agreed by Licensor in writing. Licensee waives all claims to any rights in materials bearing the Trademarks, Copyright Works and Copyright Materials beyond the limited permission to use the Trademarks granted in this Agreement.

(e) Upon Licensor's request and without further consideration, Licensee agrees to execute any additional documents proposed by Licensor, or do or have done all things as may be requested by Licensor to vest and/or confirm the sole and exclusive ownership of all right, title and interest, including copyrights and related rights in and to the Copyright Materials in favor of Licensor, its successors and assigns.

(f) Licensee hereby irrevocably assigns and transfers to Licensor, or if applicable, Licensee agrees to obtain an appropriate assignment by an author to the Licensor, to the extent permissible in any jurisdiction, any and all moral rights in and to the Copyright Materials and, where non-assignable, Licensee hereby irrevocably waives, or if applicable, Licensee agrees to obtain an appropriate waiver by any authors of, in favor of the Licensor, its successors, assigns, employees, agents, representatives and/or any persons acting under Licensor's authority, any and all moral rights in such Copyright Materials.

(g) The use of any word, name, symbol or device by Licensee to identify or distinguish any of Licensor's products shall inure to the benefit of Licensor. The use of any such word, name, symbol or device in connection with Advertisements shall be made only with Licensor's prior approval. All trademark rights in any such word, name, symbol or device shall belong to Licensor and shall be exercised by Licensee only pursuant to Licensor's prior, written approval. At its sole discretion, Licensor may amend Exhibit 1 to include any such word, name, symbol or device.

6. **RIGHTS IN THE TRADEMARKS AND COPYRIGHT WORKS**

(a) Licensee shall not make any unlicensed use, file any application for registration or claim any other proprietary right to any of the Trademarks, Copyright Works, Copyright Materials or derivations or adaptations thereof, or any marks or works similar thereto.

(b) Licensee acknowledges the validity of and Licensor's title to the Trademarks, Copyright Works and Copyright Materials and shall not do or suffer to be done any act or thing, which will impair the rights of Licensor in and to the Trademarks, Copyright Works

or Copyright Materials. Licensee shall not acquire and shall not claim any title or any other proprietary right to the Trademarks, Copyright Works, Copyright Materials or in any derivation, adaptation, variation or name thereof by virtue of this license or Licensee's creation or usage.

7. **ELECTRONIC MATERIALS**

(a) CD ROM USE

Charles & Colvard, Ltd. ("Licensor") hereby grants to you ("Licensee") a limited, non-exclusive, royalty-free license to use certain trademarks and certain copyrights in works as are made available by Licensor on specified CD Rom (the "Licensed Materials") solely in connection with the advertising, promotion, and sale of Licensee's products which incorporate Charles & Colvard created Moissanite. Licensee is granted the right to use the Licensed Materials only in conformity with the terms of this agreement and the guidelines concerning the use of Licensor's trademarks and copyright works as described in the Brand Identity Guidelines, as may be amended from time to time. Licensee may make no other use of the Licensed Materials, and Licensor reserves any rights, benefits, and opportunities not expressly granted to Licensee under this agreement.

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Licensor may terminate this agreement at any time and for any reason. Upon termination, Licensee must destroy all copies, electronic or otherwise, of the Licensed Materials and/or any materials incorporating parts thereof. Licensee may terminate this agreement at any time by destroying the Licensed Materials and/or any materials incorporating parts thereof in Licensee's possession.

Licensee agrees to comply with Licensor's standards for controlling the quality of products sold under or in connection with the Licensed Materials.

Licensee may not reverse engineer, modify, or create derivative works based upon the Licensed Materials or any part thereof, except as is specifically permitted in the Brand Identity Guidelines.

The following notice (or such other notice as shall have Licensor's prior written approval) shall appear in connection with the Licensed Materials at least once on all documentation: "Used pursuant to license from Charles & Colvard, Ltd." License shall also use "© (year of first publication) Charles & Colvard, Ltd. All Rights Reserved" in connection with copyright works and ™ or ®, as appropriate, in connection with trademarks.

Furthermore, upon notice from Licensor posted electronically that it has changed the appearance of the Licensed Materials (or any of the trademarks and/or copyright works therein), Licensee shall use only the changed version in any and all materials produced by Licensee within four (4) weeks following Licensor's initial notice.

(b) WEBSITE

Charles & Colvard, Ltd. ("Licensor") hereby grants to you ("Licensee") a limited, non-exclusive, royalty-free license to use certain trademarks and certain copyrights in works as are made available by Licensor for electronic download (the "Licensed Materials") solely in connection with the advertising, promotion, and sale of Licensee's products which incorporate Charles & Colvard created Moissanite. Licensee is granted the right to use the Licensed Materials only in conformity with the terms of this agreement and the guidelines concerning the use of Licensor's trademarks and copyright works as described in the Brand Identity Guidelines, as may be amended from time to time. Licensee may make no other use of the Licensed Materials, and Licensor reserves any rights, benefits, and opportunities not expressly granted to Licensee under this agreement.

The Licensee may not include the Licensed Materials in any electronic files to be distributed or used by others without first obtaining the specific written consent of Licensor. Furthermore, the Licensee shall have no right to, nor shall it attempt to challenge, assign, sublicense, transfer, pledge, lease, rent, or share the rights granted under this License Agreement to or with any third party, in whole or in part, without the prior written consent of Licensor. Licensee acknowledges and agrees that the Licensed Materials (and trademarks and copyrights therein) are proprietary to Licensor and protected under applicable U. S. and foreign laws.

Licensor may terminate this agreement at any time and for any reason. Upon termination, Licensee must destroy all copies, electronic or otherwise, of the Licensed Materials and/or any materials incorporating parts thereof. Licensee may terminate this agreement at any time by destroying the Licensed Materials and/or any materials incorporating parts thereof in Licensee's possession.

Licensee agrees to comply with Licensor's standards for controlling the quality of products sold under or in connection with the Licensed Materials.

Licensee may not reverse engineer, modify, or create derivative works based upon the Licensed Materials or any part thereof, except as is specifically permitted in the Brand Identity Guidelines.

The following notice (or such other notice as shall have Licensor's prior written approval) shall appear in connection with the Licensed Materials at least once on all documentation: "Used pursuant to license from Charles & Colvard, Ltd." License shall also use "© (year of first publication) Charles & Colvard, Ltd All Rights Reserved" in connection with copyright works and ™ or ®, as appropriate, in connection with trademarks.

From time to time, Licensor may add other articles, trademarks, or copyright works for electronic download, and the parties agree that by such action this agreement shall be amended to include such additions. Furthermore, upon notice from Licensor posted electronically that it has changed the appearance of the Licensed Materials (or any of the trademarks and/or copyright works therein), Licensee shall use only the changed version in any and all materials produced by Licensee within four (4) weeks following Licensor's initial notice.

8. **COOPERATION WITH LICENSOR**

If Licensee learns of any infringement of the Trademarks, Copyright Works or Copyright Materials or of the existence, use or promotion of any mark or design similar to the Trademarks, Copyright Works or Copyright Materials, Licensee shall promptly notify Licensor. Licensor will, in its discretion, decide whether to object to such existence, use or promotion. Licensee agrees to cooperate fully with Licensor in the prosecution of any trademark or copyright application that Licensor may desire to file or in the conduct of any litigation relating to the Trademarks, Copyright Works or Copyright Materials, as may reasonably be required by Licensor.

9. **EXTENT AND AMENDMENT OF THE LICENSE**

From time to time, Licensor may add other articles, trademarks, or copyright works to Exhibits 1, 2 or 3, and the parties agree that by such action this Agreement shall be amended to include such additions. Furthermore, upon notice from Licensor that it has changed the appearance of any of the Trademarks or Copyright Works, Licensee shall incorporate the new version of the changed Trademark or Copyright Work into all Advertisements bearing the changed Trademark or Copyright Work within four (4) weeks following Licensor's initial notice.

10. **COMPLIANCE WITH GOVERNMENT STANDARDS**

Licensee represents and warrants that the Advertisements shall comply with, meet and/or exceed all Federal, State or Provincial, and local laws, ordinances, standards, regulations and guidelines, including, but not limited to, those pertaining to product, quality, labeling and propriety. Licensee agrees that it will not publish material in its Advertisements or cause or permit any material to be published, in violation of any such Federal, State or Provincial, or local law, ordinance, standard, regulation or guideline.

11. **POST-TERMINATION AND-EXPIRATION RIGHTS AND OBLIGATIONS**

(a) At the expiration or termination of this Agreement, all rights granted to Licensee under this Agreement shall forthwith revert to Licensor, and Licensee shall refrain from further use of the Copyright Works, Copyright Materials and/or the Trademarks, either directly or indirectly, or from use of any marks or designs similar to the Copyright Works, Copyright Materials or the Trademarks. Licensee will immediately cease all use of Advertisements bearing or including the Trademarks, Copyright Works and/or Copyright Materials. Licensee also shall turn over to Licensor all photographs, codes and other materials, which reproduce the Copyright Works, Copyright Materials or the Trademarks or shall provide evidence satisfactory to Licensor of their destruction. Licensee shall be responsible to Licensor for any damages caused by the unauthorized use by Licensee or by others of such photographs, codes and other materials, which are not turned over to Licensor.

(b) Licensee acknowledges that any breach or threatened breach of any of Licensee's covenants in this Agreement relating to the Trademarks, Copyright Works and/or Copyright Materials, including without limitation, Licensee's failure to remove such materials

from its Advertisements at the termination or expiration of this Agreement will result in immediate and irreparable damage to Licensor and to the rights of any subsequent license of Licensor. Licensee acknowledges and admits that there is no adequate remedy at law for any such breach or threatened breach, and Licensee agrees that in the event of any such breach or threatened breach, Licensor shall be entitled to injunctive relief and such other relief as any court with jurisdiction may deem just and proper, without the necessity of Licensor posting any bond.

12. **ASSIGNMENT AND SUBLICENSE**

(a) Licensee shall not assign or transfer any of its rights under this Agreement or delegate any of its obligations under this Agreement (whether voluntarily, by operation of law, change in control or otherwise) without Licensor's prior approval. Any attempted assignment, transfer, or delegation by Licensee without such approval shall be void and a material breach of this Agreement. A change in the majority ownership or a material change in the management of Licensee shall constitute an assignment of rights under this Section requiring Licensor's prior approval.

(b) Licensee may sublicense its rights hereunder to authorized jewelry distributors or retailers engaged in the sale of Licensee's products which incorporate Charles & Colvard created Moissanite jewels; provided Licensee shall first notify, in writing, Licensor of any such authorized jewelry distributor or retailer to be sublicensed hereunder and each of which must agree to be bound by the terms of this Agreement. Each such sublicense shall be deemed automatically approved by Licensor. Any other proposed sublicense shall require Licensor's prior written approval. Licensee shall use all commercially reasonable efforts to insure the use of the rights granted by the sublicense are used in conformity with the terms of this Agreement, including but not limited to notification by Licensee to Licensor of any misuse of the rights and full cooperation with Licensor in asserting Licensor's rights to the full extent of the law.

13. **INDEPENDENT CONTRACTOR**

Licensee is an independent contractor and not an agent, partner, joint venture, affiliate or employee of Licensor. No fiduciary relationship exists between the parties. Neither party shall be liable for any debts, accounts, obligations or other liabilities of the other party, its agents or employees, Licensee shall have no authority to obligate or bind Licensor in any manner. Licensor has no proprietary interest in Licensee and has no interest in the business of Licensee, except to the extent expressly set forth in this Agreement.

14. **SEVERABILITY**

If any provision of this Agreement shall be determined to be illegal and unenforceable by any court of law or any competent government or other authority, the remaining provisions shall be severable and enforceable in accordance with their terms so long as this Agreement without such terms or provisions does not fail of its essential purpose or purposes. The parties will negotiate in good faith to replace any such illegal or unenforceable provision or provisions with suitable substitute provisions which will maintain the economic purposes and intentions of this Agreement.

15. **SURVIVAL**

Licensee's obligations and agreements under Sections 5, 6, 9 and 10 shall survive the termination or expiration of this Agreement.

16. **MISCELLANEOUS**

(a) Captions. The captions for each Section have been inserted for the sake of convenience and shall not be deemed to be binding upon the parties for the purpose of interpretation of this Agreement.

(b) Scope and Amendment of Agreement. This Agreement constitutes the entire agreement between the parties with respect to the use of Licensor's Trademarks, Copyright Works and Copyright Materials and supersedes any and all prior and contemporaneous negotiations, understandings or agreements in regard to such subject matter and is intended as a final expression of their Agreement. With the exception of the addition of new Trademarks, Copyright Works, and Copyright Materials as provided for in Section 7, this Agreement may be amended only by written instrument expressly referring to this Agreement, setting forth such amendment and signed by Licensor and Licensee.

(c) Governing Law and Interpretation. This Agreement will be deemed to have been executed in the State of North Carolina, United States of America and will be construed and interpreted according to the laws of that State without regard to its conflicts of law principles or rules. The parties agree that each party and its counsel has reviewed this Agreement and the normal rule of construction that any ambiguities are to be resolved against the drafting party shall not be employed in the interpretation of this Agreement.

(d) Attorneys' Fees. If Licensor brings any legal action or other preceding to interpret or enforce the terms of this Agreement, or if Licensor retains a collection agent to collect any amounts due under this Agreement, then Licensor shall be entitled to recover reasonable attorneys' fees and any other costs incurred, in addition to any other relief to which it is entitled.

(e) Waiver. The failure of Licensor to insist in any one or more instances upon the performance of any term, obligation or condition of this Agreement by Licensee or to exercise any right or privilege herein conferred upon Licensor shall not be construed as thereafter waiving such term, obligation, or condition or relinquishing such right or privilege, and the acknowledged waiver or relinquishment by Licensor of any default or right shall not constitute waiver of any other default or right. No waiver shall be deemed to have been made unless expressed in writing and signed by the Chief Executive Officer.

IN WITNESS WHEREOF, the parties have caused this Agreement to be executed by their authorized representatives on the dates indicated below.

CHARLES & COLVARD, LTD.

By: */s/ Robert S. Thomas* Date: 8/12/04

Robert S. Thomas, President & CEO

LICENSEE: Reeves Park, Inc.

By: */s/ Klaus Jung* Date: 8/12/04

Klaus H. Jung

Exhibit 1 - Trademarks

(Current versions to be used)

Charles & Colvard Created Moissanite® or Moissanite Created By Charles & Colvard®

CHARLES & COLVARD®
Created
MOISSANITE

MOISSANITE
Created By
CHARLES & COLVARD®

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moiss

Exhibit 2 – Copyright Works

The following advertising materials:

- Product Brochure—"Unique Jewel Born from a Star"
- Product Catalog (Starfield Cover) – soon to be retired
- Cut Course Brochure "CUT: Its Relevance and Importance As It Pertains to a Jewel's Optical Physics"
- The Charles & Colvard Business Opportunity Brochure
- Consumer Card—"moissanite…stellar beauty, superior brilliance"
- Consumer Card— "splendor from the heavens…" (soon to be retired)
- Jewelers Bench Guide
- Lucite Logo Blocks
- Starfield Pocket Folders
- Professional Jeweler Article Reprints
- 11x17 Counter Card (shapes and sizes)
- Now Available on Earth Poster
- Shapes and Sizes Poster
- J-Fire Unit and photography of
- Current Consumer Ad
- Current Trade Ad
- Newspaper Ad Slicks
- Educational Video VHS
- Educational Video Betas
- :30 Commercial on Beta
- International Educational Videos (Spanish, French, Italian and German subtitled)
- CD of marketing materials
- CD of educational video and commercial
- DAT tape of radio commercial

All documents received from Charles & Colvard bearing the Copyright©, Trademark™ or Registered® symbol(s). As revised on July 25, 2003

As revised on July 25, 2003

Exhibit 3 – Brand Identity Guidelines

Welcome

The purpose of the Brand Identity Guidelines is to provide standards that will ensure consistency in the application of the Charles & Colvard created Moissanite brand message. The guidelines set very specific regulations for the use of brand name, logo, registration and identifiers. While Charles & Colvard, Ltd. has approval rights on all uses of its trademarks, it is mandatory that all distributors, manufacturers, designers and jewelers have permission from Charles & Colvard to use the trademark and that use of the Charles & Colvard trademark be consistent with the brand-building program. The environment surrounding the Charles & Colvard created Moissanite logo is a critical component in the overall image of the brand. We have developed standards, which will enable you to project the brand's personality with maximum impact.

Background

Business Strategy

The Charles & Colvard business strategy is to introduce a new category of jewels – the 5th jewel – and build a "new world" brand in a tradition-bound industry. Charles & Colvard will create the first brand to resonate with a rapidly growing group of women who will buy this branded jewel for themselves as a form of self-expression. The Charles & Colvard brand will be for women, about women, and bought by women. The branding strategy dictates a distinctive look and feel, pushing pre-existing boundaries and capitalizing on the impact of a unique approach to building a brand in the jewelry industry.

Brand Strategy/Target Consumer

The Charles & Colvard brand will capitalize on the needs of the members of the target group to: express pride in her achievements, be recognized as an individual of significance, and as a member of an elite, international community of women who have made their mark in the world. The target consumer encompasses a growing community of women achievers whose ambition and ability establishes her as a significant member in her chosen field of endeavor, whether that field is business, the arts, motherhood or medicine. Her mindset is global; her reach may be national or international.

Global Perspective

As a market-driving enterprise, Charles & Colvard will shape and set the brand strategy. It will be global in form and spirit, but executed in a country-by-country basis with flexibility for cultural nuances to be taken into account, yet recognizing our target woman is not average; she is the exception. She is a leader. Advertising is an important element of the brand-building program. It must be as distinctive as the jewel. It cannot have the wallpaper look of much of current jewelry advertising. Charles & Colvard created Moissanite advertising must engage, educate and evoke a sense of discovery. It must provoke the response: "That's for me."

For additional information please contact:

Charles & Colvard, Ltd.
Director of Marketing
3800 Gateway Blvd., Suite 310
Morrisville, NC 27560

(919) 468-0399
(919) 468-0486
www.moissanite.com

ID Guidelines

In order to ensure that our logo and other trademarked materials are presented to consumers in the proper method, and in line with Federal Trade Commission (FTC) guidelines, the following is required in all advertising and collateral communications for Charles & Colvard created Moissanite.

- “Moissanite Created by” must precede the words Charles & Colvard in the first reference; the word “moissanite” may be used alone in subsequent references.
- The proper descriptor for Charles & Colvard created Moissanite is “jewel”. Terms such as “gem”, “gemstone”, and “stone” should be avoided, as their use is subject to FTC and industry regulation to prevent consumer confusion. If the descriptor “jewel” is not easily translated in certain countries, Charles & Colvard must give approval on the usage of alternative descriptors.

Trademark Guidelines

Protecting the Charles & Colvard trademark is mandatory. The following guidelines must be adhered to in all communications:

- The Charles & Colvard trademark and logo distinguish our products from those of other companies. Therefore, any use of the Charles & Colvard trademark and logo must be pre-approved and it must be consistent with the brand-building program. For international distributors, the trademark must be used at least once per year. Proof of trademark use must be provided annually to Charles & Colvard by submitting a copy of all materials containing the logo.
- Use the Charles & Colvard trademark and logo exactly as they appear in Schedule 13 (a) Exhibit 1 attached to this Agreement.
- Use the Charles & Colvard trademark and logo only on, or to market, Charles & Colvard created Moissanite products.
- Use the appropriate symbol “TM” to show that Charles & Colvard is a licensed trademark in the country where the goods are sold. The appropriate trademark notice should appear at least once in each piece of printed matter, preferably the first time the trademark appears.
- Charles & Colvard, Ltd. has approval rights on all uses of the Charles & Colvard logo and trademark.

Helpful Hints

We highly recommend that all distributors, manufacturers, designers and jewelers use the advertising and marketing materials developed by Charles & Colvard. These materials reflect our global marketing plan which is inspiring many consumers to purchase Charles & Colvard created Moissanite. However, should you choose to develop your own creative ads, you must seek permission from the Charles & Colvard marketing department to use the Charles & Colvard trademark and/or logo. Please remember that when you are creating your own advertisements, Charles & Colvard MUST pre-approve all materials containing the Charles & Colvard trademark and logo.

In protection of the Charles & Colvard brand position, the following are a few points to keep in mind when developing your advertising:

- No diamond comparisons should be made in any creative copy.
- No discounted pricing information should appear in any creative copy.
- Charles & Colvard-supplied advertising is not to be altered in any way.

EXHIBIT 10.65
EXECUTION COPY

SECURITY AGREEMENT

THIS SECURITY AGREEMENT (this "Agreement"), dated effective as of August 15, 2004, between REEVES PARK, INC., a Minnesota corporation whose mailing address is 5050 Lincoln Drive, Suite 470, Edina, MN 55436, Attention: Klaus Jung (hereinafter referred to as "Debtor") and CHARLES & COLVARD, LTD, a North Carolina corporation whose mailing address is 300 Perimeter Park Drive, Suite A, Morrisville, NC 27560 (hereinafter referred to as "Secured Party").

R E C I T A L S:

A. Debtor has entered into that certain Moissanite Consignment Agreement (as defined below).

B. The execution and delivery of this Agreement is required by the Moissanite Consignment Agreement as a condition to making extensions of credit thereunder.

NOW THEREFORE, in consideration of the premises and for other good and valuable consideration, the adequacy, receipt, and sufficiency of which are hereby acknowledged, and in order to induce Secured Party to enter the Transaction pursuant to the Moissanite Consignment Agreement, the parties hereto hereby agree as follows:

ARTICLE I
DEFINITIONS

Section 1.1. Definitions. As used in this Agreement, the following terms have the following meanings:

"Account" means any "account," as such term is defined in Article 9 of the UCC, now owned or hereafter acquired by Debtor

"Collateral" has the meaning specified in Section 2.1 of this Agreement.

"Event of Default" means the occurrence of any of the following: (i) any failure by Debtor to pay any amount due to Secured Party when and as due under the Moissanite Consignment Agreement, any other Transaction Document or in connection with the Transaction, (ii) Debtor shall default in the due observance or performance of any other covenant, condition or agreement set forth in this Agreement, the Moissanite Consignment Agreement, any other Transaction Document; (iii) entry of any single judgment against Debtor in excess of $100,000, or entry of judgments against Debtor that in the aggregate exceed $100,000 and that are not bonded over or discharged within 30 days; (iv) Debtor shall become insolvent or shall be adjudicated bankrupt; bankruptcy, insolvency, reorganization, arrangement, debt

adjustment, liquidation, or receivership proceedings in which Debtor is alleged to be insolvent or unable to pay its debts as they mature, are instituted by or against Debtor, and Debtor shall consent to the same or shall admit in writing the material allegations of the petition filed in such proceedings, or the proceedings are not dismissed within the time permitted for the posting of bond and no bond shall have been posted in the matter (v) any material statement, representation or warranty of Debtor herein is untrue in any material respect; or (vi) Debtor shall default under its fine jewelry consignment agreement with J.C. Penny Corporation dated July 20, 2004.

"General Intangibles" means any "general intangibles," as such term is defined in Article 9 of the UCC, now owned or hereafter acquired by Debtor.

"Lien" means any lien, mortgage, security interest, tax lien, financing statement, pledge, charge, hypothecation or other encumbrance of any kind or nature whatsoever (including, without limitation, any conditional sale or title retention agreement), whether arising by contract, operation of law or otherwise.

"Moissanite Consignment Agreement" means that certain agreement dated effective as of August 15, 2004 by and between Secured Party as "Consignor" and Debtor as "Consignee" pursuant to which Secured Party has and will consign and deliver Charles & Colvard created Moisssanite jewels to Debtor, as such agreement may be amended, restated, restated or otherwise modified from time to time.

"Obligations" shall mean and include (a) the due and punctual payment by the Debtor of: (i) all amounts payable to Secured Party pursuant to the Moissanite Consignment Agreement or otherwise payable to Secured Party in connection with the Transaction, when and as due, whether at maturity, by acceleration, upon one or more dates set for prepayment or otherwise and any renewals, modifications or extensions thereof, in whole or in part and (ii) all other monetary obligations, including fees, costs, expenses and indemnities, whether primary, secondary, direct, contingent, fixed or otherwise (including monetary obligations incurred during the pendency of any bankruptcy, insolvency, receivership or other similar proceeding, regardless of whether allowed or allowable in such proceeding) of the Debtor to the Secured Party under the Transaction Documents, (b) the due and punctual payment and performance of all other obligations of the Debtor under or pursuant to the Moissanite Consignment Agreement and the other Transaction Documents, and any renewals, modifications or extensions thereof, in whole or in part; (c) the payment and performance by Debtor of all obligations, agreements, covenants, representations and warranties in this Agreement, the Moissanite Consignment Agreement, the Transaction Documents and any other document executed and delivered in connection therewith (the liabilities, obligations and indebtedness described in clauses (a) through (c), inclusive, of this paragraph are herein collectively referred to as the "Obligations").

"Payment Intangibles" means "payment intangibles" as such term is defined in Article 9 of the UCC, now owned or hereafter acquired by Debtor.

"Proceeds" means any "proceeds," as such term is defined in Article 9 of the UCC.

"Security Agreement" means this Security Agreement dated as of August 15, 2004 by and between Secured Party and Debtor.

"Transaction" means the consignment transactions between Secured Party and Debtor pursuant to and as described in and contemplated by the Moissanite Consignment Agreement.

"Transaction Documents" means and refers collectively to the Moissanite Consignment Agreement, this Security Agreement and all other documents now or hereafter evidencing or securing the Transaction, and any renewals, modifications or extensions thereof, in whole or in part;

"UCC" means the Uniform Commercial Code as in effect in the State of North Carolina and/or any other jurisdiction the laws of which may be applicable to or in connection with the creation, perfection or priority of any Lien on any Collateral.

Terms used herein, which are defined in the UCC, shall have the meanings determined in accordance with the UCC.

ARTICLE II
SECURITY INTEREST

Section 2.1. Security Interest. As Collateral security for the prompt payment and performance in full when due of the Obligations, Debtor hereby pledges and assigns to Secured Party, and grants to Secured Party a continuing lien on and security interest in, all of Debtor's right, title, and interest in and to the following, whether now owned or hereafter arising or acquired and wherever located (collectively, the "Collateral"):

(a) all Accounts of Debtor from J.C Penney Corporation ("JC Penney") at any time owing to Debtor;

(b) all General Intangibles paid or payable by JC Penney to Debtor;

(c) all Payment Intangibles paid or payable by JC Penney to Debtor;

(d) all products and Proceeds, in cash or otherwise, of any of the property described in the foregoing clauses (a) through (c);

ARTICLE III
REPRESENTATIONS AND WARRANTIES

To induce Secured Party to enter into this Agreement and the Moissanite Consignment Agreement, Debtor represents and warrants as follows:

Section 3.1. Office and Tax Identification Number. On the date hereof, the principal place of business, mailing address and the chief executive office of Debtor is identified in the first paragraph of this Agreement Debtor's United States Federal Income Tax Identification Number is set forth on the signature page hereof.

Section 3.2. Ownership; No Encumbrances**.** Except for the security interest (and pledges and assignments as applicable) granted hereby, and subject to the terms of any Intercreditor Agreement entered into by Secured Party with SPECTRUM Commercial Services

Company, the Debtor is, and as to any property acquired after the date hereof which is included within the Collateral, Debtor will be, the owner of all such Collateral free and clear from all charges, Liens, security interests, adverse claims and encumbrances of any and every nature whatsoever.

ARTICLE IV
COVENANTS

Debtor covenants and agrees that, as long as the Obligations or any part thereof are outstanding or any amount payable under the Transaction remains unpaid under the Moissanite Consignment Agreement, Debtor will perform and observe each of the following covenants:

Section 4.1. Accounts. Debtor shall, in accordance with its customary business practices, endeavor to collect or cause to be collected from JC Penney as Account Debtor under its Accounts, as and when due, any and all amounts owing under such Accounts. Without the prior written consent of Secured Party, Debtor shall not, except in the ordinary course of business, and in no event when any Event of Default exists, (a) grant any extension of time for any payment with respect to any of the Accounts beyond sixty (60) days after such payment's due date, (b) compromise, compound, or settle any of the Accounts for less than the full amount thereof, (c) release, in whole or in part, any Person liable for payment of any of the Accounts, (d) allow any credit or discount for payment with respect to any Account other than trade or other customary discounts granted in the ordinary course of business, or (e) release any Lien or guaranty securing any Account unless the Account has been paid.

Section 4.2. Corporate Changes. Debtor shall not change its name, identity, corporate structure, or its United States Tax Identification Number in any manner that might make any financing statement filed in connection with this Agreement seriously misleading unless Debtor shall have given Secured Party not less than thirty (30) days prior written notice thereof and shall have taken all action reasonably deemed necessary or desirable by Secured Party to protect its liens with the perfection and priority thereof required by the Transaction Documents.

ARTICLE V
RIGHTS OF SECURED PARTY

Section 5.1. Power of Attorney. To the extent permitted by applicable law, Debtor hereby irrevocably constitutes and appoints Secured Party, with full power of substitution, as its true and lawful attorney-in-fact with full irrevocable power and authority in the name of Debtor or in its own name, to take, after the occurrence and during the continuance of an Event of Default, any and all actions and to execute any and all documents and instruments which Secured Party at any time and from time to time deems necessary to accomplish the purposes of this agreement and, without limiting the generality of the foregoing, such Debtor hereby gives Secured Party the power and right on behalf of Debtor and in its own name to do any of the following after the occurrence and during the continuance of an Event of Default, without notice to, or the consent of, Debtor:

(a) to demand, sue for, collect, or receive, in the name of Debtor or in Secured Party's own name, any money or property at any time payable or receivable on account of

or in exchange for any of the Collateral and, in connection therewith, endorse checks, notes, drafts, acceptances, money orders, documents of title, or any other instruments for the payment of money under the Collateral or any policy of insurance;

(b) (i) to direct Account Debtors and any other parties liable for any payment under any of the Collateral to make payment of any and all monies due and to become due thereunder directly to Secured Party or as Secured Party shall direct (Debtor agrees that if any Proceeds of any Collateral (including payments made in respect of Accounts) shall be received by Debtor while an Event of Default exists, Debtor shall promptly deliver such Proceeds to Secured Party with any necessary endorsements, and until such Proceeds are delivered to Secured Party, such Proceeds shall be held in trust by Debtor for the benefit of Secured Party and shall not be commingled with any other funds or property of Debtor); (ii) to receive payment of and receipt for any and all monies, claims and other amounts due and to become due at any time in respect of or arising out of any Collateral; (iii) to commence and prosecute any suit, action, or proceeding at law or in equity in any court of competent jurisdiction to collect the Collateral or any part thereof and to enforce any other right in respect of any Collateral; (iv) to defend any suit, action, or proceeding brought against Debtor with respect to any Collateral; (v) to settle, compromise, or adjust any suit, action, or proceeding described above and, in connection therewith, to give such discharges or releases as Secured Party may deem appropriate; insurance); and (vi) to sell, transfer, pledge, convey, make any agreement with respect to, or otherwise deal with any of the Collateral as fully and completely as though Secured Party were the absolute owner thereof for all purposes, and to do, at Secured Party's option and Debtor's expense, at any time, or from time to time, all acts and things which Secured Party deems necessary to protect, preserve, maintain, or realize upon the Collateral and Secured Party's security interest therein.

THIS POWER OF ATTORNEY IS A POWER COUPLED WITH AN INTEREST AND SHALL BE IRREVOCABLE UNTIL TERMINATION OF THIS AGREEMENT IN ACCORDANCE HEREOF.

ARTICLE VI
DEFAULT

Section 6.1. Rights and Remedies. If an Event of Default shall have occurred and be continuing, Secured Party shall have the following rights and remedies:

(a) In addition to all other rights and remedies granted to Secured Party in this Agreement or in any other Transaction Document or by applicable law, Secured Party shall have all of the rights and remedies of a Secured Party under the UCC (whether or not the UCC applies to the affected Collateral). Debtor shall be liable for all reasonable expenses of retaking, holding, preparing for sale, or the like, and all reasonable attorneys' fees, legal expenses, and other costs and expenses incurred by Secured Party in connection with the collection of the Obligations and the enforcement of Secured Party's rights under this Agreement. Debtor shall remain liable for any deficiency if the Proceeds of any sale or other disposition of the Collateral applied to the Obligations are insufficient to pay the Obligations in full. Debtor waives all rights of marshaling, valuation, and appraisal in respect of the Collateral.

(b) Secured Party may cause any or all of the Collateral held by it to be transferred into the name of Secured Party or the name or names of Secured Party's nominee or nominees.

(c) Secured Party may exercise any and all rights and remedies of Debtor under or in respect of the Collateral, including, without limitation, any and all rights of Debtor to demand or otherwise require payment of any amount under, or performance of any provision of, any of the Collateral.

ARTICLE VII
MISCELLANEOUS

Section 7.1. No Waiver; Cumulative Remedies. No failure on the part of Secured Party to exercise and no delay in exercising, and no course of dealing with respect to, any right, power, or privilege under this Agreement shall operate as a waiver thereof, nor shall any single or partial exercise of any right, power, or privilege under this Agreement preclude any other or further exercise thereof or the exercise of any other right, power, or privilege. The rights and remedies provided for in this Agreement are cumulative and not exclusive of any rights and remedies provided by law.

Section 7.2. Successors and Assigns. This Agreement shall be binding upon and inure to the benefit of Debtor and Secured Party and their respective successors and assigns, except that Debtor may not assign any of its rights or obligations under this Agreement without the prior written consent of Secured Party.

Section 7.3. Amendment. The provisions of this agreement may be amended or waived only by an instrument in writing signed by the parties hereto.

Section 7.4. Notices. All notices and other communications provided for in this Agreement shall be given or made by telefax, overnight courier service, personal delivery or U.S. Mail at the addresses shown for each party in the first paragraph of this Agreement .

Section 7.5. Governing Law. This Agreement shall be governed by, and construed in accordance with, the laws of the State of North Carolina

Section 7.6. Survival of Representations and Warranties. All representations and warranties made in this Agreement or in any certificate delivered pursuant hereto shall survive the execution and delivery of this Agreement

Section 7.7. Severability. Any provision of this Agreement which is determined by a court of competent jurisdiction to be prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions of this Agreement, and any such prohibition or unenforceability in any jurisdiction shall not invalidate or render unenforceable such provision in any other jurisdiction.

Section 7.8. Termination. If all of the Obligations shall have been paid and performed in full, Secured Party shall, upon the written request of Debtor, execute and deliver to the Debtor a proper instrument or instruments acknowledging the release and termination of the security interests created by this Agreement Notwithstanding anything to the contrary contained in this Agreement, if the payment of any amount of the Obligations is rescinded, voided or must otherwise be refunded by Secured Party upon the insolvency, bankruptcy or reorganization of the Debtor or otherwise for any reason whatsoever, then the security interests created by this Agreement will be automatically reinstated and become automatically effective and in full force and effect, all to the extent that and as though such payment so rescinded, voided or otherwise refunded had never been made and such release and termination of such security interest had never been given.

Section 7.9. Counterparts. This Agreement may be executed in counterparts (and by different parties hereto in different counterparts), each of which shall constitute an original, but all of which when taken together shall constitute a single contract. Delivery of an executed counterpart of a signature page of this Agreement by telecopy shall be effective as delivery of a manually executed counterpart of this Agreement.

IN WITNESS WHEREOF, the parties hereto have duly executed this Agreement as of the day and year first written above.

DEBTOR:

REEVES PARK, INC.

By: */s/ Klaus Jung*

Name: Klaus Jung
Title: President

Debtor's Federal Income Tax Identification Number:

_____

SECURED PARTY:

CHARLES & COLVARD, LTD

By: */s/ James R. Braun*

Name: James R. Braun
Title: Vice President Finance & CFO

REDACTED – OMITTED MATERIAL HAS BEEN FILED SEPARATELY WITH THE COMMISSION AND IS DENOTED HEREIN BY XXXXX.

August 16, 2004

Reeves Park, Inc.
5050 Lincoln Drive, Suite 470
Edina, MN 55436
Attention: Klaus Jung

Re: Charles & Colvard Created Moissanite Jewel Consignment Agreement

Dear Klaus:

This letter sets forth the terms of the agreement ("Agreement") made effective as of August 15, 2004 ("Effective Date") by and between Charles & Colvard, Ltd. ("Consignor") a North Carolina corporation, and Reeves Park, Inc. ("Reeves Park"), a Minnesota corporation, pursuant to which Consignor will consign and deliver Charles & Colvard created moisssanite Jewels (the "Jewels") to Reeves Park.

1. Consigned Merchandise. This Agreement pertains to any and all Jewels that Consignor consigns or delivers on consignment to or for the account of Reeves Park during the term of this Agreement. It is understood by the parties that Reeves Park shall incorporate all Jewels into fine jewelry items it shall consign to J.C. Penney Corporation, Inc. ("JCPenney") for the purpose of introducing moissanite into approximately 450 JCPenney retail locations.

The assortment of the Jewels being consigned and delivered to Reeves Park by Consignor will, subject to availability, be initially as set forth on Exhibit A, and subsequently such Exhibit A may be amended by a revised Exhibit A signed by both parties. Any such amended Exhibit A shall be incorporated and made a part of this Agreement.

2. Title; Security Interest.

a. This Agreement is intended to be a true consignment of the Jewels. Therefore Consignor will retain title to the Jewels until sold to customers of JCPenney. The preceding sentence shall not be deemed to waive Consignor's right to receive payments as set forth in this Agreement.

b. If, however, it is determined that the consignment created by this Agreement is one intended as security, or the consignment is a sale or return transaction, or other sale, this Agreement will constitute a security agreement pursuant to which Reeves Park grants Consignor a purchase money security interest in the Jewels. Reeves Park hereby authorizes Consignor to file UCC-1 financing statements with respect to its security interest in the Jewels. In any UCC filings made by Consignor with respect to the Jewels, Consignor agrees to describe the collateral as follows:

"All Charles & Colvard created moissanite Jewels that are now or may at any time hereafter be delivered on consignment or consigned by secured party to debtor. Future consignments and deliveries are covered.

Upon Reeves Park's satisfaction of its obligations to Consignor under this Agreement, including the payment of all amounts due Consignor and the return of all unsold Jewels, Consignor will make all appropriate filings necessary to terminate the UCC-1 filings and any other UCC filings made by Consignor with respect to the Jewels. Consignor further agrees to provide Reeves Park with "as filed" copies of all UCC filings made by it regarding the Jewels.

Within 15 days after each shipment of fine jewelry by Reeves Park to JCPenney, Reeves Park shall present evidence to Consignor of an enforceable security agreement for merchandise sent to JCPenney, as well as providing proof of insurance by either JCPenney or Reeves Park. Copies of the UCC filings will be made available to Consignor on a timely basis. Reeves Park covenants and agrees that it shall retain a perfected first priority purchase money security interest in all merchandise delivered to JCPenney and shall cause UCC Financing Statements to be timely filed in all appropriate jurisdictions with respect to such merchandise as purchase money transactions in inventory under Section 9-103 and other applicable sections of the Uniform Commercial Code so as to maintain a first priority perfected security interest in all merchandise delivered to JCPenney. Reeves Park shall also execute and deliver prior to the delivery of any merchandise to JCPenney, a collateral assignment and security agreement in form and substance satisfactory to Consignor and its counsel granting to Consignor as security for performance of all of Reeves Park's obligations to Consignor a first priority security interest in (i) the Fine Jewelry Consignment Agreement between Reeves Park and JCPenney and (ii) any and all security agreements executed by JCPenney to or for the benefit of Reeves Park in connection with the merchandise delivered to JCPenney together with all of Reeves Park rights in and to the collateral secured thereby, and proceeds thereof and all of its rights as secured party thereunder.

Reeves Park is responsible for tracking the specific locations of the Jewels and Consignor shall, upon reasonable notice, have the right to physically inspect the Jewels at all such locations.

3. Delivery. Delivery of the Jewels shall be on the terms set out in the Manufacturer's Agreement between the parties (the "Manufacturer's Agreement"). Freight charges shall be calculated and charged as set out in the Manufacturer's Agreement.

4. Invoices; Payment Terms; Replenishment; Reconciliation.

a. For each shipment of Jewels, Consignor will send Reeves Park a memo invoice for such Jewels at Consignor's prices as provided in the Manufacturer's Agreement.

b. Consignor will be paid for the Jewels upon the sale of the fine jewelry. JCPenney will furnish Reeves Park with a biweekly sales report, which will report the fine jewelry (and thus Jewels) sold in the previous two JCPenney fiscal weeks. Reeves Park shall immediately upon receipt furnish such biweekly sales report to Consignor, accompanied by a list of Jewels incorporated in such fine jewelry. Reeves Park shall grant Consignor full access to the JCPenney vendor system to monitor and verify the sales activity at JCPenney. Consignor shall invoice Reeves Park for all such Jewels sold on net 30 day terms upon receipt of the biweekly sales report, and Consignor, at its discretion, shall have the right to invoice Reeves Park for all sales activity reported on the JCPenney vendor system prior to the end of each calendar quarter.

c. Subject to the terms of this Agreement, the availability of the Jewels, and unless directed otherwise by JCPenney, Consignor shall provide Reeves Park with full replenishment of all Jewels in the fine jewelry upon receipt of information from JCPenney or Reeves Park that such fine jewelry has been sold by JCPenney. Such Jewels shall be shipped subject to the terms of this Agreement.

d. Upon Consignor's reasonable request, Reeves Park will furnish a report indicating the number, size and style of Jewels held by JCPenney on consignment from Reeves Park according to its accounting records. At least once per year, when JCPenney physically inventories the fine jewelry on consignment from Reeves Park and pays Reeves Park for any fine jewelry that is determined to have been lost, stolen, damaged or unaccounted for while in JCPenney's possession, Reeves Park shall immediately provide Consignor with a listing of such fine jewelry and shall pay Consignor for all Jewels used in such fine jewelry. In the event, JCPenney elects to undertake such physical inventory on a rolling basis over a period of months, payment by Reeves Park to Consignor shall be adjusted to reflect the actual schedule of payments received by Reeves Park. For the avoidance of doubt, Reeves Park will not be obligated to pay for any Jewels that were omitted from packing, or defective or damaged at the time of delivery to Reeves Park; provided, in the case of defective or damaged items, the same are promptly returned to Consignor.

e. A final full reconciliation will be made within 60 days of the date that (i) all unsold Jewels are returned to Consignor, or (ii) all Jewels have been sold and no further consignments are contemplated.

5. Risk of Loss. Even though Consignor retains title to the Jewels, Reeves Park will bear the risk of loss with respect to the Jewels while in Reeves Park's possession. For the avoidance of doubt, the preceding sentence does not apply to any Jewels that were omitted from packing, or defective or damaged at the time of delivery to Reeves Park.

6. Return of Jewels to Consignor. Reeves Park shall have the right to return some or all of the Jewels to Consignor upon prior notice to Consignor. If Reeves Park exercises this right, Reeves Park shall return the designated Jewels not later than 60 days from the date such notice is given by it. All Jewels shall be returned as loose jewels and not in fine jewelry.

Reeves Park shall bear any and all costs associated with its return of the Jewels to Consignor's facility pursuant to this section. The risk of loss with respect to the Jewels returned to Consignor pursuant to this section shall be on Reeves Park until delivery to Consignor's facility, at which time risk of loss shall pass to Consignor.

7. Events of Default. The following shall constitute an "Event of Default" under this Agreement: (a) Reeves Park's failure to pay any and all payments required to be made by it under this Agreement; (b) either party breaches a representation, warranty, guaranty or other obligation of it under this Agreement; or (c) either party becomes insolvent or subject to any bankruptcy, insolvency, or receivership proceeding. Upon the occurrence of an Event of Default, the non-defaulting party shall notify the defaulting party, and the defaulting party shall have a period of 15 days from receipt of notice to cure the Event of Default. If the Event of Default is not cured within the 15-day period, the non-defaulting party may terminate Agreement immediately upon notice to the defaulting party.

8. Term; Termination. The term of this Agreement will commence on the Effective Date and continue until January 31, 2005. Termination shall not relieve Reeves Park of any liability to Consignor for payment for any Jewels not returned to Consignor. Upon termination, Reeves Park shall return all unsold Jewels to Consignor's facility as loose Jewels, promptly following, but in no event later than 60 days from the effective date of, such termination. The provisions of section 6 of this Agreement will apply to such return.

9. Property Taxes. Reeves Park will pay any taxes, levies and/or assessments that may be owed or imposed by virtue of Reeves Park's possession of the Jewels in its facilities, or its customers.

10. Consignor's Standard Terms and Conditions. Except to the extent expressly modified by or inconsistent with this Agreement, or inconsistent with the consignment nature of the contemplated transactions, Consignor's standard terms and conditions as set out in its Manufacturing Agreement with Reeves Park will apply to the consignment transactions and the Jewels.

11. Notice. Any notice given by either party pursuant to this Agreement shall be given in writing and be deemed to have been received by the other party upon the sending thereof by receipted courier, express mail, registered or certified mail, or facsimile transmission, addressed to such party at the address or facsimile number, designated by that party. A notice given by facsimile transmission shall not be effective until the original of such notice is also sent by receipted courier, express mail, or registered or certified mail.

12. Governing Law. THIS AGREEMENT SHALL BE GOVERNED AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NORTH CAROLINA WITHOUT GIVING EFFECT TO PRINCIPLES OF CONFLICTS OF LAW THEREOF. THE PARTIES HEREBY SUBMIT TO EXCLUSIVE JURISDICTION AND VENUE IN THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF NORTH CAROLINA IN RALEIGH, NORTH CAROLINA.

13. General.

a. This Agreement may not be modified except in writing signed by both parties.

b. This Agreement shall be binding upon and inure to the benefit of the parties and their respective successors, permitted assigns (with prior written consent), and any subsidiary or affiliated company effectively controlled by any of them.

c. Each party has caused this Agreement to be properly executed on its behalf as of the Effective Date first above written.

We have sent two originals of this Agreement. Please have both signed by an authorized officer where indicated below, and return one to us.

Sincerely,

CHARLES & COLVARD, LTD.

By: */s/ Robert S. Thomas*

Robert S. Thomas, President

ACCEPTED AND AGREED this 16th day
of August, 2004.

REEVES PARK, INC.

By: */s/ Klaus Jung*

Print Name: Klaus Jung

Title: President

EXHIBIT A

SALES ORDER ACKNOWLEDGEMENT

Order No: 29842-0 Date Entered: 8/5/2004

Cust. PO No: Date Sched Ship: 8/5/2004

Sold To: 3268

REEVES PARK INC.
P.O. Box 455
HOPKINS, MN55345-0455

Ship To:

XXXXXXXX
XXXXXXXX
XXXXXXXX
XXXXXXXXXXXXXXXX

Carrier: XXXXXXXXXXXXXXXXXXXXXX

Terms: XXXXXXXXXXXX

FOB: XXXXXXX

Tax: XXXXXXXXXXXXXXXXXXX

Location: XXXXXX

Item No/Description	UOM	Ordered	Unit Price	Amount
XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX	XX	XXXXX	XXXXX	XXXXX
XXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXXX	XX	XXXXX	XXXXX	XXXXX
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Exhibit 10.67

CHARLES & COLVARD®
Created
MOISSANITE

November 8, 2004

Mr. Klaus H. Jung
Reeves Park, Inc.
5050 Lincoln Drive
Suite 470
Edina, MN 55436

Re: Amendment to Manufacturing Agreement

Dear Klaus:

This letter sets forth the agreement of Charles & Colvard, Ltd. ("C&C") and Reeves Park, Inc. ("Buyer") to amend the standard Terms and Conditions as set forth in the Manufacturing Agreement dated August 12, 2004 between C&C and Buyer. Notwithstanding any provision of such Terms and Conditions, by mutual agreement C&C and Buyer may extend various terms to Buyer and payment shall be due in full pursuant to the terms as set out on the applicable C&C invoice to Buyer.

Other than as set out in this amendment, the terms and conditions of the Manufacturing Agreement shall remain in effect. If the foregoing meets with your understanding of our agreement, please sign and return one copy of this letter for our files.

Charles & Colvard, Ltd.

By: */s/ James R. Braun*

Name: James R. Braun

Title: Vice President Finance & CFO

Agreed and Accepted by "Buyer"

By: */s/ Klaus Jung*

Name: Klaus Jung

Title: President

300 Perimeter Park, Suite A Morrisville, NC 27560 Telephone 919.468.0399
Facsimile 919.468.0486 www.moissanite.com

Exhibit 10.68

FIRST AMENDMENT TO SECURITY AGREEMENT

THIS FIRST AMENDMENT (this "Amendment") is made as of this 8th day of November, 2004, to that certain Security Agreement (the "Agreement") by and between REEVES PARK, INC., a Minnesota corporation ("Debtor"), and CHARLES AND COLVARD, LTD, a North Carolina corporation ("Secured Party"), dated effective as of August 15, 2004.

RECITALS:

WHEREAS, Debtor and Secured Party are parties to a Moissanite Consignment Agreement (as defined in the Agreement) and a Manufacturing Agreement, dated as of August 12, 2004 (the "Manufacturing Agreement"); and

WHEREAS, in order to induce the Secured Party to continue making sales to Debtor under the Manufacturing Agreement, the parties desire to amend the Agreement to reflect that the Collateral (as defined in the Agreement) shall also secure Debtor's obligations under the Manufacturing Agreement;

NOW, THEREFORE, in consideration of the premises and for other good and valuable consideration, the adequacy, receipt, and sufficiency of which are hereby acknowledged, and in order to induce Secured Party to continue selling moissanite to Debtor pursuant to the Manufacturing Agreement, the parties hereto agree as follows:

1. Capitalized terms used herein and not otherwise defined shall have the meanings set forth in the Agreement.

2. The following definitions in Section 1.1 of the Agreement are hereby amended as follows:

   (a) The definition of "Event of Default" is hereby amended by amended and restating subsections (i) and (ii) of such definition in their entirety to read as follows:

   "(i) any failure by Debtor to pay any amount due to Secured Party when and as due under the Moissanite Consignment Agreement, the Manufacturing Agreement, any other Transaction Document or in connection with the Transaction; (ii) Debtor shall default in the due observance or performance of any other covenant, condition or agreement set forth in this Agreement, the Moissanite Consignment Agreement, the Manufacturing Agreement or any other Transaction Document;"

   (b) The definition of "Obligations" is hereby amended and restated in its entirety to read as follows:

   ""Obligations" shall mean and include (a) the due and punctual payment by the Debtor of: (i) all amounts payable to Secured Party pursuant to the Moissanite Consignment Agreement, the Manufacturing Agreement or otherwise payable to Secured Party in connection with the Transaction, when and as due, whether at maturity, by acceleration, upon one or more dates set for prepayment or otherwise

and any renewals, modifications or extensions thereof, in whole or in part and (ii) all other monetary obligations, including fees, costs, expenses and indemnities, whether primary, secondary, direct, contingent, fixed or otherwise (including monetary obligations incurred during the pendency of any bankruptcy, insolvency, receivership or other similar proceeding, regardless of whether allowed or allowable in such proceeding) of the Debtor to the Secured Party under the Transaction Documents and/or the Manufacturing Agreement; (b) the due and punctual payment and performance of all other obligations of the Debtor under or pursuant to the Moissanite Consignment Agreement, the other Transaction Documents and the Manufacturing Agreement, and any renewals, modifications or extensions thereof, in whole or in part; and (c) the payment and performance by Debtor of all obligations, agreements, covenants, representations and warranties in this Agreement, the Moissanite Consignment Agreement, the Manufacturing Agreement, the Transaction Documents and any other document executed and delivered in connection therewith (the liabilities, obligations and indebtedness described in clauses (a) through (c), inclusive, of this paragraph are herein collectively referred to as the "Obligations")."

(c) The definition of "Security Agreement" is hereby amended and restated in its entirety to read as follows:

""Security Agreement" means this Security Agreement dated as of August 15, 2004 by and between Secured Party and Debtor, as the same may be hereafter amended."

3. Section 1.1 of the Agreement is hereby amended by adding a new definition into such section (in appropriate alphabetical order), which shall read as follows:

""Manufacturing Agreement" shall mean the Manufacturing Agreement by and between Secured Party and Debtor, dated August 12, 2004, consisting of an executed cover letter between the parties dated August 12, 2004, the Terms and Conditions attached thereto and the License Agreement attached as Exhibit A thereto."

4. Section 2.1 of the Agreement is hereby amended and restated in its entirety to read as follows:

"2.1 Security Interest. In addition to any other security interest granted in any other collateral pursuant to the Moissanite Consignment Agreement or the Manufacturing Agreement, as Collateral security for the prompt payment and performance in full when due of the Obligations, Debtor hereby pledges and assigns to Secured Party, and grants to Secured Party a continuing lien on and security interest in, all of Debtor's right, title, and interest in and to the following, whether now owned or hereafter arising or acquired and wherever located (collectively, the "Collateral"):

(a) any jewelry or settings (including, but not limited to, rings, necklaces, earrings, bracelets, pendants) which include the moissanite jewels shipped or provided to Debtor pursuant to the Moissanite Consignment Agreement;

(b) all Accounts of Debtor from J.C. Penney Corporation ("J.C. Penney") at any time owing to Debtor;

(c) all General Intangibles paid or payable by J.C. Penney to Debtor;

(d) all Payment Intangibles paid or payable by J.C. Penney to Debtor; and

(e) all products and Proceeds, in cash or otherwise, of any of the property described in the foregoing clauses (a) through (d).

5. Section 3.2 of the Agreement is hereby amended and restated in its entirety to read as follows:

Section 3.2 Ownership; No Encumbrances. Except for the security interest (and pledges and assignments as applicable) granted hereby, and subject to the Liens granted by Debtor to Associated Bank Minnesota National Association and to SPECTRUM Commercial Services Company and as to which UCC financings statements have been filed as of the date hereof, the Debtor is, and as to any property acquired after the date hereof which is included within the Collateral, Debtor will be, the owner of all such Collateral free and clear from all charges, Liens, security interests, adverse claims and encumbrances of any and every nature whatsoever.

6. Except as set forth herein the Agreement shall remain in full force and effect.

7. This Amendment may be executed in one or more counterparts each of which shall be deemed an original, but all of which, when taken together, shall constitute one and the same instrument.

IN WITNESS WHEREOF, the parties have executed this Amendment as of the date set forth above.

CHARLES & COLVARD, LTD.

By: */s/ James R. Braun*

Name: James R. Braun
Title: Vice President Finance & CFO

REEVES PARK, INC.

By: */s/ Klaus Jung*

Name: Klaus Jung
Title: President

Exhibit 31.1

I, Robert S. Thomas, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Charles & Colvard, Ltd.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on the registrant's most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 9, 2004

/s/ Robert S. Thomas

Robert S. Thomas
President & Chief Executive Officer

Exhibit 31.2

I, James R. Braun, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Charles & Colvard, Ltd.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (c) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on the registrant's most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

November 9, 2004

/s/ James R. Braun

James R. Braun
Vice President of Finance & Chief Financial Officer

Exhibit 32.1

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Charles & Colvard, Ltd. (the "Company") on Form 10-Q for the period ending September 30, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Robert S. Thomas, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15 (d) of the Securities Exchange Act of 1934; and

(2) The information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Robert S. Thomas

Robert S. Thomas
President and Chief Executive Officer
November 9, 2004

Exhibit 32.2

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 906
OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Charles & Colvard, Ltd. (the "Company") on Form 10-Q for the period ending September 30, 2004 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, James R. Braun, Vice President of Finance and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

(1) The Report fully complies with the requirements of section 13(a) or 15 (d) of the Securities Exchange Act of 1934; and

(2) The information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ James R. Braun

James R. Braun
Vice President of Finance and Chief Financial Officer
November 9, 2004

A signed original of this written statement required by Section 906 has been provided to Charles & Colvard, Ltd. and will be retained by Charles & Colvard, Ltd. and furnished to the Securities and Exchange Commission or its staff upon request.