UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

x Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended March 31, 2010

OR

o Transition report pursuant to Section 13 of 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 (State or other jurisdiction of incorporation or organization)	**56-1928817** (I.R.S. Employer Identification No.)
300 Perimeter Park Drive, Suite A **Morrisville, North Carolina** (Address of principal executive offices)	**27560** (Zip Code)

(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 x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☐ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☐	Accelerated filer	☐
Non-accelerated filer	☐ (Do not check if a smaller reporting company)	Smaller reporting company	x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

As of May 12, 2010, there were approximately 19,091,524 shares of the registrant's common stock, no par value per share, outstanding.

CHARLES & COLVARD, LTD.

FORM 10-Q
For the Quarterly Period Ended March 31, 2010

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

CHARLES & COLVARD, LTD.
CONDENSED CONSOLIDATED BALANCE SHEETS

	March 31, 2010 (unaudited)	December 31, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 2,785,973	$ 7,405,685
Accounts receivable, net	1,707,827	1,043,296
Interest receivable	39,746	65
Note receivable, net	-	54,627
Inventory, net	4,280,353	3,340,712
Prepaid expenses and other assets	212,008	188,812
Total current assets	9,025,907	12,033,197
Held-to-maturity investments	5,054,096	-
Inventory, non-current, net	34,207,000	35,785,205
Property and equipment, net	246,832	218,418
Patent and license rights, net	255,757	260,548
Deferred income taxes, non-current	102,443	-
Other assets, non-current	1,990	1,990
TOTAL ASSETS	$ 48,894,025	$ 48,299,358
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 297,269	$ 265,439
Accrued cooperative advertising	311,000	173,000
Accrued expenses and other liabilities	200,993	157,954
Total current liabilities	809,262	596,393
Long-term liabilities:		
Accrued income taxes	1,031,137	1,058,659
Total liabilities	1,840,399	1,655,052
Commitments and contingencies		
Shareholders' equity:		
Common stock, no par value	52,912,365	52,906,459
Additional paid-in capital – share-based compensation	6,516,756	6,411,727
Accumulated deficit	(12,375,495)	(12,673,880)
Total shareholders' equity	47,053,626	46,644,306
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 48,894,025	$ 48,299,358

See Notes to Condensed Consolidated Financial Statements.

CHARLES & COLVARD, LTD.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited)

	Three Months Ended March 31,	
	2010	**2009**
Net sales	$ 2,853,675	$ 2,485,188
Costs and expenses:		
Cost of goods sold	1,058,981	1,100,089
Sales and marketing	586,598	333,966
General and administrative	1,023,665	2,108,392
Research and development	41,857	210,180
Total costs and expenses	2,711,101	3,752,627
Income (loss) from operations	142,574	(1,267,439)
Interest income	26,522	10,261
Interest expense	(676)	-
Income (loss) before income taxes	168,420	(1,257,178)
Income tax net benefit (expense)	129,965	(27,102)
Net income (loss)	$ 298,385	$ (1,284,280)
Net income (loss) per common share:		
Basic	$ 0.02	$ (0.07)
Fully diluted	$ 0.02	$ (0.07)
Weighted average number of shares used in computing net income (loss) per common share:		
Basic	19,019,402	18,376,588
Fully diluted	19,214,466	18,376,588

See Notes to Condensed Consolidated Financial Statements.

CHARLES & COLVARD, LTD.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Three Months Ended March 31,	
	2010	2009
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 298,385	$ (1,284,280)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	31,887	42,918
Amortization of bond premium	2,894	-
Share-based compensation	107,485	(80,610)
Provision for uncollectible accounts	(40,000)	148,309
Provision for sales returns	(30,000)	(170,000)
Provision for inventory reserves	(96,000)	107,000
Provision (benefit) for deferred income taxes	(102,443)	2,282
Changes in assets and liabilities:		
Accounts receivable	(594,531)	1,823,012
Interest receivable	(39,681)	2,263
Income tax receivable	-	(204)
Note receivable	54,627	-
Inventory	734,564	789,956
Other assets, net	(23,196)	113,963
Accounts payable	31,830	(1,053,951)
Deferred revenue	-	(171,181)
Accrued cooperative advertising	138,000	(176,575)
Accrued income taxes	(27,522)	25,025
Other accrued liabilities, net	43,039	122,526
Net cash provided by operating activities	489,338	240,453
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(48,459)	-
Purchases of long-term investments	(5,056,990)	-
Patent and license rights costs	(7,051)	(203)
Net cash used in investing activities	(5,112,500)	(203)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Stock option exercises	3,450	-
Net cash provided by financing activities	3,450	-
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(4,619,712)	240,250
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	7,405,685	5,587,144
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 2,785,973	$ 5,827,394
Supplemental schedule of non-cash operating activities:		
Inventory acquired from settlement of accounts receivable	$ -	$ 1,188,126

See Notes to Condensed Consolidated Financial Statements.

CHARLES & COLVARD, LTD.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. DESCRIPTION OF BUSINESS

Charles & Colvard, Ltd. (the "Company"), a North Carolina corporation founded in 1995, manufactures, markets, and distributes Charles & Colvard Created Moissanite® jewels (hereinafter referred to as moissanite or moissanite jewels) for sale in the worldwide jewelry market. Moissanite, also known by its chemical name of silicon carbide ("SiC"), is a rare mineral first discovered in a meteor crater. Because naturally occurring SiC crystals are too small for commercial use, larger crystals must be grown in a laboratory. Leveraging the Company's advantage of being the sole source worldwide of lab-created moissanite jewels, the Company's strategy is to establish itself with reputable, high-quality, and sophistica ted brands and to position moissanite as an affordable, luxurious alternative to other gemstones, such as diamond. The Company believes this is possible due to moissanite's exceptional brilliance, fire, luster, durability, and rarity like no other jewel available on the market. The Company primarily sells loose moissanite jewels to jewel distributors and jewelry manufacturers, although it has begun to wholesale a limited amount of finished moissanite jewelry.

2. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation and Principles of Consolidation - The accompanying condensed consolidated financial statements included in this Quarterly Report on Form 10-Q have been prepared in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP") for interim financial information. However, certain information or footnote disclosures normally included in complete financial statements prepared in accordance with U.S. GAAP have been condensed, or omitted, pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). In the opinion of the Company's management, the unaudited statements in this Quarterly Report on Form 10-Q include all normal and recurring adjustments necessary for the fair statement of the results for the interim periods presented. The results for the three months ended March 31, 2010 are not necessarily indicative of the results to be expected for the fiscal year ending December 31, 2010.

The condensed consolidated financial statements as of and for the three months ended March 31, 2010 and 2009 included in this Quarterly Report on Form 10-Q are unaudited. The balance sheet as of December 31, 2009 is obtained from the audited financial statements as of that date. The balance sheet as of December 31, 2009 and the statements of operations and of cash flows for the three months ended March 31, 2009 have been adjusted for a change in accounting for inventories discussed below. The accompanying statements should be read in conjunction with the audited financial statements and related notes, together with management's discussion and analysis of financial condition and results of operations, contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2009 filed with the SEC on March 29, 2010 (the "2009 Annual Report").

The accompanying condensed consolidated balance sheets as of March 31, 2010 and December 31, 2009 and the condensed consolidated statements of operations and of cash flows for the three months ended March 31, 2010 and 2009 include the accounts of the Company and its wholly owned subsidiary in Hong Kong, Charles & Colvard (HK) Ltd., which became a dormant entity in the second quarter of 2009 and the operations of which were ceased in 2008. All intercompany accounts have been eliminated.

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

	Three Months Ended March 31,	
	2010	**2009**
Net sales		
United States	$ 1,646,405	$ 1,728,504
International	1,207,270	756,684
Total	$ 2,853,675	$ 2,485,188

	March 31, 2010	December 31, 2009
Property and equipment, net		
United States	$ 246,832	$ 218,418
International	-	-
Total	$ 246,832	$ 218,418

	March 31, 2010	December 31, 2009
Patent and license rights, net		
United States	$ 84,703	$ 85,496
International	171,054	175,052
Total	$ 255,757	$ 260,548

Significant Accounting Policies - In the opinion of the Company's management, other than a change in method of accounting for inventories, the significant accounting policies used for the three months ended March 31, 2010 are consistent with those used for the year ended December 31, 2009. Accordingly, please refer to the 2009 Annual Report for the Company's significant accounting policies.

Inventories - In April 2010, the Audit Committee of the Company's Board of Directors approved a plan to change the Company's method of accounting for inventories from the first-in, first-out ("FIFO") method to the average cost method. The Company believes that the average cost method is preferable on the basis that it conforms to the manner in which the Company operationally manages its inventories and evaluates wholesale and retail pricing. In addition, the Company is shifting the focus of its business from solely a loose jewel manufacturer to a jewelry manufacturer, and it now considers its peers to be jewelry manufacturers and retailers. Many of these peers utilize the average cost method for valuing their inventories, and this chan ge makes the Company's inventory reporting more consistent to improve comparability among the peer companies. The change was effective January 1, 2010, and prior periods have been retrospectively adjusted for comparative purposes. See Note 5, "Change in Method of Accounting," for additional details.

Use of Estimates - The preparation of financial statements in conformity with U.S. GAAP requires management to 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 the reported amounts of revenues and expenses during the reporting period. The most significant estimates impacting the Company's consolidated financial statements relate to valuation and classification of inventories, accounts receivable reserves, deferred tax assets, uncertain tax positions, and cooperative advertising. Actual results could differ materially from those estimates.

Reclassifications - Certain amounts in the prior year's financial statements have been reclassified to conform to the current year presentation.

Recently Adopted/Issued Accounting Pronouncements - *Multiple-Deliverable Revenue Arrangements.* In October 2009, the Financial Accounting Standards Board ("FASB") issued new U.S. GAAP guidance that requires an entity to allocate revenue arrangement consideration at the inception of an arrangement to all of its deliverables based on their relative selling prices (the relative-selling-price method). The guidance eliminates the use of the residual method of allocation, in which the undelivered element is measured at its estimated selling price and the delivered element is measured as the residual of the arrangement consideration, and requires the relative-selling-price method in all circumstances in which an entity recognizes revenue for an arrangement with multiple deliverables. The new guidance must be adopted no later than the beginning of the first fiscal year beginning on or after June 15, 2010, with early adoption permitted through either prospective application for revenue arrangements entered into, or materially modified, after the effective date or through retrospective application to all revenue arrangements for all periods presented. The Company does not expect the adoption of this guidance to have an effect on its consolidated financial statements.

Improving Disclosures About Fair Value Measurements. In January 2010, the FASB issued new U.S. GAAP guidance to enhance the usefulness of fair value measurements that requires both the disaggregation of information in certain existing disclosures, as well as the inclusion of more robust disclosures about valuation techniques and inputs to recurring and non-recurring fair value measurements. The amended guidance is effective for interim and annual reporting periods beginning after December 15, 2009. The adoption of this guidance did not have a material effect on the Company's consolidated financial statements.

All other new and recently issued, but not yet effective, accounting pronouncements have been deemed to be not relevant to the Company and therefore are not expected to have any impact once adopted.

3. INVESTMENTS

Investments consist of highly liquid, long-term U.S. government agency securities carried at amortized cost. The Company classifies its marketable securities as held-to-maturity based upon management's positive intention and ability to hold these securities until their maturity dates.

The following table summarizes information about held-to-maturity investments at March 31, 2010:

	Amortized Cost	Gross Unrealized Losses	Estimated Fair Value
U.S. government agency securities	$ 5,054,096	$ (24,448)	$ 5,029,648

As of March 31, 2010, the estimated fair value of the investments was less than the amortized cost. Because management believes the unrealized losses are temporary and the investments are classified as held-to-maturity, a permanent impairment to record the investments at fair value was not considered necessary.

The maturities of held-to-maturity investments at March 31, 2010 are as follows:

	After 2 Years through 3 Years	After 3 Years through 4 Years	After 4 Years through 5 Years	Total
U.S. government agency securities	$ 1,510,324	$ 2,783,070	$ 760,702	$ 5,054,096

4. FAIR VALUE MEASUREMENTS

Under U.S. GAAP, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. U.S. GAAP also establishes a hierarchy for inputs used in measuring fair value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are obtained from independent sources and can be validated by a third party, whereas unobservable inputs reflect assumptions regarding what a third party would use in pricing an asset or liability. The fair value hierarchy consists of three levels based on the reliability of inputs, as follows:

Level 1 – quoted prices in active markets for identical assets and liabilities
Level 2 – inputs other than Level 1 quoted prices that are directly or indirectly observable
Level 3 – unobservable inputs that are not corroborated by market data

The Company evaluates assets and liabilities subject to fair value measurements on a recurring and non-recurring basis to determine the appropriate level to classify them for each reporting period. This determination requires significant judgments to be made by the Company. The instruments identified as subject to fair value measurements on a recurring basis are cash and cash equivalents, trade accounts receivable, held-to-maturity investments, trade accounts payable, and accrued expenses. All instruments other than held-to-maturity investments are reflected in the consolidated balance sheets at carrying value, which approximates fair value due to the short-term nature of these instruments. As of March 31, 2010, the Company's held-to-maturity investments utilized Level 2 inputs of similar investments traded on active securities exch anges.

Assets that are measured at fair value on a non-recurring basis include property and equipment and patent and license rights. These items are recognized at fair value when they are considered to be impaired. Level 3 inputs are primarily based on the estimated future cash flows of the asset determined by market inquiries to establish fair market value of used machinery or future revenue expected to be generated with the assistance of patent and license rights.

5. CHANGE IN METHOD OF ACCOUNTING

In April 2010, the Audit Committee of the Company's Board of Directors approved a plan to change the Company's method of accounting for inventories from the FIFO method to the average cost method effective as of January 1, 2010. Accounts affected by this change are net inventories, accumulated deficit, and cost of goods sold. Prior periods have been retrospectively adjusted for comparative purposes.

Components of the Company's consolidated balance sheets adjusted for the effect of the change from the FIFO method to the average cost method are as follows:

	December 31, 2009		
	As Reported	Adjustment	As Adjusted
Current assets:			
Inventory, net	$ 3,470,136	$ (129,424)	$ 3,340,712
Total current assets	12,162,621	(129,424)	12,033,197
Inventory, non-current, net	37,888,622	(2,103,417)	35,785,205
TOTAL ASSETS	50,532,199	(2,232,841)	48,299,358
Shareholders' equity:			
Accumulated deficit	(10,441,039)	(2,232,841)	(12,673,880)
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	50,532,199	(2,232,841)	48,299,358

Components of the Company's consolidated statements of income adjusted for the effect of the change from the FIFO method to the average cost method are as follows:

	Three Months Ended March 31, 2009		
	As Reported	Adjustment	As Adjusted
Costs and expenses:			
Cost of goods sold	$ 1,082,309	$ 17,780	$ 1,100,089
Total costs and expenses	3,734,847	17,780	3,752,627
Loss from operations	(1,249,659)	(17,780)	(1,267,439)
Loss before income taxes	(1,239,398)	(17,780)	(1,257,178)
Net loss	(1,266,500)	(17,780)	(1,284,280)
Net loss per common share:			
Basic	$ (0.07)	$ -	$ (0.07)
Fully diluted	$ (0.07)	$ -	$ (0.07)

Components of the Company's consolidated statements of cash flows adjusted for the effect of the change from the FIFO method to the average cost method are as follows:

	Three Months Ended March 31, 2009		
	As Reported	Adjustment	As Adjusted
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net loss	$ (1,266,500)	$ (17,780)	$ (1,284,280)
Changes in assets and liabilities:			
Inventory	879,176	17,780	896,956
Net cash provided by operating activities	240,453	-	240,453

Had the Company not changed its method of accounting for inventories from the FIFO method to the average cost method, total net inventories as of March 31, 2010 would have been approximately $64,000 lower and cost of goods sold would have been approximately $64,000 higher than reported, resulting in approximately $64,000 of lower income from operations for the three months ended March 31, 2010. Both basic and fully diluted earnings per share would have decreased from $0.02 to $0.01 for the period.

6. INVENTORIES

The Company's total net inventories consisted of the following as of March 31, 2010 and December 31, 2009:

	March 31, 2010	December 31, 2009
Raw materials	$ 6,416,819	$ 6,131,435
Work-in-process	1,731,440	1,714,945
Finished goods	29,165,216	30,153,698
Finished goods on consignment	1,173,878	1,125,839
Totals	$ 38,487,353	$ 39,125,917
Current portion	$ 4,280,353	$ 3,340,712
Non-current portion	34,207,000	35,785,205
Totals	$ 38,487,353	$ 39,125,917

Inventories are stated at the lower of cost or market on an average cost basis. Inventory costs include direct material and labor, inbound freight, purchasing and receiving costs, inspection costs, and warehousing costs. Any inventory on hand in excess of the Company's current requirements based on historical and anticipated levels of sales is classified as non-current on the Company's consolidated balance sheets.

The Company has historically sold one grade of jewel that is classified as very good ("VG") and consists of near-colorless jewels that meet certain standards. Previously, only VG jewels were valued in inventory. During the first quarter of 2010, the Company began a project of sorting its jewels into multiple grades and has identified several potential markets for sale of these jewels.

Obsolescence is not a factor in the Company's loose jewel inventory valuation. The Company's jewels do not degrade over time and inventory generally consists of the cuts and sizes most commonly used in the jewelry industry. In addition, the majority of jewel inventory is not mounted in finished jewelry settings and is therefore not subject to fashion trends. The Company has very small market penetration in the worldwide jewelry market, and the Company has the exclusive right in the United States through mid-2015 and in many other countries through mid-2016 to produce and sell lab-created SiC for use in jewelry applications. In view of the foregoing factors, management has concluded that no excess or obsolete inventory reserve requirements exist as of March 31, 2010.

All inventories are carefully reviewed for quality standards before they are entered into finished goods. As conditions warrant, the Company's grading standards change. The Company reviews the inventory on an ongoing basis to ensure its inventory meets current quality standards.

Periodically, the Company ships finished goods inventory to customers on consignment, or "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. Finished goods on consignment at March 31, 2010 and December 31, 2009 are net of reserves of $150,000 and $147,000, respectively, to allow for certain jewelry on consignment at a customer that has filed for Chapter 11 bankruptcy protection and to allow for certain jewels on consignment with customers that may not be returned or may be returned in a condition that does not meet our current grading standards.

Total loose jewel inventories at March 31, 2010 and December 31, 2009, net of a reserve of $400,000 and including inventory on consignment net of reserves, were $36,778,517 and $37,391,853, respectively. The reserve on loose jewel inventories was established to allow for the carat weight loss associated with the possible future re-cutting of a portion of the inventory to achieve higher quality standards. To date, no portion of the loose jewel inventories has been re-cut. The need for adjustments to reserves is evaluated on a period-by-period basis.

All jewelry inventories are finished goods, the majority of which the Company acquired as part of the January 2009 settlement agreement with Reeves Park, Inc., a former customer, to reduce the outstanding receivable to the Company. Due to the lack of a plan to market this inventory at that time, a jewelry inventory reserve was established to reduce the majority of the jewelry inventory value to scrap value, or the amount the Company would expect to obtain by melting the gold in the jewelry and returning to loose-jewel finished goods inventory those jewels that meet grading standards. This reserve was $1,247,000 and $1,348,000 at March 31, 2010 and December 31, 2009, respectively. Total jewelry inventories at March 31, 2010 and December 31, 2009, net of reserves and including net inventory on consignment, were $1,609,705 and $1,634,049, respectively.

7. INCOME TAXES

During 2008, the Company recorded a valuation allowance against certain deferred tax assets. Due to continued uncertainty over sufficient future taxable income to fully use these deferred tax assets, the Company did not record an income tax benefit for the losses incurred during the three months ended March 31, 2009. However, because of the availability of operating loss carryforwards that are netted against a valuation allowance, the Company also did not recognize an income tax expense for income generated during the three months ended March 31, 2010.

The Company recognized approximately $130,000 of income tax net benefit during the three months ended March 31, 2010. This income tax net benefit consists of a $102,000 reduction of a deferred tax asset valuation allowance to offset liabilities associated with an uncertain tax position and a $41,000 reduction of the liability for the same uncertain tax position, offset by $13,000 of income tax expense recorded for estimated penalties and interest associated with other uncertain tax positions.

8. COMMITMENTS AND CONTINGENCIES

Lease Commitments

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 common-area expenses 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 provided for two rent holidays (August 2004 through September 2004 and August 2005 through May 2006) during which no rent was payable and a $74,000 moving allowance that was paid to the Company in September 2004. The Company recognizes rent expense on a straight-line basis, giving consideration to the rent holidays and the moving allowance paid to the Company. At the Company's option, the lease can be extended for three successive five-year periods.

The future minimum lease payments of the Company are $121,000 in 2010 and $95,000 in 2011, totaling $216,000. Rent expense for the three months ended March 31, 2010 and 2009 was approximately $55,000 and $42,000, respectively.

Purchase Commitments

On June 6, 1997, the Company entered into an amended and restated exclusive supply agreement with Cree, Inc. ("Cree"). The exclusive supply agreement had an initial term of ten years that was extended in January 2005 to July 2015. In connection with the amended and restated exclusive supply agreement, the Company has committed to purchase from Cree a minimum of 50%, by dollar volume, of its raw material SiC crystal requirements. If the Company's orders require Cree to expand beyond specified production levels, the Company must commit to purchase certain minimum quantities. In September 2008, the Company entered into an agreement with Cree to delay the Company's commitment to purchase $710,000 of SiC crystals during the fourth quarter of 2008. Effective March 22, 2010, the Company entered into a letter agreemen t with Cree in connection with the amended and restated exclusive supply agreement under which the Company agreed to purchase approximately $1.2 million of SiC crystals over a period of approximately eight months in 2010 to satisfy this existing purchase commitment and to preserve the exclusivity terms of the amended and restated exclusive supply agreement. During the three months ended March 31, 2010, the Company purchased $289,000 in raw materials, resulting in a remaining purchase commitment of approximately $880,000 at March 31, 2010.

In February 2005, the Company entered into an exclusive supply agreement with Norstel AB ("Norstel") for the supply of raw material SiC crystals for use in the manufacture of moissanite jewels. In April 2008, the Company entered into an amendment to the exclusive supply agreement with Norstel due to an update of Norstel's delivery schedule and capability and also due to the Company's desire to limit its purchase of raw materials. Under this amendment, the Company's minimum purchase commitment from Norstel was to continue until (i) the Company has purchased an aggregate amount of approximately $7.9 million of SiC crystals, or (ii) September 26, 2011, whichever occurs first. This purchase commitment was contingent upon Norstel being able to deliver SiC crystals of acceptable quality in the amount committed. In October 2008, the Company entered into a new letter agreement with Norstel that suspended the Company's commitment to purchase SiC crystals from Norstel during the fourth quarter of 2008.

In addition, as part of the exclusive supply agreement, the Company advanced $400,000 to Norstel in 2005 for the purchase of certain equipment. This advance, which was in the form of a note receivable, began to be repaid in January 2007 through a 20% reduction on each invoice for subsequent purchases of SiC crystals. Effective March 1, 2008, pursuant to the April 2008 amendment, the Company began receiving a 30% reduction on each invoice for subsequent purchases of SiC crystals. In December 2009, the Company received notification from Norstel that it had reached an agreement in principle with a new investor. This agreement was conditioned upon Norstel initiating a company reorganization that would involve unsecured creditors' acceptance of a composition offer to receive 25% of outstanding debts as payment in full. As a result, the Company recorded a reserve of $170,000 on the outstanding advance of $224,627 in the fourth quarter of 2009. Though the Company did not consent to the composition offer, it received notice in January 2010 that the District Court of Norrköping had approved it, and the Company received a cash payment of $56,127 in February 2010. It is the Company's position that, as a result of the failure of Norstel to repay the advance in full as stipulated in the exclusive supply agreement, it has no further purchase obligations under the agreement.

9. SHARE-BASED COMPENSATION

The following table summarizes the components of the Company's share-based compensation included in net income:

	Three Months Ended March 31, 2010	Three Months Ended March 31, 2009
Employee stock options	$ 33,050	$ (160,930)
Restricted stock awards	74,435	80,320
Income tax expense (benefit)	(26,903)	6,525
Total	$ 80,582	$ (74,085)

Due to the Company's valuation allowance against deferred tax assets, all of the above income tax benefit was reserved as of March 31, 2010.

No share-based compensation was capitalized as a cost of inventory during the three months ended March 31, 2010 and 2009. Compensation costs on employee stock options decreased $180,000 during the three months ended March 31, 2009 due to the February 2009 termination of three executive officers.

Stock Options - The following is a summary of the stock option activity for the three months ended March 31, 2010:

	Shares	Weighted Average Exercise Price
Outstanding, December 31, 2009	790,009	$ 2.88
Granted	72,500	$ 1.76
Exercised	(7,500)	$ .46
Canceled	(18,367)	$ 4.07
Outstanding, March 31, 2010	836,642	$ 2.78

The fair value of each option grant is estimated on the grant date using the Black-Scholes-Merton option pricing model. The valuations of options granted during the three months ended March 31, 2010 were based on the following weighted average assumptions:

Dividend yield	0.0 %
Expected volatility	87.5 %
Risk-free interest rate	2.38 %
Expected lives (years)	5.0

Although the Company issued dividends in prior years, a dividend yield was not used due to the uncertainty of future dividend payments. Expected volatility is estimated by giving primary consideration to the historical volatility of the Company's common stock. The risk-free interest rate is based on the published yield available on U.S. Treasury issues with an equivalent term remaining equal to the expected life of the option. The expected lives of the options represent the estimated period of time until exercise or forfeiture and are based on historical experience of similar awards.

The following table summarizes information about stock options outstanding at March 31, 2010:

Options Outstanding			Options Exercisable			Options Vested or Expected to Vest		
Balance as of 3/31/2010	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Balance as of 3/31/2010	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Balance as of 3/31/2010	Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price
836,642	6.32	$ 2.78	500,503	4.12	$ 4.13	808,259	6.21	$ 2.84

As of March 31, 2010, the unrecognized share-based compensation expense related to unvested stock options was approximately $166,000, which is expected to be recognized over a weighted average period of approximately 32 months.

The aggregate intrinsic value of options outstanding, exercisable, and vested or expected to vest at March 31, 2010 was $550,387, $195,918, and $526,901, respectively. This amount is before applicable income taxes and represents the closing market price of the Company's common stock at March 31, 2010 less the grant price, multiplied by the number of options that have a grant price that is less than the closing market price. This amount represents the amount that would have been received by the optionees had these options been exercised on that date. During the three months ended March 31, 2010, the aggregate intrinsic value of options exercised was $6,925.

Restricted Stock - The following is a summary of the restricted stock activity for the three months ended March 31, 2010:

	Shares	**Weighted Average Grant Date Fair Value**
Unvested, December 31, 2009	636,908	$ 0.48
Granted	-	$ -
Vested	(103,262)	$ 0.46
Canceled	-	$ -
Unvested, March 31, 2010	533,646	$ 0.49

On February 23, 2009, the Company granted five of its non-employee Board members (excluding Richard A. Bird) an aggregate of 103,262 shares of restricted stock in connection with the negotiation between the Company and Bird Capital Group, Inc. ("BCG") of a management services agreement ("the BCG Agreement"). The restrictions on these shares lapsed on February 23, 2010. The aggregate fair value of the restricted stock granted was $47,500 based on the closing market price of the Company's common stock on February 19, 2009.

On May 18, 2009, the Company granted its non-employee Board members (excluding Richard A. Bird) an aggregate of 329,787 shares of restricted stock. The restrictions on these shares will lapse on the date of the annual meeting in May 2010, subject to continued service on the Board. The aggregate fair value of the restricted stock granted was $155,000 based on the closing market price of the Company's common stock on May 18, 2009.

On June 23, 2009, the Company granted its newly appointed Chief Financial Officer 60,000 shares of restricted stock. The restrictions on these shares will lapse on June 15, 2010, subject to the Chief Financial Officer's continued employment or service to the Company. The fair value of the restricted stock granted was $30,000 based on the closing market price of the Company's common stock on June 23, 2009.

On June 26, 2009, the Board appointed Dr. Charles D. Lein to serve as a director of the Company, and he was granted 98,039 shares of restricted stock. The restrictions on these shares will lapse on the date of the annual meeting in May 2010, subject to continued service on the Board. The fair value of the restricted stock granted was $50,000 based on the closing market price of the Company's common stock on June 26, 2009.

On November 5, 2009, the Board appointed H. Marvin Beasley to serve as a director of the Company, and he was granted 45,820 shares of restricted stock. The restrictions on these shares will lapse on the date of the annual meeting in May 2010, subject to continued service on the Board. The fair value of the restricted stock granted was $26,576 based on the closing market price of the Company's common stock on November 5, 2009.

As of March 31, 2010, the unrecognized share-based compensation expense related to unvested restricted stock was approximately $42,000, which is expected to be recognized over a weighted average period of approximately two months.

Dividends - The Company has not paid any cash dividends in the current year through March 31, 2010.

10. NET INCOME (LOSS) PER COMMON SHARE

Basic net income (loss) per common share is computed by dividing net income (loss) by the weighted average number of common shares outstanding during the periods. Diluted net income (loss) per common share is computed using the weighted average number of common and dilutive common equivalent shares outstanding during the periods. Common equivalent shares consist of stock options that are computed using the treasury stock method.

The following table reconciles the differences between the basic and diluted earnings per share presentations:

	Three Months Ended March 31,	
	2010	**2009**
Numerator:		
Net income (loss)	$ 298,385	$ (1,284,280)
Denominator:		
Weighted average common shares outstanding		
Basic	19,019,402	18,376,588
Stock options	195,064	-
Diluted	19,214,466	18,376,588
Net income (loss) per common share:		
Basic	$ 0.02	$ (0.07)
Diluted	$ 0.02	$ (0.07)

For the three months ended March 31, 2010 and 2009, stock options to purchase approximately 398,000 and 699,000 shares, respectively, were excluded from the computation of diluted net income (loss) per common share because the exercise price of the options was greater than the average market price of the common shares or the effect of inclusion of such amounts would be anti-dilutive to net income (loss) per common share.

11. MAJOR CUSTOMERS AND CONCENTRATION OF CREDIT RISK

Financial instruments that potentially subject the Company to concentrations of credit risk consist primarily of cash and cash equivalents, investments, and trade accounts receivable. The Company maintains cash, cash equivalents, and investments with high quality financial institutions and invests in low risk securities, primarily money market funds or highly liquid, long-term U.S. government agency obligations. At times, cash balances may exceed the Federal Deposit Insurance Corporation ("FDIC") insurable limits.

Trade receivables potentially subject the Company to credit risk. The Company's standard payment terms on trade receivables are generally between 30 and 90 days. The Company extends credit to its customers based upon a number of factors, including an evaluation of the customer's financial condition and credit history, the customer's payment history with the Company, the customer's reputation in the trade, and an evaluation of the Company's opportunity to introduce its moissanite jewels to new or expanded markets. Collateral is not generally required from customers. The need for an allowance for doubtful accounts is determined based upon factors surrounding the credit risk of specific customers, historical trends, and other information.

As of March 31, 2010, three customers accounted for 26%, 20%, and 12% of trade accounts receivable, respectively. As of December 31, 2009, two customers accounted for 18% and 13% of trade accounts receivable, respectively.

A significant portion of sales is derived from certain customer relationships. The following is a summary of customers that represent greater than or equal to 10% of total gross sales:

	Three Months Ended March 31,	
	2010	2009
Customer A	23%	10%
Customer B	19%	-
Customer C	14%	7%
Customer D	-	11%

12. SUBSEQUENT EVENTS

The Company has performed an evaluation of subsequent events through May 14, 2010, which is the date the financial statements were issued.

On April 21, 2010, the Company entered into a manufacturing/distribution agreement and licensing agreement (the "Agreement"), effective April 19, 2010, with Frederick Goldman, Inc. ("Goldman"). The Agreement sets forth the terms and conditions of the sale of moissanite jewels by the Company to Goldman to be used by Goldman in the manufacturing of jewelry for the exclusive sale and distribution to one of Goldman's customers as part of a test program. If the test program does not begin by a certain date, or if Goldman's customer does not purchase merchandise from Goldman beyond the initial test program merchandise by a certain date, then Goldman's exclusive distribution rights will terminate and revert to non-exclusive rights. Otherwise, Goldman's exclusive distribution rights will automatical ly renew on an annual basis for so long as Goldman satisfies its annual purchase commitment from the Company. As part of the Agreement, the Company granted a non-exclusive license to Goldman to use certain of the Company's trademarks. The Agreement also contains other customary terms and conditions.

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

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, or the Exchange Act. Statements expressing expectations regarding our future and projections relating to products, sales, revenues, and earnings are typical of such statements and are made under the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, but are not limited to, statements about our plans, objectives, representations, and contentions and are not historical facts and typically are identified by use of terms such as "may," "will," "should," "could," "expect," " plan," "anticipate," "believe," "estimate," "predict," "continue," and similar words, although some forward-looking statements are expressed differently.

All forward-looking statements are subject to the risks and uncertainties inherent in predicting the future. You should be aware that although the forward-looking statements included in this report represent management's current judgment and expectations, our actual results may differ materially from those projected, stated, or implied in these forward-looking statements as a result of many factors including, but not limited to, the following:

- *Our future financial performance depends upon increased consumer acceptance and growth of sales of our products.*
- *Our company has recently experienced significant leadership changes.*
- *A further decline in sales could continue to have a material adverse effect on us and our results of operations.*
- *Our business and our results of operations could be materially adversely affected as a result of general economic and market conditions, including the current economic crisis.*
- *We expect to remain dependent upon Cree, Inc., or Cree, for the supply of our SiC crystals for the foreseeable future.*
- *We are currently substantially dependent on a limited number of distributors and jewelry manufacturers*

for the sale of our jewels in North America.

- *We face intense competition in the worldwide jewelry industry.*
- *The financial difficulties or insolvency of one or more of our major customers could adversely affect results.*
- *We are subject to certain risks due to our international distribution channels and vendors.*
- *We rely upon our ability to protect our intellectual property.*
- *Governmental regulation and oversight might adversely impact our operations.*
- *Sales of moissanite jewelry could be dependent upon the pricing on precious metals, which is beyond our control.*
- *Some anti-takeover provisions of our charter documents, agreements, and plan may delay or prevent a takeover of our company.*
- *If we fail to evaluate, implement, and integrate strategic opportunities successfully, our business may suffer.*

Forward-looking statements speak only as of the date they are made. We undertake no obligation to update or revise such statements to reflect new circumstances or unanticipated events as they occur except as required by the federal securities laws, and you are urged to review and consider disclosures that we make in the reports that we file with the Securities and Exchange Commission, or the SEC, that discuss other factors relevant to our business.

The following discussion is designed to provide a better understanding of our unaudited financial statements, including a brief discussion of our business and products, key factors that impacted our performance, and a summary of our operating results. The following discussion should be read in conjunction with the unaudited financial statements and the notes thereto included in Part I, Item 1 of this Quarterly Report on Form 10-Q and the consolidated financial statements and notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended December 31, 2009. Historical results and percentage relationships among any amounts in the financial statements are not necessarily indicative of trends in operating results for any future periods .

Overview

We manufacture, market, and distribute Charles & Colvard Created Moissanite® jewels (which we refer to as moissanite or moissanite jewels) for sale in the worldwide jewelry market. Moissanite, also known by its chemical name of silicon carbide, or SiC, is a rare mineral first discovered in a meteor crater. Because naturally occurring SiC crystals are too small for commercial use, larger crystals must be grown in a laboratory. Leveraging our advantage of being the sole source worldwide of lab-created moissanite jewels, our strategy is to establish Charles & Colvard with reputable, high-quality, and sophisticated brands and to position moissanite as an affordable, luxurious alternative to other gemstones, such as diamond. We believe this is possible due to moissanite's exceptional brilliance, fire, luster, durability, and rarity like no other jewel available on the market.

We primarily sell loose moissanite jewels to some of the largest jewelry manufacturers and distributors in the world, which mount them into fine jewelry. We have also begun to wholesale a limited amount of finished moissanite jewelry. We have historically marketed moissanite to the self-purchasing woman as the perfect reward or indulgence to celebrate her achievements or milestones in her life. However, in 2009, we expanded our marketing message beyond the self-purchasing woman, and with the assistance of our new marketing agency engaged in the first quarter of 2010, we are revising our messaging to expand moissanite's global reach, increase market awareness of our moissanite jewels, develop additional marketing channels to the jewelry trade and the consumer, and help create a more compelling consumer value proposition that we belie ve will drive increased demand for our product.

We have realized some initial successes from the implementation of our strategy and corresponding messaging in the first quarter of 2010. Though the current global economic recession has resulted in a significant slowdown in the retail environment, with the impact on the jewelry industry particularly severe, we believe that market conditions are stabilizing, and we are receiving some feedback from channel partners that demand is improving. Despite this, a number of major retailers continue to have excessive inventories of moissanite jewelry and have curtailed their purchases from jewelry manufacturers to which we sell our moissanite jewels. As a result, in the first quarter of 2010 we focused our sales efforts on (i) supporting existing channel partners to improve sell-through to retailers and end consumers and (ii) identifying new channe l partners that had no inventory overhang issues to open new markets, both domestically and internationally. As a result, our total net sales for the three months ended March 31, 2010 were 15% greater than total net sales during the same period of 2009, with loose jewel sales improving 31% but jewelry sales decreasing 60% as we continued to search for opportunities to replace the JCPenney trunk show event sales that were discontinued in September 2009.

In addition, we achieved a $1.04 million reduction in costs and expenses in the first three months of 2010 as a result of very tight cost control, as well as a non-recurrence of bad debt, severance, certain professional services including management fees paid to Bird Capital Group, Inc., or BCG, and research and development expenses that we incurred in the first three months of 2009.

Net income for the three months ended March 31, 2010 was $298,000, or $0.02 per diluted common share, compared with a net loss of $1.28 million, or $0.07 per diluted common share, for the same period of 2009. Net income for the three months ended March 31, 2010 included a $130,000 income tax benefit resulting in part from the reduction of a deferred tax asset valuation allowance to offset liabilities associated with an uncertain tax position and a reduction of the liability for the same uncertain tax position. We did not recognize an income tax benefit for our operating losses during the first three months of 2009 due to the uncertainty of sufficient future taxable income to utilize our deferred tax assets.

Though we experienced a positive trend in the first quarter of 2010, we continue to operate in a challenging business environment. Therefore, our current priorities continue to be generating positive cash flow and strengthening our financial position through cost-reduction initiatives and selling down our inventory. We will also continue to execute on our strategy developed under the leadership of our new Chief Executive Officer, Randy McCullough, of growing our core business with key jewelry manufacturers and distributors, developing leading global jewelry brands featuring moissanite, and increasing our focus on the end consumer. We believe the results of these efforts will propel Charles & Colvard to new heights of revenue growth and profitability, but we fully recognize the challenges of our business in the current environment. How ever, we believe that we have made much progress in building the right leadership team and defining a strategic roadmap that can significantly improve our business.

Critical Accounting Policies and Estimates

Our discussion and analysis of financial condition and results of operations are based upon our financial statements, which we prepared in accordance with accounting principles generally accepted in the United States, or U.S. GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues, and expenses and related disclosures of contingent assets and liabilities. “Critical accounting policies and estimates” are defined as those most important to the financial statement presentation and that require the most difficult, subjective, or complex judgments. We base our estimates on historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making j udgments about the carrying value of assets and liabilities that are not readily apparent from other sources. Under different assumptions and/or conditions, actual results of operations may materially differ. We have disclosed our critical accounting policies and estimates in our Annual Report on Form 10-K for the year ended December 31, 2009, and that disclosure should be read in conjunction with this Quarterly Report on Form 10-Q.

In April 2010, the Audit Committee of our Board of Directors approved a plan to change our method of accounting for inventories from the first-in, first-out, or FIFO, method to the average cost method. We believe that the average cost method is preferable on the basis that it conforms to the manner in which we operationally manage our inventories and evaluate wholesale and retail pricing. In addition, we are shifting the focus of our business from solely a loose jewel manufacturer to a jewelry manufacturer, and we now consider our peers to be jewelry manufacturers and retailers. Many of these peers utilize the average cost method for valuing their inventories, and this change makes our inventory reporting more consistent to improve comparability among the peer companies. The change was effective January 1, 2010, and prior periods have bee n retrospectively adjusted for comparative purposes. See Note 5, “Change in Method of Accounting,” to our condensed consolidated financial statements in this report for additional details.

Results of Operations

The following table sets forth certain consolidated statements of operations data for the three months ended March 31, 2010 and 2009:

	Three Months Ended March 31, 2010	Three Months Ended March 31, 2009
Net sales	$ 2,853,675	$ 2,485,188
Costs and expenses:		
Cost of goods sold	1,058,981	1,100,089
Sales and marketing	586,598	333,966
General and administrative	1,023,665	2,108,392
Research and development	41,857	210,180
Total costs and expenses	2,711,101	3,752,627
Income (loss) from operations	142,574	(1,267,439)
Interest income	26,522	10,261
Interest expense	(676)	-
Income (loss) before income taxes	168,420	(1,257,178)
Income tax benefit (expense)	129,965	(27,102)
Net income (loss)	$ 298,385	$ (1,284,280)

Net Sales

Net sales for the three months ended March 31, 2010 and 2009 comprise the following:

	Three Months Ended March 31,		Change	
	2010	2009	Dollars	Percent
Loose jewels	$ 2,664,499	$ 2,028,969	$ 635,530	31%
Jewelry	178,315	448,148	(269,833)	-60%
Other	10,861	8,071	2,790	35%
Total net sales	$ 2,853,675	$ 2,485,188	$ 368,487	15%

Net sales were $2.85 million for the three months ended March 31, 2010 compared to $2.49 million for the three months ended March 31, 2009, an increase of $368,000 or 15%. In the first quarter of 2010, carat sales of moissanite jewels and jewelry increased 56% to approximately 20,000 carats from 13,000 carats in the first quarter of 2009. Sales of moissanite jewelry represented 6% of total net sales in the first quarter of 2010 compared to 18% of total net sales in the same period of 2009. The majority of our moissanite jewelry sales in 2009 were to JCPenney for sales at trunk show events, which were discontinued after September 2009. We are pursuing new opportunities in finished jewelry in 2010, but if these opportunities do not come to fruition, we may experience a significant decline in our jewelry sales in 2010. In the first quarter o f 2010, the average selling price per carat for our sales of loose jewels decreased 9% from the first quarter of 2009, primarily as a result of lower prices we implemented in December 2009 and special pricing in the first quarter of 2010 that we extended to support new customers launching in new markets. U.S. net sales accounted for approximately 58% and 70% of net sales during the three months ended March 31, 2010 and 2009, respectively.

U.S. net sales decreased by 5% for the three months ended March 31, 2010 despite an increase in U.S. carat shipments of 58%, which do not include shipments of consigned inventory. U.S. sales decreased during this period primarily due to the reduced average selling price and special programs extended to new customers in support of the development of new markets. As we work to build new manufacturer and distributor relationships to replace lower sales from some of our existing customers due to their high levels of moissanite jewelry and less than desired inventory turns, we may continue to experience in the short-term increased carat shipments with flat to slight growth in our U.S. net sales. As the new management team continues to reposition moissanite and explore new opportunities for our product, we anticipate orders and related sales wi ll continue to improve in 2010; however, as existing retailers evaluate their businesses, we are at risk that some retailers may not be able to achieve acceptable financial performance and may choose not to continue selling moissanite jewelry.

Our two largest U.S. customers during the three months ended March 31, 2010 accounted for 23% and 14%, respectively, of our total sales compared to 10% and 7%, respectively, during the same period of 2009. This improvement in orders occurred as we worked to regain their confidence in us. A third customer accounted for 11% of our total sales in the same period of 2009 but had no sales during the three months ended March 31, 2010. No additional U.S. customers accounted for more than 10% of total sales during the three months ended March 31, 2010 or the same period in 2009. We expect that we will remain dependent on our ability and that of our largest customers to maintain and enhance their retail programs. A change in or loss of any of these customer or retailer relationships could have a material adverse effect on our results of operations.

International net sales and carat shipments, which do not include shipments of consigned inventory, increased by 60% and 54%, respectively, for the three months ended March 31, 2010 as compared to the three months ended March 31, 2009. Our largest international customer during the three months ended March 31, 2010 accounted for 19% of our total sales. International sales increased primarily due to the acquisition of a new customer in India as well as improved sales to existing customers in India and the United Kingdom, offset in part by lower sales in Hong Kong and Thailand. A portion of our international sales represents jewels sold internationally that will be re-imported to North American retailers. Our top three international distributors during the three months ended March 31, 2010 were located in India and the United Kingdom.

Costs and Expenses

Cost of Goods Sold

Cost of goods sold for the three months ended March 31, 2010 and 2009 are as follows:

	Three Months Ended March 31,		Change	
	2010	2009	Dollars	Percent
Cost of goods sold	$ 1,058,981	$ 1,100,089	$ (41,108)	-4%

Cost of goods sold was $1.06 million for the three months ended March 31, 2010 compared to $1.10 million for the three months ended March 31, 2009, a decrease of $41,000 or 4%. Cost of goods sold primarily is composed of inventory sold during the period; inventory written off during the period due to ongoing quality reviews or through customer returns; salaries and benefits for personnel involved in preparing and shipping product to customers; an allocation of shared expenses such as rent, utilities, communication expenses, and depreciation related to preparing and shipping product to customers; and outbound freight charges.

Cost of goods sold decreased primarily due to a $96,000 decrease in our inventory reserves for the three months ended March 31, 2010, compared to an increase in reserves of $107,000 for the same period of 2009. These factors were partially offset during the three months ended March 31, 2010 by increased sales during the period.

Sales and Marketing

Sales and marketing expenses for the three months ended March 31, 2010 and 2009 are as follows:

	Three Months Ended March 31,		Change	
	2010	2009	Dollars	Percent
Sales and marketing	$ 586,598	$ 333,966	$ 252,632	76%

Sales and marketing expenses were $587,000 for the three months ended March 31, 2010 compared to $334,000 for the three months ended March 31, 2009, an increase of $253,000 or 76%.

The increase in sales and marketing expenses is primarily due to a $297,000 net increase in advertising expenses and a $105,000 increase in compensation costs, offset in part by $82,000 in expenses associated with the JCPenney trunk shows that were discontinued in September 2009 and lower general allocations of operating expenses, such as bank fees and commercial insurance, resulting from cost reduction initiatives implemented in the latter part of 2009. Our advertising expenses increased primarily due to cooperative advertising resulting from additional marketing support we provided to a new international customer to help increase our presence in the customer's country and a $128,000 reduction in first quarter 2009 expenses due to customers utilizing less cooperative advertising than estimated. Our cooperative advertising program r eimburses a portion of our customers' marketing costs based on the amount of their purchases from us and is subject to the customer providing us documentation of all advertising copy that includes our products. The increase in compensation costs for the three months ended March 31, 2010 as compared to the same period in 2009 is primarily attributable to $180,000 of previously recorded share-based compensation that was reversed during the three months ended March 31, 2009 due to certain stock options not vesting for terminated employees.

General and Administrative

General and administrative expenses for the three months ended March 31, 2010 and 2009 are as follows:

	Three Months Ended March 31,		Change	
	2010	2009	Dollars	Percent
General and administrative	$ 1,023,665	$ 2,108,392	$ (1,084,727)	-51%

General and administrative expenses were $1.02 million for the three months ended March 31, 2010 compared to $2.11 million for the three months ended March 31, 2009, a decrease of $1.09 million or 51%.

The decrease in general and administrative expenses is primarily due to a $628,000 reduction in professional services, consisting primarily of $350,000 in fees paid during the three months ended March 31, 2009 to BCG under its February 2009 management services agreement with us, $234,000 in reduced fees for legal services, and $57,000 in audit, tax, and investor relations services due to changes in providers and the timing of work performed. Other factors contributing to lower general and administrative expenses in the three months ended March 31, 2010 include $250,000 in severance expense in the three months ended March 31, 2009, offset in part by a $100,000 increase in salaries in the first quarter of 2010 due to new executive leadership; a $190,000 decrease in bad debt expense; and a $52,000 decrease in corporate insurance premiums for the three months ended March 31, 2010 as compared to the same period in 2009.

Research and Development

Research and development expenses for the three months ended March 31, 2010 and 2009 are as follows:

	Three Months Ended March 31,		Change	
	2010	2009	Dollars	Percent
Research and development	$ 41,857	$ 210,180	$ (168,323)	-80%

Research and development expenses were $42,000 for the three months ended March 31, 2010 compared to $210,000 for the three months ended March 31, 2009, a decrease of $168,000 or 80%.

The decrease in research and development expenses during the three months ended March 31, 2010 is primarily attributable to $150,000 of expense associated with our December 2008 research and development agreement that required us to pay $50,000 per month through May 2009.

Interest Income

Interest income for the three months ended March 31, 2010 and 2009 is as follows:

	Three Months Ended March 31,		Change	
	2010	2009	Dollars	Percent
Interest income	$ 26,522	$ 10,261	$ 16,261	158%

Interest income was $27,000 for the three months ended March 31, 2010 compared to $10,000 for the three months ended March 31, 2009, an increase of $16,000 or 158%.

This increase resulted primarily from higher cash balances in 2010 and investments made in the first quarter of 2010 of cash in excess of operating requirements in U.S. government agency securities with higher yields than those of previous cash equivalent investments.

Provision for Income Taxes

During 2008, we recorded a valuation allowance against certain deferred tax assets. Due to continued uncertainty over sufficient future taxable income to fully use these deferred tax assets, we did not record an income tax benefit for the losses incurred during the three months ended March 31, 2009. However, because of the availability of operating loss carryforwards that are netted against a valuation allowance, we also did not recognize an income tax expense for income generated during the three months ended March 31, 2010. Until such time that the uncertainty is overcome, we do not expect to recognize income tax expense or benefit for operating income or loss in future periods.

We recognized approximately $130,000 of income tax net benefit in the first quarter of 2010. This income tax net benefit consists of a $102,000 reduction of a deferred tax asset valuation allowance to offset liabilities associated with an uncertain tax position and a $41,000 reduction of the liability for the same uncertain tax position, offset by $13,000 of income tax expense recorded for estimated penalties and interest associated with other uncertain tax positions.

During the three months ended March 31, 2009, we recorded an income tax expense of $27,000 primarily due to interest and penalties accrued under U.S. GAAP for uncertain tax positions.

Our statutory tax rate is 38.5% and consists of the federal income tax rate of 34% and the North Carolina state income tax rate of 4.5%, net of the federal benefit.

Liquidity and Capital Resources

We require cash to fund our operating expenses and working capital requirements, including outlays for capital expenditures. As of March 31, 2010, our principal sources of liquidity were cash and cash equivalents totaling $2.79 million, trade accounts receivable of $1.71 million, and inventory of $4.28 million, as compared to cash and cash equivalents totaling $7.41 million, trade accounts receivable of $1.04 million, and inventory of $3.34 million as of December 31, 2009. During the three months ended March 31, 2010, we purchased $5.05 million of highly liquid U.S. government agency securities that we have classified as held-to-maturity long-term assets on our consolidated balance sheets due to our positive intention and ability to hold these securities until their maturity dates.

During the three months ended March 31, 2010, our working capital decreased by approximately $3.22 million to $8.22 million from $11.44 million at December 31, 2009. As described more fully below, the decrease in working capital at March 31, 2010 is primarily attributable to cash invested in long-term investments, a decrease in note receivable, and increases in accrued expenses, offset in part by increases in trade accounts receivable, interest receivable, and reclassifications of inventory between short-term and long-term.

During the three months ended March 31, 2010, $489,000 of cash was provided by operations primarily as a result of our net income of $298,000, a net decrease in inventory of $639,000, and an increase in accrued cooperative advertising of $138,000, which more than offset a net increase in trade accounts receivable of $665,000. Accounts receivable increased primarily due to higher sales during the quarter.

We purchased $289,000 of raw material during the three months ended March 31, 2010 in partial satisfaction of outstanding purchase commitments with Cree, as discussed below. Our raw material inventories of SiC crystals are purchased under exclusive supply agreements with a limited number of suppliers. Because the supply agreements restrict the sale of these crystals exclusively to us, the suppliers negotiate minimum purchase commitments with us that, combined with our reduced sales, have resulted in levels of inventories that are higher than we might otherwise maintain. Our current rate of sales and our high level of inventory resulted in $34.21 million of our inventories being classified as long-term assets at March 31, 2010.

Our Amended and Restated Exclusive Supply Agreement with Cree, or the Cree Exclusive Supply Agreement, for the supply of SiC crystals expires in July 2015. In connection with the Cree Exclusive Supply Agreement, we have committed to purchase from Cree a minimum of 50%, by dollar volume, of our raw material SiC crystal requirements. If our orders require Cree to expand beyond specified production levels, we must commit to purchase certain minimum quantities. In September 2008, we entered into an agreement with Cree to delay our commitment to purchase $710,000 of SiC crystals during the fourth quarter of 2008. Effective March 22, 2010, we entered into a letter agreement with Cree in connection with the Cree Exclusive Supply Agreement under which we agreed to purchase approximately $1.2 million of SiC crystals over a period of approximately eight months in 2010 to satisfy this existing purchase commitment and to preserve the exclusivity terms of the Cree Exclusive Supply Agreement.

Under an Exclusive Supply Agreement with Norstel, or the Norstel Exclusive Supply Agreement, for the supply of raw material SiC crystals, our minimum purchase commitment from Norstel was to continue until (i) we purchased an aggregate amount of approximately $7.9 million of SiC crystals, or (ii) September 26, 2011, whichever occurs first. We have purchased $550,000 of SiC crystals since inception of the Norstel Exclusive Supply Agreement.

As part of the Norstel Exclusive Supply Agreement, we advanced $400,000 to Norstel in 2005 for the purchase of certain equipment. The balance on the advance as of September 30, 2009 was $224,627. In December 2009, we received notification from Norstel that it had reached an agreement in principle with a new investor. This agreement was conditioned upon Norstel initiating a company reorganization that would involve unsecured creditors' acceptance of a composition offer to receive 25% of outstanding debts as payment in full. As a result, we recorded a reserve of $170,000 on the advance in the fourth quarter of 2009. Though we did not consent to the composition offer, we received notice in January 2010 that the District Court of Norrköping had approved it, and we received a cash payment of $56,127 in February 2010. It is our posit ion that, as a result of the failure of Norstel to repay the advance in full as stipulated in the Norstel Exclusive Supply Agreement, we have no further purchase obligations under the agreement.

Despite current period operating income, we did not make any income tax payments during the three months ended March 31, 2010 due to our net operating loss carryforwards. As of March 31, 2010, we have $434,000 of remaining federal income tax credits, $102,000 of which expire between 2014 and 2016 and the balance without an expiration, which can be carried forward to offset future income tax. As of March 31, 2010, we also had a federal operating loss carryforward of approximately $5.3 million expiring between 2028 and 2029, which can be used to offset against future federal taxable income, and a North Carolina tax net operating loss carryforward of approximately $9.8 million expiring between 2015 and 2024, which can be offset against future state taxable income.

In November 2009, our Board of Directors authorized a repurchase program for up to 1,000,000 shares of our common stock through August 12, 2010. Repurchases can be made in the open market or in privately negotiated transactions. We expect to use available cash to finance these purchases and will determine the timing and amount of stock repurchases based on our evaluation of market conditions and other factors. As of March 31, 2010, there remained 958,330 shares of our common stock approved for repurchase under the repurchase program. During the three months ended March 31, 2010, we repurchased no shares.

Our future capital requirements and the adequacy of available funds will depend on many factors, including the risk factors described in more detail in "Risk Factors" in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2009. 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, provided that there are no extraordinary events and that economic conditions impacting consumer spending do not further deteriorate and adversely affect the demand for moissanite. There can be no assurance that the efforts taken to date and future actions will be able to withstand the impact of any economic downturn that extends deeper or longer than we currently anticipate , or that any strategic efforts by our management to increase sales will be successful. Under these conditions, our operations and other sources of funds may not be sufficient to fund our operations, and we may be required to seek alternative sources of funding. There is no assurance, however, that we will be able to obtain financing on acceptable terms, or at all, especially in light of the ongoing turmoil in the financial markets.

Recent Developments

On April 21, 2010, we entered into a manufacturing/distribution agreement and licensing agreement, or the Agreement, effective April 19, 2010, with Frederick Goldman, Inc., or Goldman. The Agreement sets forth the terms and conditions of the sale of moissanite jewels by us to Goldman to be used by Goldman in the manufacturing of jewelry for the exclusive sale and distribution to one of Goldman's customers as part of a test program. If the test program does not begin by a certain date, or if Goldman's customer does not purchase merchandise from Goldman beyond the initial test program merchandise by a certain date, then Goldman's exclusive distribution rights will terminate and revert to non-exclusive rights. Otherwise, Goldman's exclusive distribution rights will automatically renew on an annual basis for so long as Goldman satisfies its annual purchase commitment from us. As part of the Agreement, we granted a non-exclusive license to Goldman to use certain of our trademarks. The Agreement also contains other customary terms and conditions.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Not applicable.

Item 4. Controls and Procedures

Not applicable.

Item 4T. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a compan y in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate, to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, as ours are designed to do, and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control Over Financial Reporting

We routinely review our internal control over financial reporting and from time to time make changes intended to enhance the effectiveness of our internal control over financial reporting. We will continue to evaluate the effectiveness of our disclosure controls and procedures and internal control over financial reporting on an ongoing basis and will take action as appropriate. During the three months ended March 31, 2010, we made no changes to our internal control over financial reporting, as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, that we believe materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1. Legal Proceedings

There are no material pending legal proceedings to which the Company is a party or to which any of the Company's property is subject.

Item 1A. Risk Factors

We discuss in our Annual Report on Form 10-K for the year ended December 31, 2009 various risks that may materially affect our business. For the three months ended March 31, 2010, there were no material changes to such risks.

Item 6. Exhibits

The following exhibits are being filed herewith and are numbered in accordance with Item 601 of Regulation S-K:

Exhibit No.	Description
10.1	Corporate Incentive Plan, effective January 1, 2010 (incorporated herein by reference to Exhibit 10.1 to our Current Report on Form 8-K, filed with the SEC on March 23, 2010)
10.2	Letter Agreement, effective March 22, 2010, between Cree, Inc. and Charles & Colvard, Ltd. (incorporated herein by reference to Exhibit 10.6 to our Annual Report on Form 10-K for the year ended December 31, 2009)*
10.3	Director Compensation Structure, effective November 11, 2009 (incorporated herein by reference to Exhibit 10.18 to our Annual Report on Form 10-K for the year ended December 31, 2009)
10.4	Independent Contractor Agreement, effective as of July 1, 2009, by and between Charles & Colvard, Ltd. and Neil Boss, as supplemented through February 26, 2010
18.1	Preferability Letter from Frazer Frost, LLP regarding change in accounting principle
31.1	Certification by Chief Executive Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification by Chief Financial Officer pursuant to Rule 13a-14(a) under the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification by 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 by Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

* Asterisks located within the exhibit denote information which has been redacted pursuant to a request for confidential treatment filed with the SEC.

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.

May 14, 2010	By:	/s/ Randy N. McCullough Randy N. McCullough President and Chief Executive Officer
May 14, 2010	By:	/s/ Timothy L. Krist Timothy L. Krist Chief Financial Officer (Principal Financial Officer and Chief Accounting Officer)

EXHIBIT INDEX

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INDEPENDENT CONTRACTOR AGREEMENT

THIS INDEPENDENT CONTRACTOR AGREEMENT, made effective as of the 1st day of July, 2009 by and between Charles & Colvard, Ltd., a North Carolina corporation (the "Company"), and Neil Boss (the "Contractor").

RECITALS:

A. The Company is engaged in the business of designing, developing, manufacturing, and selling moissanite jewels (the "Business") and desires to engage the Contractor to assist the Company in providing financial and accounting services (the "Services") for the business.

B. The Contractor desires to provide such services to the Company on the terms and for the compensation set forth herein.

NOW THEREFORE, the parties hereto agree as follows:

1. Engagement. The Company hereby engages the Contractor as a nonexclusive contractor to perform the Services (as defined herein) subject to the terms and conditions of this Agreement, and the Contractor hereby accepts such engagement for and in consideration of the compensation hereinafter provided and agrees to use his best efforts in performing the Services. The Contractor shall perform his obligations hereunder in compliance with the terms of this Agreement and any and all applicable laws and regulations. The Contractor acknowledges that this is a nonexclusive engagement by the Company and that the Company retains the right to appoint additional contractors as the Company, in its sole and unrestricted judgment, may from time to time determine to be in the best interests of the Company without liability or obligation to the Contractor.

2. Services.

a. The Contractor agrees to provide financial and accounting services for the Company and perform other duties related thereto as the Company may determine from time to time (the "Services"). Contractor warrants to the Company that the Services will be performed in a professional, timely and workmanlike manner.

b. The Contractor shall execute a Confidential Disclosure Agreement in substantially the form attached hereto as Exhibit A concurrent with the execution of this Agreement.

3. Licenses, Tools and Materials. Contractor shall be responsible for obtaining, at Contractor's own expense, all licenses, permits and bonds as may be required by any federal, state or local law or regulation for the performance of Contractor's duties hereunder. The Company shall be responsible for supplying at its cost all necessary tools and materials to be used by Contractor.

4. Limitations. Nothing in this Agreement shall be construed to give the Contractor authority to represent the Company before any court or governmental or regulatory agency without the express prior written authorization of the Company. In addition, all files, books, accounts, records and other information of any nature, however recorded or stored, and related to the Company (the "Records") shall at all times belong to the Company and to the extent possessed by the Contractor hereunder, such possession shall be for the benefit

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

of and as agent for the Company. The Contractor's possession of the Records is at the will of the Company and is solely for the purpose of enabling the Contractor to perform his obligations hereunder. The Records shall be readily separable from the records of the Contractor.

5. **Term.** The term of this Agreement shall commence on the date hereof and shall continue thereafter through and including the close of business on June 30, 2010. Notwithstanding the foregoing, the Company may terminate this Agreement for "cause," as defined herein, by giving written notice of at least 30 days in advance of its desire to terminate this Agreement for cause. The Company shall be deemed to have cause for terminating Contractor's engagement in the event Contractor (i) demonstrates any dishonesty or engages in any act of moral turpitude, (ii) impr operly performs or fails to perform the Services described herein, (iii) causes intentional damage to substantial property of the Company, or (iv) is unable to perform the Services because of death or a disability which renders him unable to perform the Services for 30 consecutive calendar days.

6. **Fees.** As compensation for the performance of the Services, the Company shall pay the Contractor at a rate of $90 per hour worked, billable in ¼ hour increments. Contractor will submit a report of hours worked every 2 weeks and C&C will pay contractor within 2 weeks from receipt of this report. No amounts (including without limitation, social security, federal and state withholding taxes) shall be withheld or otherwise subtracted from the compensation paid to the Contractor pursuant to this Section 5 unless required by law. In addition, the Contractor sh all be reimbursed for all expenses incurred by the Contractor on behalf (and with the prior written authorization) of the Company, in accordance with the attached C&C Travel and Expense Policy, from the date the Contractor delivers an itemized report of such expenses, together with receipts or other evidence of payment reasonably satisfactory to the Company and its accountant. C&C agrees to pay for existing employee healthcare benefits for the month of July 2009.

7. **Background Check, Credit Check, Drug Testing and Searches.** The Contractor understands and agrees that (i) the Company may require the Contractor to undergo a criminal background check, a credit check and/or drug testing as a condition of being allowed to perform the Services, (ii) in the sole discretion of the Company, the Contractor may be prohibited from performing the Services based upon the results of a background check, a credit check or drug test, and (iii) the Company may conduct a reasonable search of the Contractor if the Company has reasonable suspicion to believe that the Contractor has in his possession property belonging to the Company.

8. **Indemnification.** The Contractor shall defend, release, indemnify and hold the Company and its directors, officers, shareholders, employees and agents and the personal representatives and assigns of each, harmless from and against any and all claims, suits, liability, costs and expenses, including, without limitation, attorneys' fees and expenses, in connection with any knowing and intentional act or omission of the Contractor, his employees and/or agents in connection with the provision of the Services.

9. **Insurance Representations, Workplace Safety.** The Contractor agrees to maintain liability, worker's compensation, errors and omission and/or other insurance in such amounts and with such carriers as the Company may reasonably request, each of which policies shall, upon request of the Company, name the Company as an additional insured. In addition, the Contractor shall be solely responsible for workplace safety, shall maintain the workplace in accordance with industry standards and shall comply with all governmental (including federal, state and local) regulations.

10. **Notices.** All notices, demands, requests or other communications which may be or are required to be given, served or sent by one party to the other party pursuant to this Agreement shall be in writing and shall be hand delivered or mailed by certified mail, return receipt requested, postage prepaid, or sent by telefax, addressed as follows:

If to the Company:

300 Perimeter Park Dr. Suite A
Morrisville, NC 27560
Attention: Richard A. Bird, CEO
Phone: 919-468-0399

If to the Contractor:

Neil S. Boss
9409 Treymore Drive
Raleigh, NC 27617
919-426-4143

Each party may designate by notice in writing a new address to which any notice, demand, request or communication may thereafter be delivered, given or sent. Documents delivered by hand shall be deemed to have been received upon delivery; documents sent by telefax shall be deemed to have been received when the answer back is received; and documents sent by mail shall be deemed to have been received upon their receipt, or at such time as delivery is refused by the addressee upon presentation.

11. Security. The Contractor agrees that he will at all times comply with all security regulations in effect from time to time at the Company's premises or applicable outside such premises, to materials belonging to the Company. The Contractor agrees not to use or disclose to any party any information, systems, equipment, ideas, processes, or methods of operation observed in connection with the performance of his obligations hereunder.

12. Independent Contractor.

a. Acknowledgment by Contractor. Contractor acknowledges and agrees that Contractor will be treated, vis-a-vis the Company as an independent contractor *and not as an employee, agent or authorized representative of the Company*. Contractor shall have no authority to bind the Company to any contract, agreement or obligation whatsoever. The acts of Contractor shall in no way constitute the acts of the Company and Contractor shall not represent to any third party that Contractor has any express or implied authority to bind the Company to any such contract, agreement or obligation.

b. Tax Matters. Because Contractor is an independent contractor, the Company will not withhold from any compensation paid to Contractor any amounts for federal or state income taxes, or social security (FICA) for Contractor, nor will the Company pay any social security or unemployment tax with respect to Contractor. Such taxes are the responsibility of Contractor. Contractor agrees to indemnify and hold the Company (including its employees, officers, directors, agents, subsidiaries or affiliates) harmless, and hereby indemnifies and hold the Company harmless, from and against any damage, claim, assessment, interest charge or penalty incurred by or charged to the Company as a result of any claim, cause of action or assessment by any federal or state government or agency for any nonpayment or late payment by Contractor of any tax or contribution based upon compensation paid hereunder or because the Company did not withhold any taxes from compensation paid hereunder.

c. No Insurance. Consistent with Contractor's status as an independent contractor, the Company will not provide Contractor with any company, individual or group insurance policy or any other kind of insurance coverage whatsoever.

13. Assignment. Neither this Agreement or any interest herein or any rights hereunder shall be sold or assigned by the Contractor, nor shall any of the duties of the Contractor hereunder be delegated to any person, firm or corporation, without prior notice to and consent of the Company.

14. Intellectual Property. Any inventions, copyrights, or other intellectual property created or developed by Contractor or Contractor's employees, or associates or sub-contractors during the term of this Agreement related to the work performed under the Agreement shall be assigned to the Company.

15. Standard of Care. The Contractor warrants that he will exercise due diligence to perform the Services in a professional manner in compliance with all applicable laws and regulations and the highest ethical standards. In addition the Contractor represents and warrants that any information which he may supply the Company during the term of this Agreement (i) will have been obtained by the Contractor lawfully and from publicly available sources, and (ii) will not be confidential or proprietary to any third person. Nothing in this Agreement shall be construed as authorizing o r encouraging the Contractor to obtain information for the Company in violation of any third party's rights to copyright or trade secret protection.

16. Miscellaneous.

a. The provisions of this Agreement may be waived, altered, amended or repealed, in whole or in part, only on the written consent of the Company and the Contractor.

b. Section headings and numbers used in this Agreement are included for convenience of reference only, and, if there is any conflict between any such numbers and headings, and the text of this Agreement, the text shall control. Each of the statements set forth in the premises of this Agreement is incorporated into the Agreement as a valid and binding representation of the party or parties to whom it relates.

c. This Agreement shall be governed by and construed in accordance with the laws of the State of North Carolina without reference to the choice of law principles thereof. If any dispute arises hereunder, the parties hereto agree that any suit brought by either party shall be heard in the courts of North Carolina or any federal court sitting in North Carolina, and the parties hereto consent to the jurisdiction of such courts.

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

e. This Agreement, together with the Confidential Disclosure Agreement herein referenced represent the entire agreement of the parties with respect to the subject matter hereof and supersede in their entirety any and all prior written or oral agreements with respect thereto.

f. Neither party shall have the right under this Agreement to use the name, trademark or trade names of the other, unless prior written approval has been obtained. Any such approval or authorization shall cease upon termination of this Agreement.

g. During the term of this agreement, C&C will supply contractor with a laptop computer and blackberry.

IN WITNESS WHEREOF, the duly authorized representatives of the parties have executed this Independent Contractor Agreement as of the date and year first above written.

COMPANY

CHARLES & COLVARD, LTD.

By: /s/ R. A. Bird
Richard A. Bird, CEO

CONTRACTOR

By: /s/ Neil S. Boss
Neil S. Boss

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ADDENDUM TO INDEPENDENT CONTRACTOR AGREEMENT

THIS ADDENDUM will supplement the INDEPENDENT CONTRACTOR AGREEMENT, made effective as of the 1st day of July, 2009 by and between Charles & Colvard, Ltd., a North Carolina corporation (the "Company"), and Neil Boss (the "Contractor").

RECITALS:

A. The Company agrees to offer Contractor a minimum of 25 hours of billable time each week during the period beginning August 1, 2009 and ending January 31, 2010. If the Company does not offer 25 hours of work per week during this period, the company will still pay contractor at $90 per hour for the 25 hour minimum. Contractor also agrees to make himself available for a minimum of 25 hours per week during this period. Contractor can inform the Company of time needed off with at least 7 days notice and time off may not exceed 7 consecutive business days. Company is not obligated to pay the minimum 25 hours per week for time requested off by Contractor.
B. All other terms of the Independent Contractor Agreement made effective July 1, 2009 remain in effect.

IN WITNESS WHEREOF, the duly authorized representatives of the parties have executed this Independent Contractor Agreement as of the date and year first above written.

COMPANY

CHARLES & COLVARD, LTD.

By: /s/ Timothy L. Krist
Timothy Krist, CFO

CONTRACTOR

By: /s/ Neil S. Boss
Neil S. Boss

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2nd ADDENDUM TO INDEPENDENT CONTRACTOR AGREEMENT

THIS 2nd ADDENDUM will supplement the INDEPENDENT CONTRACTOR AGREEMENT (“IC Agreement”), made effective as of the 1st day of July, 2009 by and between Charles & Colvard, Ltd., a North Carolina corporation (the "Company"), and Neil Boss (the "Contractor").

RECITALS:

A. The Company agrees to offer Contractor a minimum of 25 hours of billable time each week during the period beginning February 1, 2010 and ending April 30, 2010. If the Company does not offer 25 hours of work per week during this period, the company will still pay contractor at $80 per hour for the 25 hour minimum. Contractor also agrees to make himself available for a minimum of 25 hours per week during this period. Contractor can inform the Company of time needed off with at least 7 days notice and time off may not exceed 7 consecutive business days. Company is not obligated to pay the minimum 25 hours per week for time requested off by Contractor.
B. Item 5 of the IC Agreement is hereby amended to reflect that the term of the IC Agreement shall be extended through June 30, 2011.
C. Item 6 of the IC Agreement is hereby amended to reflect that the company shall pay Contractor at a rate of $80 per hour effective February 1, 2010. Effective May 1, 2010 and through the term of the IC agreement, Contractor will not be paid for consultations of less than 15 minutes.
D. All other terms of the Independent Contractor Agreement made effective July 1, 2009 remain in effect.
E. All other terms of the 1st Addendum to Independent Contractor Agreement made remain in effect unless otherwise superceded in this 2nd Addendum.

IN WITNESS WHEREOF, the duly authorized representatives of the parties have executed this Independent Contractor Agreement as of the date and year first above written.

COMPANY

CHARLES & COLVARD, LTD.

By: /s/ Timothy L. Krist
Timothy Krist, CFO

Date 12/13/09

CONTRACTOR

By: /s/ Neil S. Boss
Neil S. Boss

Date 12/14/09

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3td ADDENDUM TO INDEPENDENT CONTRACTOR AGREEMENT

THIS 3rd ADDENDUM will supplement the INDEPENDENT CONTRACTOR AGREEMENT ("IC Agreement"), made effective as of the 1st day of July, 2009 by and between Charles & Colvard, Ltd., a North Carolina corporation (the "Company"), and Neil Boss (the "Contractor").

RECITALS:

A. The Company agrees to offer Contractor a minimum of 25 hours of billable time each week during the period beginning May 1, 2010 and ending July 31, 2010. If the Company does not offer 25 hours of work per week during this period, the company will still pay contractor at $80 per hour for the 25 hour minimum. Contractor also agrees to make himself available for a minimum of 25 hours per week during this period. Contractor can inform the Company of time needed off with at least 7 days notice and time off may not exceed 7 consecutive business days. Company is not obligated to pay the minimum 25 hours per week for time requested off by Contractor. The weekly minimum of 25 hours is subject to change upon mutual agreement of the parties.
B. All other terms of the Independent Contractor Agreement made effective July 1, 2009 remain in effect.
C. All other terms of the 1st Addendum and 2nd Addendum to Independent Contractor Agreement made remain in effect unless otherwise superceded in this 3rd Addendum.

IN WITNESS WHEREOF, the duly authorized representatives of the parties have executed this Independent Contractor Agreement as of the date and year first above written.

COMPANY

CHARLES & COLVARD, LTD.

By: /s/ Timothy L. Krist
Timothy Krist, CFO

Date 2/26/10

CONTRACTOR

By: /s/ Neil S. Boss
Neil S. Boss

Date 2/26/10

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

{Frazer Frost, LLP Letterhead}

Board of Directors
Charles & Colvard, Ltd.
300 Perimeter Park Drive, Suite A
Morrisville, North Carolina 27560

Dear Directors,

We are providing this letter to you for inclusion as an exhibit to your Form 10-Q filing pursuant to Item 601 of Regulation S-K.

We have been provided a copy of Charles & Colvard, Ltd.'s (the "Company") quarterly report on Form 10-Q for the period ended March 31, 2010. Note 5, therein describes a change in accounting principle for inventory costing from the first-in, first-out method to the average cost method. It should be understood that the preferability of one acceptable method of accounting over another for inventory costing has not been addressed in any authoritative accounting literature, and in expressing our concurrence below, we have relied on management's determination that this change in accounting principle is preferable. Based on our reading of management's stated reasons and justification for this change in accounting principle in th e Form 10-Q and our discussions with management as to their judgment about the relevant business planning factors relating to the change, we concur with management that such change represents, in the Company's circumstances, the adoption of a preferable accounting principle in conformity with Accounting Standard Codification 250-10, "Accounting Changes and Error Corrections." We have not audited any financial statements of the Company as of any date or for any period subsequent to December 31, 2009. Accordingly, our comments are subject to change upon completion of an audit of the financial statements covering the period of the accounting change.

Very truly yours,

/s/ FRAZER FROST, LLP

Little Rock, Arkansas
May 13, 2010

Exhibit 31.1

**CERTIFICATION PURSUANT TO SECURITIES AND EXCHANGE ACT OF 1934
RULE 13a-14(a) AS ADOPTED PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, Randy N. McCullough, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2010 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 other certifying officer 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) 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

   (d) 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 (the registrant's fourth fiscal quarter in the case of an annual report) 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 and I have disclosed, based on our 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.

By: /s/ Randy N. McCullough

Randy N. McCullough
President and Chief Executive Officer

May 14, 2010

Exhibit 31.2

**CERTIFICATION PURSUANT TO SECURITIES AND EXCHANGE ACT OF 1934
RULE 13a-14(a) AS ADOPTED PURSUANT TO SECTION 302
OF THE SARBANES-OXLEY ACT OF 2002**

I, Timothy L. Krist, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2010 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 other certifying officer 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) 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

   (d) 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 (the registrant's fourth fiscal quarter in the case of an annual report) 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 and I have disclosed, based on our 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.

	By: /s/ Timothy L. Krist
May 14, 2010	Timothy L. Krist
	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 quarterly period ended March 31, 2010 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Randy N. McCullough, Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; 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/ Randy N. McCullough
Randy N. McCullough
President and Chief Executive Officer
May 14, 2010

This Certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and shall not be deemed “filed” by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and shall not be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Report, irrespective of any general incorporation language contained in such filing.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

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 quarterly period ended March 31, 2010 as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Timothy L. Krist, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, to my knowledge, that:

(1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; 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/ Timothy L. Krist
Timothy L. Krist
Chief Financial Officer
May 14, 2010

This Certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, and shall not be deemed “filed” by the Company for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, and shall not be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Report, irrespective of any general incorporation language contained in such filing.

A signed original of this written statement required by Section 906 of the Sarbanes-Oxley Act of 2002 has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.