NUTRACEA
Form 10-Q
May 12, 2008

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**SECURITIES AND EXCHANGE COMMISSION**
**Washington, D.C. 20549**

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**FORM 10-Q**

(Mark one)
x QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2008

¨ TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____________ to _____________

Commission File Number 0-32565

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**NUTRACEA**
(Exact Name of Registrant as Specified in its Charter)

| **California**<br>(State or other jurisdiction of incorporation or organization) | **87-0673375**<br>(I.R.S. Employer Identification No.) |
|---|---|
| **5090 North 40th St., Suite 400**<br>**Phoenix, AZ**<br>(Address of Principal Executive Offices) | **85018**<br>(Zip Code) |

**Issuer's telephone number, including area code: (602) 522-3000**

Check whether the issuer (1) 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 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.

Large accelerated filer o Accelerated filer x

Non-accelerated filer o (do not check if a smaller reporting company) Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule l2b-2 of the Exchange Act). Yes o No x

**APPLICABLE ONLY TO CORPORATE ISSUERS**

State the number of shares outstanding of each of the issuer's classes of common equity, as of the latest practicable date: 167,693,724 as of May 2, 2008.

**FORM 10-Q**

Index


| | | |
|---|---|---|
| **PART I.** | **FINANCIAL INFORMATION** | |
| Item 1. | Financial Statements | |
| | (a) Consolidated Condensed Balance Sheets at March 31, 2008 (Unaudited) and December 31, 2007 | 4 |
| | (b) Consolidated Condensed Statements of Operations for the three months ended March 31, 2008 and 2007 (Unaudited) | 5 |
| | (c) Consolidated Condensed Statements of Comprehensive (Loss) Income for the three months ended March 31, 2008 and 2007 (Unaudited) | 6 |
| | (d) Consolidated Condensed Statements of Cash Flows for the three months ended March 31, 2008 and 2007 (Unaudited) | 7 |
| | (e) Notes to Unaudited Consolidated Condensed Financial Statements | 8 |
| Item 2. | Management's Discussion and Analysis of Financial Condition and Results of Operations | 22 |
| Item 3. | Quantitative and Qualitative Disclosures About Market Risk | 26 |
| Item 4. | Controls and Procedures | 26 |
| **PART II.** | **OTHER INFORMATION** | 28 |
| Item 1. | Legal Proceedings | 28 |
| Item 1A. | Risk Factors | 28 |
| Item 2. | Unregistered Sales of Equity Securities and Use of Proceeds | 35 |
| Item 3. | Defaults Upon Senior Securities | 35 |
| Item 4. | Submission of Matters to a Vote of Security Holders | 35 |
| Item 5. | Other Information | 35 |
| Item 6. | Exhibits | 35 |
| Signatures | | 37 |
| Certifications | | |

**FORWARD-LOOKING STATEMENTS**

This quarterly report on Form 10-Q contains “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact are “forward-looking statements” for purposes of federal and state securities laws, including, but not limited to, any projections of earnings, revenue or other financial items; any statements of the plans, strategies and objectives of management for future operations; any statements concerning proposed new services or developments; any statements regarding future economic conditions or performance; any statements of belief; and any statements of assumptions underlying any of the foregoing.

Forward-looking statements may include the words “may,” “could,” “will,” “estimate,” “intend,” “continue,” “believe,” “e “anticipate” or other similar words. The forward-looking statements contained herein reflect our current views with respect to future events and are subject to certain risks, uncertainties and assumptions. Actual results may differ materially from those projected in such forward-looking statements due to a number of factors, risks and uncertainties, including the factors that may affect future results set forth in this Current Report on Form 10-Q and in our annual Report on Form 10-K for the year ended December 31, 2007. We disclaim any obligation to update any forward looking statements as a result of developments occurring after the date of this quarterly report.

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**PART 1. FINANCIAL INFORMATION**

**Item 1. Financial Statements**

**NUTRACEA AND SUBSIDIARIES**
**CONSOLIDATED CONDENSED BALANCE SHEETS**

| | March 31, 2008 (Unaudited) | December 31, 2007 |
|---|---|---|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | $ 5,816,000 | $ 41,298,000 |
| Restricted cash | 5,281,000 | 758,000 |
| Trade accounts receivable, net of allowance for doubtful accounts of $3,168,000 and $2,999,000, respectively | 3,066,000 | 2,346,000 |
| Inventories | 3,831,000 | 1,808,000 |
| Notes receivable, current portion, net of allowance for doubtful notes receivable of $543,000 and $250,000, respectively | 7,145,000 | 2,936,000 |
| Deposits and other current assets | 2,480,000 | 2,545,000 |
| | | |
| Total current assets | 27,619,000 | 51,691,000 |
| | | |
| Restricted cash | 1,791,000 | 1,791,000 |
| Notes receivable, net of current portion | 44,000 | 5,039,000 |
| Property and equipment, net | 38,939,000 | 19,328,000 |
| Investment in joint venture | 9,348,000 | 1,191,000 |
| Patents and trademarks, net of accumulated amortization | 5,534,000 | 5,743,000 |
| Other non-current | 50,000 | - |
| Goodwill | 52,765,000 | 39,510,000 |
| | | |
| Total assets | $ 136,090,000 | $ 124,293,000 |
| | | |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable and accrued liabilities | $ 13,646,000 | $ 7,506,000 |
| Deferred revenue | 291,000 | 90,000 |
| Note payable, current portion | 4,424,000 | 23,000 |
| | | |
| Total current liabilities | 18,361,000 | 7,619,000 |
| | | |
| Long-term liabilities: | | |
| Long-term liabilities | 6,278,000 | - |
| Notes payable, net of current portion | 71,000 | 77,000 |
| Total liabilities | 24,710,000 | 7,696,000 |
| | | |
| Commitments and contingencies | | |
| | | |
| Shareholders' equity: | | |

| | | | | |
|---|---|---|---|---|
| Common stock, no par value, 350,000,000 shares authorized, 145,525,000 and 144,108,000 shares issued and outstanding | | 179,237,000 | | 177,813,000 |
| Accumulated deficit | | (67,968,000) | | (61,216,000) |
| Foreign currency cumulative translation gain | | 111,000 | | - |
| Total shareholders' equity | | 111,380,000 | | 116,597,000 |
| | | | | |
| Total liabilities and shareholders' equity | $ | 136,090,000 | $ | 124,293,000 |

The accompanying notes are an integral part of these consolidated condensed financial statements.

**NUTRACEA AND SUBSIDIARIES**
**CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS**
**(Unaudited)**

| | Quarters ended | |
|---|---|---|
| | **March 31, 2008** | **March 31, 2007** |
| Revenues | | |
| Net product sales | $ 5,084,000 | $ 1,987,000 |
| Royalty | 27,000 | 10,000 |
| Total revenue | 5,111,000 | 1,997,000 |
| | | |
| Cost of goods sold | 4,279,000 | 1,113,000 |
| Product warranty cost | 515,000 | - |
| Total cost of sales | 4,794,000 | 1,113,000 |
| | | |
| Gross Margin | 317,000 | 884,000 |
| | | |
| Operating expenses | | |
| Research and development expenses | 264,000 | 121,000 |
| Selling, general and administrative expenses | 5,178,000 | 2,293,000 |
| Professional fees | 1,958,000 | 459,000 |
| Total operating expenses | 7,400,000 | 2,873,000 |
| | | |
| Loss from operations | (7,083,000) | (1,989,000) |
| | | |
| Other income (expense) | | |
| Interest and other income | 260,000 | 512,000 |
| Interest expense | (120,000) | - |
| Other income | 245,000 | - |
| Equity (loss) in joint venture | (17,000) | - |
| Gain on settlement | - | 1,250,000 |
| Net loss before taxes | (6,715,000) | (227,000) |
| | | |
| Provision for income taxes | (37,000) | (20,000) |
| | | |
| Net loss | $ (6,752,000) | $ (247,000) |
| | | |
| Basic and diluted earnings per share: | | |
| Basic loss per share | $ (0.05) | $ (0.00) |
| | | |
| Weighted average basic number of shares outstanding | 144,779,000 | 111,959,000 |

The accompanying notes are an integral part of these consolidated condensed financial statements.

**NUTRACEA AND SUBSIDIARIES**
**CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE LOSS**
**(Unaudited)**

| | Quarters ended March 31, 2008 | Quarters ended March 31, 2007 |
|---|---|---|
| Net loss | $ (6,752,000) | $ (247,000) |
| | | |
| Other comprehensive income: | | |
| Cumulative Foreign currency translation gain | 111,000 | - |
| | | |
| Net comprehensive loss | $ (6,641,000) | $ (247,000) |

The accompanying notes are an integral part of these consolidated condensed financial statements.

**NUTRACEA AND SUBSIDIARIES**
**CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS**
**(Unaudited)**

| | Three Months Ended | |
|---|---|---|
| | **March 31, 2008** | **March 31, 2007** |
| Cash flows from operating activities: | | |
| Net loss | $ (6,752,000) | $ (247,000) |
| Adjustments to reconcile net loss to net cash used in operating activities: | | |
| Depreciation and amortization | 728,000 | 278,000 |
| Provision for doubtful notes receivable | 293,000 | - |
| Provision for doubtful accounts receivable | 75,000 | - |
| Stock-based compensation | 800,000 | 438,000 |
| Loss on equity investment | 17,000 | - |
| | | |
| Net changes in operating assets and liabilities (net of effects of Irgovel acquisition and Vital Living, Inc. consolidation): | | |
| Trade accounts receivable | 447,000 | 363,000 |
| Inventories | (1,044,000) | (547,000) |
| Other current assets | 675,000 | (678,000) |
| Accounts payable and accrued liabilities | 3,624,000 | (1,379,000) |
| Recognition of deferred income | 201,000 | (69,000) |
| Other non-current liabilities | 123,000 | - |
| Net cash used in operating activities | (813,000) | (1,841,000) |
| | | |
| Cash flows from investing activities: | | |
| Restricted cash | (4,523,000) | - |
| Proceeds from payments of notes receivable | 677,000 | 625,000 |
| Issuance of notes receivable | (182,000) | (309,000) |
| Investment in Irgovel (net of cash acquired with purchase) | (14,970,000) | - |
| Purchases of property and equipment | (8,128,000) | (2,356,000) |
| Investment in joint venture | (8,175,000) | - |
| Purchases of other intangible assets | (96,000) | (24,000) |
| Net cash used in investing activities | (35,397,000) | (2,064,000) |
| | | |
| Cash flows from financing activities: | | |
| Proceeds from private placement financing, net of expenses | - | 46,877,000 |
| Proceeds from exercise of common stock options | 685,000 | 3,930,000 |
| Registration costs | (61,000) | - |
| Payments on notes payable | (7,000) | -- |
| Net cash provided by financing activities | 617,000 | 50,807,000 |
| | | |
| Effect of foreign currency | 111,000 | - |
| Net (decrease) increase in cash | (35,482,000) | 46,902,000 |
| | | |
| Cash, beginning of period | 41,298,000 | 14,867,000 |
| Cash, end of period | $ 5,816,000 | $ 61,769,000 |
| | | |
| Supplemental disclosures: | | |
| Cash paid for interest | $ 120,000 | $ - |

| | | | | |
|---|---|---|---|---|
| Cash paid for income taxes | $ | 37,000 | $ | - |
| Non-cash disclosures of investing and financing activities: | | | | |
| Issuance of note payable for acquisition of building | $ | 4,400,000 | $ | - |
| Accounts receivable converted to note receivable | $ | - | $ | 3,516,000 |
| Conversion of preferred stock to common stock | $ | - | $ | 5,488,000 |

The accompanying notes are an integral part of these consolidated condensed financial statements.

**NUTRACEA AND SUBSIDIARIES**
**NOTES TO UNAUDITED CONSOLIDATED CONDENSED FINANCIAL STATEMENTS**

## 1. BASIS OF PRESENTATION

The accompanying unaudited interim consolidated condensed financial statements of NutraCea have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission (“SEC”), and should be read in conjunction with the audited consolidated financial statements and notes thereto contained in NutraCea’s Annual Report filed with the SEC on Form 10-K. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of financial position and the results of operations for the interim periods presented have been reflected herein. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year. Notes to the consolidated financial statements that would substantially duplicate the disclosures contained in the audited financial statements for 2007 as reported in the 10-K have been omitted.

The unaudited condensed consolidated financial statements include the accounts of NutraCea and our wholly-owned subsidiaries as well as a variable interest entity, Vital Living, Inc., for which we are the primary beneficiary as defined by Financial Accounting Standards Board (“FASB”), Interpretation No. 46 (revised 2003), “Consolidation of Variable Interest Entities,” or FIN 46R. We have a 90% interest in NutraCea-Cura LLC, which is also consolidated under FIN 46R. In February 2007, we acquired 100% ownership of Irgovel, which operates a rice-bran oil manufacturing facility in Pelotas, Brazil (see Note 10). All inter-company accounts and transactions have been eliminated.

We operate in two business segments (see Note 14); Nutracea, which manufactures and distributes nutritional supplements primarily derived from Stabilized Rice Bran (“SRB”), and Irgovel, our rice-bran oil manufacturing subsidiary in Pelotas, Brazil.

***Foreign currencies***

The functional currency for the Company’s wholly owned subsidiary, Irgovel is the Brazilian Real (R$). Accordingly, balance sheet accounts of these subsidiaries are translated into United States dollars using the exchange rate in effect at the balance sheet date, and revenues and expenses are translated using the average exchange rates in effect during the period. The gains and losses from foreign currency translation of the financial statements of these subsidiaries are reported as a separate component of stockholders’ equity under the caption “Accumulated other comprehensive income (loss).”

## 2. STOCK-BASED COMPENSATION

On January 1, 2006, NutraCea adopted SFAS No. 123(R), “Share-Based Payment” (“SFAS 123(R)”). SFAS 123(R) replaced SFAS No. 123 and supersedes APB Opinion No. 25. SFAS 123(R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. NutraCea adopted SFAS 123(R) using the modified prospective method which requires the application of the accounting standard as of January 1, 2006. The consolidated financial statements as of and for the three months ended March 31, 2008 and 2007 reflect the impact of adopting SFAS 123(R).

For all agreements where stock is awarded as partial or full consideration, the expense is valued at the fair value of the stock. Expenses for stock options and warrants issued to consultants and employees are calculated based upon fair value using the Black-Scholes valuation method.

Stock-based compensation expenses consisted of the following for the three months ended March 31:

| | 2008 | 2007 |
|---|---|---|
| Consultants | $ 397,000 | $ 85,000 |
| Directors | 197,000 | 47,000 |
| Employees | 423,000 | 251,000 |
| Research and development | 33,000 | - |
| To directors and former director for services Outside of directors duties | - | 55,000 |
| Total stock-based compensation expense | $ 1,050,000 | $ 438,000 |

The Company used the following weighted average assumptions to estimate the fair value of options and warrants granted for the three months ended March 31, 2008 and 2007:

| | 2008 | 2007 |
|---|---|---|
| Risk-free interest rate | 3.15% | 4.79% |
| Expected volatility | 84.1% | 69.6% |
| Expected term (years) | 2.6 | 3.3 |
| Resulting average fair value | $ 0.60 | $ 2.50 |

The Company's unrecognized compensation expense, before income tax and adjusted for estimated forfeitures, related to outstanding unvested stock-based awards as of March 31, 2008 was approximately as follows:

| | Weighted average Remaining Expense Life (years) | Unrecognized Expense |
|---|---|---|
| Options and warrants | 4.24 | $ 6,461,000 |

**3. MARKETABLE SECURITIES**

On September 8, 2004, NutraCea purchased 1,272,026 shares of Langley Park Investment Trust, PLC ("Langley"), a United Kingdom closed-end mutual fund that is actively traded on a London exchange. Per the Stock Purchase Agreement, NutraCea paid with 7,000,000 shares of its own common stock. On September 8, 2006, NutraCea commenced a lawsuit against Langley in the United States District Court for the Eastern District of California, Sacramento Division regarding this transaction. The matter was settled on March 27, 2007. Pursuant to the settlement, NutraCea received $1,250,000 from Langley in March. The $1,250,000 settlement is included in the statement of operations as other income in the three months ended March 31, 2007. During the third quarter of 2007 Langley ceased trading and began the process of liquidating the investments. NutraCea has received cash of $127,000 from this liquidation. The realizable value of the balance of the funds is uncertain and as a result we have recorded the fair market value of Langley as $0 at December 31, 2007.

**4. INVENTORY**

Inventories are composed of the following;

| | March 31, 2008 | December 31, 2007 |
|---|---|---|
| Finished goods | $ 1,972,000 | $ 1,396,000 |
| Work in process | 399,000 | - |
| Raw materials | 1,008,000 | 184,000 |
| Packaging supplies | 452,000 | 228,000 |
| | $ 3,831,000 | $ 1,808,000 |

**5. NOTES RECEIVABLE**

At March 31, 2008, we held eleven secured promissory notes payable to the Company with aggregate outstanding amounts under these notes of $7,189,000 (net of allowance for doubtful notes receivable of $543,000), $7,145,000 is reported as current and $44,000 as long-term. These secured promissory notes bear interest at annual rates ranging from 5% to 10% with the principal and all accrued interest due and payable to us at dates ranging from July 2007 to October 2012.

During the three months ended March 31, 2008 we loaned a total of $182,000 to certain strategic customers, which loans were evidenced by promissory notes, and received payments totaling $677,000 on existing promissory notes. During the three months ended March 31, 2008 and 2007 we also accrued interest income of $106,000 and $139,000, respectively, and received cash payments of $31,000 and $115,000 for accrued interest, respectively.

In April 2007, we converted $365,000 of a customers' accounts receivable to a note receivable, combining it with an existing note from that customer for a total note receivable of $500,000, bearing interest at 10% and due in October 2007. This note was past due as of December 31, 2007. We recorded an allowance for doubtful notes of $250,000 against this receivable for the year ended December 31, 2007. In March, 2008 we re-negotiated the settlement terms and extended the due date to April 2008, received payment of the penalty interest due of $10,000 on this note and added the remaining accrued interest due on the note to the balance due creating a total note receivable of $542,000. As of May 2, 2008 this note remains unpaid therefore we have recorded an additional allowance for doubtful accounts of $293,000 against this note in the first quarter of 2008 (see Note 9).

During the second quarter of 2007, we granted to Pacific Holdings Advisors Limited ("PAHL") certain rights under a license to use and distribute SRB. PAHL paid a one-time fee of $5,000,000 for these rights by issuing to NutraCea an interest bearing promissory note due over five year terms. In January 2008, the payment terms of the promissory note were amended to allow for the forgiveness of accrued interest on the note if the full principal was paid by March 31, 2008. We received the $5,000,000 payment on April 1, 2008, however, as the payment was in transit on that date the company agreed to honor the forgiveness of interest due thru March 31, 2008 of approximately $175,000. As of March 31, 2008 we reduced interest receivable and interest income by $175,000.

**6. PROPERTY AND EQUIPMENT**

Property and equipment consists of the following:

| | March 31, 2008 | December 31, 2007 |
|---|---|---|
| Land | $ 237,000 | $ 15,000 |
| Furniture and fixtures | 2,425,000 | 2,405,000 |
| Vehicles | 32,000 | - |
| Software | 410,000 | 402,000 |
| Leasehold improvements | 1,027,000 | 700,000 |
| Property, plant and equipment | 22,272,000 | 14,243,000 |
| Construction in progress | 15,786,000 | 4,347,000 |
| Total property, plant, and equipment | 42,189,000 | 22,112,000 |
| | | |
| Less accumulated depreciation | (3,250,000) | (2,784,000) |
| Total property, plant, and equipment, net | $ 38,939,000 | $ 19,328,000 |

Depreciation expense for the three months ended March 31, 2008 and 2007 was $519,000 and $178,000, respectively.

**7. OTHER INTANGIBLE ASSETS**

Other intangibles consisted of the following at:

| | March 31, 2008 | December 31, 2007 |
|---|---|---|
| Patents | $ 2,657,000 | $ 2,657,000 |
| Copyrights and trademarks | 3,288,000 | 3,288,000 |
| Non-compete agreements | 650,000 | 650,000 |
| License and supply agreement | 220,000 | 220,000 |
| Subtotal of other intangible assets | 6,815,000 | 6,815,000 |
| Less accumulated amortization | (1,281,000) | (1,072,000) |
| Total other intangible assets, net | $ 5,534,000 | $ 5,743,000 |

Amortization expense for the three months ended March 31, 2008 and 2007 was $209,000 and $100,000, respectively.

**8. LOSS PER SHARE**

Basic loss per share is computed by dividing net loss by the weighted average number of common shares outstanding during all periods presented. Options and warrants are excluded from the basic loss per share calculation and may be considered in calculating the diluted (loss) earnings per share.

The dilutive effect of outstanding options, warrants is calculated using the treasury stock method and the dilutive effect of the convertible series B preferred stock, and convertible series C preferred stock is calculated using the as-if converted method.

As of March 31, 2008, and 2007, options and warrants to purchase approximately 41,552,000 and 51,444,000 shares of our common stock were outstanding, respectively. These are excluded from the calculation of diluted loss per share

at March 31, 2008 and 2007 because their inclusion would have been anti-dilutive.

Components of basic and diluted loss per share were as follows:

| | Three Months Ended March 31, | |
|---|---|---|
| | 2008 | 2007 |
| Net loss | $ (6,752,000) | $ (247,000) |
| Weighted average outstanding shares of common stock | 144,779,000 | 111,959,000 |
| Loss per share: | | |
| Basic and diluted loss per share | $ (0.05) | 0.00 |

At March 31, 2008, and 2007, the number of "in-the-money" options and warrants outstanding was 19,834,000 and 39,182,000, respectively. The weighted average exercise price of "in-the-money" anti-dilutive options and warrants for the three months ended March 31, 2008 and 2007 were $0.45 and $0.70, respectively.

**9. CONCENTRATION OF CREDIT RISK**

Financial instruments that potentially subject us to significant concentrations of credit risk consist primarily of trade accounts receivable and notes receivable for sales to major customers. We perform credit evaluations on our customers' financial condition and generally do not require collateral on accounts receivable.

*Accounts receivable*

We maintain an allowance for doubtful accounts on our receivables based upon expected collection of all accounts receivable. A summary of the activity in the allowance for doubtful accounts for the three months ended March 31, 2008 and 2007 follows:

| | Three Months Ended March 31, | |
|---|---|---|
| | 2008 | 2007 |
| Balance, beginning of period | $ 2,999,000 | $ 20,000 |
| Irgovel acquisition | 94,000 | - |
| Adjusted beginning balance | 3,093,000 | 20,000 |
| Provision for allowance for doubtful accounts charged to operations | 96,000 | - |
| Losses charged against allowance | (21,000) | - |
| Balance, end of period | $ 3,168,000 | $ 20,000 |

During the three months ended March 31, 2008 and 2007 we recorded an allowance for doubtful accounts receivable of $75,000 and $0, respectively. Our bad debt expense for the three months ended March 31, 2008 and 2007 was $96,000 (consisting of the $75,000 provision and $21,000 of specific write-offs) and $0, respectively.

For the three months ended March 31, 2008, two customers accounted for a total of 16% of sales: 12%, and 4% respectively. No other customer was responsible for more than 4% of total sales.

As of March 31, 2008 two customers accounted for 51%, or $3,041,000, of our trade accounts receivable. Our reserve for doubtful accounts receivable above of $3,168,000 includes a 100% reserve against the amounts due from both of those customers.

For the three months ended March 31, 2007, two customers accounted for a total of 73% of sales: 64%, and 9% respectively.

*Notes receivable*

We maintain an allowance for doubtful accounts on our notes receivables based upon expected collection of all notes receivable. A summary of the activity in the allowance for doubtful accounts for the three months ended March 31, 2008 and 2007 follows:

| | Three Months Ended March 31, | |
|---|---|---|
| | 2008 | 2007 |
| Balance, beginning of period | $ 250,000 | $ - |
| Provision for doubtful notes receivable charged to operations | 293,000 | - |
| Balance, end of period | $ 543,000 | $ - |

During the three months ended March 31, 2008 and 2007 we recorded a provision for doubtful notes receivable of $293,000 and $0, respectively.

**10. ACQUISITIONS AND JOINT VENTURES**

*Irgovel*

On January 31, 2008, NutraCea entered into a Quotas (share) Purchase and Sale Agreement (“Purchase Agreement”) with the Quota Holders (“Sellers”) of Irgovel - Industria Riograndens De Oleos Vegetais Ltda., a limited liability company organized under the laws of the Federative Republic of Brazil (“Irgovel”). Irgovel, located in Brazil, owns and operates a rice bran oil processing facility in Pelotas, Brazil, South America.

In February 2008, we completed the purchase of Irgovel paying $15,049,000 for 100% of the company. The total consideration of $15,049,000 includes approximately $50,000 in legal fees which we incurred and added to the purchase price and a $649,000 hold-back provision which is due to the sellers in June 2008. Additionally, we agreed to fund as necessary up to $5,300,000 to pay deferred taxes due to the Brazilian government. These deferred taxes are included in the liabilities on Irgovel’s financial statements and are payable over periods up to 10 years.

The following table summarized the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition. The Company is in the process of obtaining third-party valuations of property, plant, and equipment and certain intangible assets; the allocation of the purchase price is subject to refinement:

| | |
|---|---|
| Cash | $ 79,000 |
| Accounts receivable | 1,242,000 |
| Inventory | 979,000 |
| Other current assets | 635,000 |
| Property and equipment | 7,605,000 |
| Other non-current assets | 23,000 |
| Goodwill | 13,158,000 |
| Total Assets | 23,721,000 |

| | |
|---|---|
| Accounts payable and accrued liabilities | 2,516,000 |
| Other non-current liabilities | 6,156,000 |
| | |
| Net assets acquired | $ 15,049,000 |

*Medan, LLC*

On January 24, 2008, NutraCea, through a newly formed wholly-owned subsidiary, Medan, LLC, a Delaware limited liability company ("Medan"), entered into a Stock Purchase Agreement ("Purchase Agreement") with Fortune Finance Overseas Ltd., a British Virgin Islands company ("FFOL"). Pursuant to the Purchase Agreement, on March 28, 2008, Medan purchased 9,700 shares of capital stock of PT Panganmas Inti Nusantara, an Indonesian Company ("PIN"), from FFOL for $8,175,000 after approval of PIN's Foreign Investment Application. In addition, Medan will purchase an additional 3,050 shares from PIN for $2,500,000 after certain government approvals are obtained. Upon completion of these transactions, Medan will own 51% of the capital stock of PIN and FFOL will own 49%. PIN owns land and has obtained the permits necessary to construct a wheat facility in Kuala Tnajung, Medan, North Sumatra, Indonesia. A principle shareholder of FFOL, Agus Irawn is also a former director of PIN and a principle officer and shareholder of PAHL.

Medan and FFOL will enter a voting agreement where each party will vote all of their shares in a manner so that PIN's Board of Directors and Board of Commissioners shall consist of an even number of persons designated each by Medan and FFOL. NutraCea entered into this Purchase Agreement to construct and operate a full scale, wheat bran stabilization facility in the Republic of Indonesia. The purchase agreement includes a provision for Theorem Capital Partners to earn a $500,000 commission upon the completion of the transaction. The $500,000 is payable immediately upon completion of the transaction which is considered to be reasonably assured and is expected to occur in the second quarter of 2008. We have accrued the charge for this broker fee in our statement of operations for the three months ended March 31, 2008. Additionally, upon completion of the transaction Theorem will earn an option to purchase 500,000 shares of our common stock at an exercise price of $1.50, which expires in five years. The estimated fair value of this option is $250,000 as of March 31, 2008 and we have accrued this charge in our statement of operations for the quarter ended March 31, 2008.

Concurrently with the Purchase Agreement, NutraCea entered into a Wheat Bran Stabilization Equipment Lease ("Lease") with PIN. Pursuant to the Lease, NutraCea will lease to PIN wheat stabilization equipment developed by NutraCea for use at PIN's facility. The term of the lease will be for 15 years with an automatic extension of 5 years if the facility is fully operational and the equipment is still being used in the operations of the facility. The lease amount payable by PIN will be the actual cost incurred for manufacturing and installing the equipment at the facility.

Our investment in PIN is accounted for under the equity method of accounting. At March 31, 2008 the value of our investment was $8,175,000.

*Rice Science LLC*

In December 2007 we formed Rice Science, LLC ("RS"), a Delaware LLC with Herbal Science Singapore PTe. Ltd. ("HS"), a Singapore corporation. We formed this LLC with HS to acquire from Herbal Science certain Isolates License Rights and to commercialize and sell the SRB Isolates. NutraCea and HS have an 80% and 20% interest in the operating results, respectively, but HS has no interest in the initial capital contributions.

We made an initial capital contribution to RS in December 2007 of $1,200,000 as specified in the LLC agreement. We may make an additional $1,000,000 contribution at our discretion and maintain our 80% holding. HS contributed certain Licenses as their capital contribution with a deemed value of $440,000. There are no further capital contributions required of either member. However HS does not have an interest in the initial capital contributed by NutraCea and will not have a minority interest until there are results of operations.

NutraCea holds an 80% interest in RS and therefore will account for the investment as a consolidated subsidiary. As of March 31, 2008 the LLC had no sales, operations or expenses. Summary financial information for RS as of March 31, 2008 is as follows:

| Assets | | |
|---|---|---|
| Cash | $ | 1,200,000 |
| Liabilities and Equity | | |
| Members equity - NutraCea, Inc. | | 1,200,000 |
| Total liabilities and equity | $ | 1,200,000 |

Grainnovation, Inc.

In April 2007, we acquired 100% of the outstanding stock of Grainnovation, Inc. (“GI”) a privately held company that had equipment for pelletizing horse feed for equine customers of strategic value to NutraCea, and certain assets used in GI’s business for a total of $2,150,000, of which $1,605,000 of the purchase price was paid at closing, with the balance held in third-party escrow. In November, 2007, the second installment of $235,000 due was distributed and in April 2008 the last and final installment of $310,000 was distributed to the sellers from the third-party escrow as agreed.

The following table summarized the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition. We incurred $20,000 in legal fees relating to this purchase, which are added to the purchase price and Goodwill. The Company is in the process of obtaining third-party valuations of certain intangible assets; the allocation of the purchase price is subject to refinement:

| | | |
|---|---|---|
| Cash | $ | 1,000 |
| Accounts receivable | | 26,000 |
| Inventory | | 11,000 |
| Property and equipment | | 623,000 |
| Covenant not to compete | | 650,000 |
| Goodwill | | 917,000 |
| Total Assets | | 2,228,000 |
| | | |
| Accrued liabilities | | 58,000 |
| | | |
| Net assets acquired | $ | 2,170,000 |

*Grain Enhancements LLC*

In June 2007, we entered into a joint venture with PAHL to form Grain Enhancements LLC (“GE”), a Delaware limited liability company. NutraCea and PAHL each hold a 47.5% share of Grain Enhancements. The remaining interest is held by Theorem Group LLC (“Theorem”) (3.333%) and Ho’okipa Capital Partners, Inc. (1.667%). The purpose of GE is to develop and market stabilized rice bran (“SRB”) and related products in certain Southeast Asian countries. GE will purchase SRB exclusively from NutraCea until its own facilities are in operation and NutraCea will lease to GE at cost the necessary equipment for such facilities. Payments under the equipment lease will be payable in full upon installation of the equipment.

Under the agreement, NutraCea and PAHL will contribute up to $5,000,000 each to GE to fund the operations, of which $1,500,000 each was due on June 30, 2007. Both members made their initial contribution in July 2007. Additionally, $2,000,000 each was to be contributed no later than October 2007, and the remaining $1,500,000 from each member was due no later than August 2008. Only the initial capital contribution of $1,500,000 from each

member has been made. On January 24, 2008, NutraCea and PAHL amended certain terms of the Operating Agreement. Pursuant to the modified agreement, the timing of mandatory capital contributions of the members was changed from the agreed upon schedule to a determination by GE's finance committee on an as-needed basis. In addition, PAHL will no longer receive a monthly management fee.

Theorem was paid $750,000 and $500,000 by NutraCea and GE, respectively, for services relating to the formation of the joint venture. Our portion of Grain Enhancements net loss for the three months ended March 31, 2008 was $17,000.

Our investment in Grain Enhancements is accounted for under the equity method of accounting. At March 31, 2008 the value of our investment was $1,173,000.

Summary financial information of Grain Enhancements, LLC at March 31, 2008 is:

| | | |
|---|---|---|
| Assets | | |
| Cash | $ | 2,366,000 |
| Liabilities and equity | | |
| Accounts payable and accrued liabilities | $ | 20,000 |
| Members equity | | 3,000,000 |
| Accumulated deficit | | (654,000) |
| Total equity | | 2,346,000 |
| Total liabilities and equity | $ | 2,366,000 |

*Vital Living, Inc.*

In April 2007, we acquired certain securities of Vital Living, Inc. ("VLI"), a publicly traded company. VLI distributes nutritional supplements using similar processes as NutraCea for manufacturing and distribution. We paid $1,000,000 for 1,000,000 shares of outstanding preferred stock and $4,226,000 for the outstanding Senior Secured Notes ("Notes"). The Notes are convertible to VLI common stock and bear interest at 12% per annum, payable June 15 and December 15 and mature in December 2008. On September 11, 2007, NutraCea and VLI entered into a letter agreement confirming their agreement to eliminate the conversion rights of the Notes. In addition, the parties agreed that until such time, if any, as NutraCea gives 30 days prior written notice to VLI, VLI may not pay accrued interest under the Notes in shares of VLI Common Stock, without NutraCea's consent, and that during such time VLI will not be deemed to be in default under the Notes as a result of not paying accrued interest in such shares.

On September 28, 2007, NutraCea entered into an Asset Purchase Agreement (the "Purchase Agreement") with Vital Living. The Purchase Agreement provides that NutraCea will purchase substantially all of Vital Living's intellectual property and other assets used by Vital Living and certain subsidiaries in its business, including rights to nutritional supplements and nutraceutical products that are marketed for distribution to healthcare practitioners. As part of the transaction, Vital Living will assign to NutraCea its rights under various distribution and other agreements relating to the products being acquired. NutraCea will not acquire inventory, raw materials, cash or accounts receivable of Vital Living.

The purchase price consists of (i) $1,500,000 to be paid by NutraCea at the closing, (ii) cancellation of outstanding indebtednesses of Vital Living, its subsidiaries and certain related entities to NutraCea, including all of the Notes, and (iii) cancellation of all shares of Series D Preferred Stock of Vital Living held by NutraCea.

Completion of the transaction is subject to a variety of customary closing conditions, including, among other things, approval of the transaction by the stockholders of Vital Living at a special meeting of stockholders of Vital Living and the absence of a material adverse effect on the assets between the date of the agreement and the closing date. NutraCea anticipates that Vital Living will prepare and file with the SEC a proxy statement relating to the transaction. NutraCea expects that the transaction will close in the third quarter of 2008, although the actual timing of the closing will depend on many factors including preparation of the proxy statement and the SEC's review of the proxy statement, and the closing may occur later than the second quarter of 2008.

16

The Purchase Agreement contains customary representations and warranties of the parties, covenants, closing conditions, and certain termination rights for both NutraCea and Vital Living, and further provides that, upon termination of the Purchase Agreement under specified circumstances, Vital Living may be required to pay NutraCea a termination fee.

Our accounting for the purchase of these securities of VLI qualifies as a Variable Interest Entity ("VIE") in accordance with FIN 46R. As the primary beneficiary, we have consolidated VLI into the Financial Statements.

The purchase price allocated to the assets and liabilities in April 2007 is as follows:

| Assets | | |
|---|---|---|
| Cash | $ | 83,000 |
| Accounts receivable | | 1,017,000 |
| Inventory | | 30,000 |
| Property and equipment | | 15,000 |
| Other assets | | 15,000 |
| Goodwill | | 6,278,000 |
| Total Assets | | 7,438,000 |
| Liabilities | | |
| Accounts payable | | 737,000 |
| Accrued liabilities | | 725,000 |
| Notes payable | | 750,000 |
| Total Liabilities | | 2,212,000 |
| Net assets acquired | $ | 5,226,000 |

We have included in our balance sheet at March 31, 2008 the financial position of VLI as of the period ended March 31, 2008, and VLI's results of operations for the three months ended March 31, 2008 in our statement of operations for the three months ended March 31, 2008, while eliminating inter-company balances. The effect on our consolidated, condensed balance sheet at March 31, 2008 was a decrease in total assets of $1,015,000, an increase in total liabilities of $1,480,000 and a decrease in shareholder equity of $2,495,000. The effect on our consolidated income statement for the three month period was an increase in revenues of $440,000, an increase in cost of goods sold of $292,000, an increase in operating expenses of $10,000, and an increase in net income of $139,000.

*Rice RX LLC*

In December 2007 we formed Rice Rx LLC ("RRX"), a Delaware LLC, with Herbal Science Singapore PTe. Ltd. ("HS"), a Singapore corporation. We formed RRX with HS to obtain and commercialize certain patentable pharmaceutical license rights from HS. NutraCea, Inc. and HS each have a 50% interest in RRX.

Commencing in July 2008, if and to the extent the members determine that capital contributions are necessary, each member agrees to contribute capital of up to $150,000.

In conjunction with the formation of RRX, NutraCea, Inc. sold to HS, for $300,000 an exclusive license to develop, manufacture and sell certain SRB isolates and identify and commercialize certain patentable pharmaceuticals. Payment for this license was made in the form of $150,000 cash and the execution of a promissory note payable to NutraCea for $150,000 at the Bank of America prime rate of interest and due in December 2008.

Our investment in RRX is accounted for under the equity method of accounting. As of March 31, 2008 no capital contributions had been made, and RRX had no operations, expenses or income.

17

**11. NOTES PAYABLE**

In October 2007, we executed a promissory note in favor of the lessor of our new West Sacramento warehouse for $105,000 at 8% due over four years in payments of $2,572 per month for the build-out of tenant improvements. At March 31, 2008 the short-term portion of this note was approximately $24,000 and the remaining long-term portion was approximately $71,000.

In March 2008, we purchased a building in Phoenix, AZ for $8,412,000, giving $4,012,000 in cash and executing a 90 day note payable due in June 2008, for $4,400,000 bearing interest at 8%. The Company is attempting to re-finance this note with a secured real estate loan before the note becomes due.

**12. RELATED PARTY TRANSACTIONS**

Medan, LLC

In March 2008, our wholly owned subsidiary Medan, LLC purchased 9,700 shares of PIN (see Note 10) from FFOL for $8,175,000. A principle of FFOL, Agus Irawan is also a former director of PIN and a principle officer and shareholder of PAHL

Vital Living, Inc.

In conjunction with our purchase of certain securities of VLI (Note 10), we have begun consolidating VLI financial results into our financial results. Additionally, during fiscal 2007, we entered into a business relationship with Wellness Watchers Global, LLC (“WWG”) a customer that is also the major customer of VLI. The CEO of VLI is also a principal member of WWG. During the year ended December 31, 2007, we recorded sales of $2,460,000 to WWG. In the three months ended March 31, 2008 we recorded $192,000 of sales to WWG. At March 31, 2008 we had $1,440,000 due from this customer included in our accounts receivable of $2,785,000 (net of allowance for doubtful accounts). As of March 31, 2008 the CEO of VLI has advanced VLI $462,000 of short-term, non-interest bearing loans which are included in the liabilities of VLI. In our consolidated balance sheet we have offset the $462,000 due to VLI’s CEO by VLI against accounts receivable due VLI from WWG.

**13. COMMITMENTS AND CONTINGENCIES**

Medan, LLC

Pursuant to the formation of our subsidiary Medan, LLC (see Note 10) we expect to purchase an additional 3,050 shares of PIN for $2,500,000, during the second quarter of 2008, after certain governmental approvals are obtained,. Further, we expect to spend up to $25,000,000 (with a like amount contributed by PIN’s 49% minority investor) during the next 18 months to build a wheat mill incorporating our wheat stabilization equipment.

Purchase of customer list

During the second quarter of 2008 we expect to complete the purchase of a customer list from one of our rice mill suppliers for $3,000,000. The closing of this transaction will result in a new book of business and immediate purchase orders for NutraCea’s stabilized rice bran products, as well as new and direct sales relationships with a number of significant sized U.S. corporations.

Contractual Obligations

We lease corporate office space in Phoenix, AZ; warehouse facilities in Sacramento, California; property for our production facilities in Lake Charles, Louisiana and Freeport Texas, and a small office in Burley, Idaho. Future amounts due under these leases at March 31, 2008 are included in the following table:

| | |
|---|---|
| Fiscal Year 2008 | 1,219,000 |
| Fiscal Year 2009 | 1,614,000 |
| Fiscal Year 2010 | 1,609,000 |
| Fiscal Year 2011 | 1,583,000 |
| Fiscal Year 2012 | 1,478,000 |
| Fiscal Year 2013 | 1,478,000 |
| Thereafter | 3,193,000 |
| Total | $ 12,174,000 |

Total rent expense for the three months ended March 31, 2008 and 2007 was $410,000 and $27,000, respectively.

**14. BUSINESS SEGMENTS**

We operate in two business segments; NutraCea, which manufactures and distributes nutritional supplements primarily derived from SRB" (operating results from VLI are included in our NutraCea segment), and Irgovel, our rice-bran oil manufacturing subsidiary in Pelotas, Brazil. Operating results for the three months ended March 31, 2008 (the period for Irgovel is from February 19, 2008 through March 31, 2008) and summary financial information as of March 31, 2008 for the segments are presented in the following table:

| Operating Results | | **NutraCea** | | **Irgovel** |
|---|---|---|---|---|
| Net revenues | $ | 2,874,000 | $ | 2,237,000 |
| Total cost of sales | | 3,195,000 | | 1,599,000 |
| Gross Margin | | (321,000) | | 638,000 |
| | | | | |
| Operating expenses | | 6,877,000 | | 523,000 |
| Net (loss) income from operations | | (7,198,000) | | 115,000 |
| | | | | |
| Other income (expense), net | | 483,000 | | (115,000) |
| Net (loss) income before taxes | $ | (6,715,000) | $ | - |
| | | | | |
| Summary Financial Information | | | | |
| Total assets | $ | 111,900,000 | $ | 24,190,000 |

**15. STOCKHOLDERS EQUITY**

Common Stock

During the three months ended March 31, 2008:

Fourteen security holders exercised options or warrants and received a total of 1,483,282 shares of common stock for an aggregate purchase price of $685,566.

Options and Warrants

During the three months ended March 31, 2008:

We issued to ten employees options to purchase a total of 1,797,000 shares of common stock with vesting periods ranging from immediately to three years. The options expire in five years and have exercise prices per share ranging from $1.18 to $1.49.

We issued an option to purchase 100,000 shares of common stock to each of our six non-employee directors. The options vest monthly over twelve months, expire in five years, and have exercise prices per share of $1.49.

We issued to three consultants warrants to purchase a total of 1,200,000 shares of common stock with vesting periods ranging from immediately to five years or contingent upon certain performance criteria. The warrants expiration date ranges from two to eight years and have exercise prices from $1.21 to $2.50.

The expense for stock options and warrants issued to consultants and employees are calculated at fair value using the Black-Scholes valuation method.

**16. SUBSEQUENT EVENTS**

April 2008 Private Placement

In April 2008 we issued in a registered offering common stock and warrants for aggregate gross proceeds of approximately $20,000,000 ($18,775,000 after offering expenses). We issued an aggregate of 22,222,223 shares of common stock and warrants to purchase an aggregate of 6,666,664 shares of our common stock combined in “units” at a price of $0.90 per unit. Each unit consists of one share of Nutracea common stock and a five year warrant to purchase 0.3 of a share of NutraCea common stock at an exercise price of $1.20 per share. An advisor for the financing received a customary 6% cash fee based on aggregate proceeds received from the investors, reasonable expenses, and a five year warrant to purchase 1,333,333 shares of our common stock at an exercise price of $1.20. The fair value of these warrants to purchase 7,999,997 shares of common stock using the Black-Scholes method is approximately $3,102,000. If the warrants issued to the investors and the financial advisor are exercised in full, we would receive approximately $9,600,000.

**17. IMPLEMENTATION OF RECENT ACCOUNTING PRONOUNCEMENTS**

During the three months ended March 31, 2008, we implemented the following new accounting policies;

*Fair Value Measurements*

In September 2006, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 157, “Fair Value Measurements” (“SFAS No. 157”). SFAS No. 157 provides guidance for using fair value to measure assets and liabilities. It also responds to investors’ requests for expanded information about the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair valued measurements on earnings. SFAS No. 157 applies whenever standards require (or permit) assets or liabilities to be measured at fair value, and does not expand the use of fair value in any new circumstances. SFAS No. 157 is effective for financial assets and liabilities in financial statements issued for fiscal years beginning after November 15, 2007.

The Company adopted this statement for financial assets and liabilities measured at fair value effective January 1, 2008. There was no financial statement impact as a result of adoption. In accordance with the guidance of FASB Staff

Position No. 157-2, the Company has postponed adoption of the standard for non-financial assets and liabilities that are measured at fair value on a non-recurring basis, until the fiscal year beginning after November 15, 2008. The adoption of FAS 157 did not have a material impact on the Company's fair value measurements. The provisions of FAS 157 have not been applied to non-financial assets and non-financial liabilities.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities—Including an amendment of FASB Statement No. 115" ("FAS 159"). FAS 159 permits companies to measure many financial instruments and certain other items at fair value. The Company adopted FAS 159 in the first quarter of 2008; as the Company did not apply the fair value option to any of its outstanding instruments, FAS 159 did not have an impact on the Company's consolidated financial statements.

Recent Accounting Pronouncements

*Business Combinations and Non-controlling Interests*

In December 2007, the FASB released FAS 141R, *"Business Combinations"* and FAS 160, *"Non-controlling Interests in Consolidated Financial Statements."* Both standards will be effective for transactions that occur after January 1, 2009.

FAS 141R applies to all business combinations and will require the acquiring entity to recognize the assets and liabilities acquired at their respective fair value. This standard changes the accounting for business combinations in several areas. If we complete an acquisition after the effective date of FAS 141R, some of these changes could result in increased volatility in our results of operations and financial position. For example, transaction costs, which are currently capitalized in a business combination, will be expensed as incurred. Additionally, pre-acquisition contingencies (such as in-process lawsuits acquired) and contingent consideration (such as additional consideration contingent on specified events in the future) will be recorded at fair value at the acquisition date, with subsequent changes in fair value reflected in our results of operations. Under current accounting guidance, adjustments to these contingencies are reflected in the allocation of purchase price if they occur within a certain period of time after the acquisition date.

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

NutraCea is a health-science company focused on the development and distribution of products based upon the use of stabilized rice bran and proprietary rice bran formulations. Rice bran is the outer layer of brown rice which until recently was a wasted by-product of the commercial rice industry. These products include food supplements and medical foods which provide health benefits for humans and animals (known as "nutraceuticals") as well as cosmetics and beauty aids based on stabilized rice bran, rice bran derivatives and the rice bran oils. In February 2008, we acquired 100% of Irgovel in Pelotas, Brazil (see Note 10 to our consolidated financial statements contained herein), which operates a rice-bran oil manufacturing plant. Rice bran oil is a natural addition to NutraCea's portfolio of value added products derived from rice bran. A co-product of rice bran oil is defatted rice bran that is widely used in animal feeding and has great potential as a food ingredient in products where larger amounts of oil are less desirable." Beginning with this acquisition we treat our stabilized rice bran business as a separate segment from our rice-bran oil business for reporting purposes.

The following is a discussion of the consolidated financial condition of our results of operations for the three months ended March 31, 2008 and 2007 including the results of operations of our Irgovel subsidiary for the period from February 19 through March 31, 2008 (see Note 14 for a summary of operating results by business segment).

**THREE MONTHS ENDED MARCH 31, 2008 AND 2007**

For the three months ended March 31, 2008, the Company's net loss was ($6,752,000), or ($0.05) per share, compared to ($247,000) or $0.00 per share, in the same period of 2007, an increase of $6,505,000. The increased net loss for the quarter was primarily due to a an increase of $4,527,000 in operating expenses, and a net decrease in other income and expenses (net) of $1,378,000.

Our consolidated net revenues for the three months ended March 31, 2008 of $5,111,000 increased $3,114,000 from the $1,997,000 consolidated revenues recorded in the same period last year. The increase is comprised of a $860,000 increase in product sales, a $17,000 increase in royalty revenues, and $2,237,000 of sales from our subsidiary, Irgovel, for the period from February 19, 2008 through March 31, 2008.

Gross margins on product sales in the three months ended March 31, 2008 were $317,000, or 6% compared to $884,000, or 44%, a decrease of $567,000 compared to the same period last year. Gross margins on our various product lines vary widely and the gross margins are impacted from period to period by sales mix and utilization of production capacity. Our investment in production capacity during 2007 has increased our fixed operating costs in our NutraCea segment by approximately $750,000 per quarter. Additionally, during the first quarter of 2008 our NutraCea segment operated at 49% capacity due to difficulties in obtaining adequate quantities of useable rice bran. The combination of increased fixed costs and under-utilization of production capacity contributed to the increase in cost of goods sold in our NutraCea segment from 56% to 93% for the quarter ending March 31, 2008. Also, during the three months ended March 31, 2008 we recorded a charge to cost of goods of $515,000 on our NutraCea segment relating to a credit to a customer to reimburse them for products purchased by them during 2007 ultimately determined by the customer to not meet their specifications. This credit relates to a specialty product made for this customer only and is the only significant warranty cost that we have absorbed. We know of no other product warranty contingencies. The following table illustrates the contribution by each of our segments during the three months ended:

| | March 31, 2008 | | | | | | March 31, 2007 | |
|---|---|---|---|---|---|---|---|---|
| | **Consolidated** | % | **NutraCea** | % | **Irgovel** | % | **NutraCea** | % |
| Net revenues | $ 5,111,000 | 100 | $ 2,874,000 | 100 | $ 2,237,000 | 100 | $ 1,997,000 | 100 |
| Cost of sales | | | | | | | | |
| Cost of goods sold | 4,279,000 | 84 | 2,680,000 | 93 | 1,599,000 | 72 | 1,113,000 | 56 |
| Product warranty cost | 515,000 | 10 | 515,000 | 18 | - | - | - | |

| | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Total cost of sales | | 4,794,000 | 94 | | 3,195,000 | 111 | | 1,599,000 | 71 | | 1,113,000 | 56 |
| Gross Margin | $ | 317,000 | 06 | $ | (321,000) | (10) | $ | 638,000 | 28 | $ | 884,000 | 44 |

22

Research and Development ("R&D") expenses increased $143,000 for the quarter ended March 31, 2008 to $264,000 from $121,000 for the quarter ended March 31, 2007. The increase was attributed to higher product development costs and employee related expenses due to increased R&D activities and expanded scientific staff compared to the same period last year. The Company expects to continue research and development expenditures to establish the scientific basis for health claims of existing products and to develop new products and applications.

Sales, General and Administrative ("SG&A") expenses were $5,178,000 and $2,293,000 in the three months ended March 31, 2008 and 2007, respectively, an increase of $2,885,000, or 126%. This increase is predominately due to expanded investment in personnel, infrastructure, and sales and marketing activities to meet anticipated future demands (except as noted below). Specific changes in SG&A expense is detailed in the following schedule:

| | Three Months Ended March 31, 2008 | Three Months Ended March 31, 2007 | Increase / Decrease |
|---|---|---|---|
| Payroll | $ 1,482,000 | $ 784,000 | $ 698,000 |
| Employee benefits, payroll taxes, and hiring expenses | 225,000 | 282,000 | (57,000) |
| Sales and marketing | 473,000 | 257,000 | 216,000 |
| Allowance for bad debt expense, net | 390,000 | - | 390,000 |
| Operations | 367,000 | 145,000 | 222,000 |
| Travel and entertainment | 350,000 | 120,000 | 230,000 |
| Rent and facility costs | 410,000 | 27,000 | 383,000 |
| Stock based compensation (net of amounts applied to R&D and professional fees) | 620,000 | 353,000 | 267,000 |
| Amortization | 209,000 | 30,000 | 179,000 |
| Depreciation , net of allocation to cost of goods sold | 277,000 | 100,000 | 177,000 |
| Administration, insurance, and other | 375,000 | 195,000 | 180,000 |
| Total selling, general and administrative expenses | $ 5,178,000 | $ 2,293,000 | $ 2,885,000 |

In the three months ended March 31, 2008 our provision for the allowance for bad debt expense was $390,000 compared to $0 in the three months ended March 31, 2007. This increase is the result of a $292,000 additional provision for a doubtful note receivable, an additional charge of $72,000 for doubtful accounts receivable and $26,000 of specific charge offs of accounts receivable.

Professional fees increased $1,499,000 from $459,000 for the three months ended March 31, 2007 to $1,958,000 for the three months ended March 31, 2008. The higher professional fees in 2008 primarily relate to consulting and legal fees incurred in connection with marketing and business development activities, Sarbanes-Oxley Section 404 activities, the acquisition of our subsidiary Irgovel, and our investment in PIN made through our Medan LLC subsidiary. During the quarter end March 31, 2008 we accrued a charge of $750,000 for a broker fee and the estimated value of an option to be issued relating to our investment in PIN (see Note 10 to our consolidated financial statements contained herein). The following table lists the increases in each of the professional fees accounts for the three month periods ended:

| | March 31, 2008 | March 31, 2007 | Increase/Decrease |
|---|---|---|---|
| Legal | $ 479,000 | $ 83,000 | $ 396,000 |
| Accounting | 445,000 | 256,000 | 189,000 |
| Other consulting fees | 142,000 | 45,000 | 97,000 |
| Broker and commission fees | 750,000 | - | 750,000 |

| | | | |
|---|---|---|---|
| Shareholder relations | 142,000 | 75,000 | 67,000 |
| Total selling, general and administrative expenses | $ 1,958,000 | $ 459,000 | $ 1,499,000 |

23

Other income and expense, net, decreased by $1,394,000 in the three months ended March 31, 2008 compared to 2007. This decrease is due primarily to the $1,250,000 gain on a settlement in the three months ended March 31, 2007, a decrease of $252,000 in interest income due to lower cash balances, $120,000 of interest expense incurred by our subsidiary Irgovel, and an increase of $245,000 of other income primarily from the collection of late fees and penalty interest on past due accounts and notes receivable.

During the first quarter of 2008, and anticipated to continue through the second quarter of 2008, the Company has aggressively built inventory levels, and has leased additional warehouse space in order to have sufficient minimum supply requirements in anticipation of increases in planned sales to new and existing customers based on new product roll outs and existing product customer needs anticipated to commence in the second half of 2008.

**LIQUIDITY AND CAPITAL RESOURCES**

As of March 31, 2008, our source of liquidity was cash in the amount of $5,816,000. Our cash decreased by $35,482,000 in the three months ended March 31, 2008 from our cash position of $41,298,000 at December 31, 2007. The decrease in cash was primarily due to our $15,049,000 investment in Irgovel, the purchase of property, plant, and equipment of $8,128,000 and our purchase of 44% of PIN (see Note 10 to our consolidated financial statements contained herein) for $8,175,000.

On April 1, 2008 we received $5,000,000 from PAHL in payment of the note receivable entered into in June 2007 for the sale to PAHL of licensing rights. Originally due over five year terms the receivable agreement was modified in January 2008 to allow for the forgiveness of accrued interest on the note if the full principal was paid by March 31, 2008. As the payment was in transit on that date the company agreed to honor the forgiveness of interest due thru March 31, 2008 of approximately $175,000.

For the first three months of 2008, net cash used in operations was $813,000, compared to cash used in operations in the same period of 2007 of $1,841,000, a decrease of $1,028,000. This decrease in cash used in operations resulted primarily from the increase in our net loss of $6,752,000, plus the increase in inventories of $497,000 offset by the increase in non-cash charges against income of; $450,000 for depreciation and amortization, $368,000 in the provision for doubtful accounts and notes receivable, $362,000 for stock-based compensation, $270,000 for deferred income, a $17,000 charge for the equity loss on our joint venture, the $84,000 increase in accounts receivable, an increase of $1,353,000 in other current assets, an increase of $5,003,000 in accounts payable and accrued liabilities, and $123,000 in other non-current liabilities.

Cash used in investing activities in the first three months of 2008 was $35,397,000, compared to $2,064,000 for the same period of 2007. This increase of $33,333,000 was primarily caused by our $14,970,000 (net of $79,000 cash acquired with the purchase) investment in Irgovel (see Note 10 in our consolidated financial statements contained herein), an increase of $5,772,000 in expenditures for plant expansions and other fixed assets, our $8,175,000 investment in PIN (see Note 10), an increase of $4,523,000 in restricted cash, and $72,000 for the purchase of other assets.

Cash provided by financing activities for the first three months ended March 31, 2008, was approximately $617,000, which reflects proceeds received upon the exercise of common stock options and warrants less $61,000 for stock registration costs and payments on notes payable of $7,000. This decrease of $50,190,000 is primarily due to the $3,245,000 decrease in funds provided from the exercise of common stock options and warrants and the $46,877,000 received in a private placement financing in February 2007.

In April 2008 we issued in a registered offering, common stock and warrants for aggregate gross proceeds of approximately $20,000,000 ($18,775,000 after offering expenses). We issued an aggregate of 22,222,223 shares of common stock and warrants to purchase an aggregate of 6,666,664 shares of our common stock combined in “units” at a

price of $0.90 per unit. Each unit consists of one share of Nutracea common stock and a five year warrant to purchase 0.3 of a share of NutraCea common stock at an exercise price of $1.20 per share. An advisor for the financing received a customary 6% cash fee, base on aggregate gross proceeds received from the investors, reasonable expenses and a warrant to purchase 1,333,333 shares of our common stock at an exercise price of $1.20. The fair value of these warrants to purchase 7,999,997 shares of common stock using the Black-Scholes method is approximately $3,102,000. If exercised, the company would receive approximately $9,600,000.

On February 15, 2007, we sold an aggregate of 20,000,000 shares of our common stock at a price of $2.50 per share in connection with a private placement for aggregate gross proceeds of $50,000,000 ($46,805,000 after offering expenses). Additionally, the investors were issued warrants to purchase an aggregate of 10,000,000 shares of our common stock at an exercise price of $3.25 per share. An advisor for the financing received a customary 6% cash-fee, based on aggregate gross proceeds received from the investors, reasonable expenses and a warrant to purchase 1,200,000 shares of common stock at an exercise price per share of $3.25. The warrants have a term of five years and are exercisable after August 16, 2007.

We believe we have sufficient cash reserves to meet all anticipated short-term operating requirements.

**OFF BALANCE SHEET ARANGEMENTS**

We have not entered into any transactions with unconsolidated entities whereby we have financial guarantees, subordinated retained interests, derivative instruments or other contingent arrangements that expose us to material continuing risk, contingent liabilities, or any other obligation under a variable interest in an unconsolidated entity that provides financing and liquidity support or market risk or credit risk support to the Company.

**CRITICAL ACCOUNTING POLICIES**

Our discussion and analysis of our financial condition and results of operations are based upon unaudited consolidated condensed financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses and disclosures on the date of the financial statements. On an ongoing basis, we evaluate the estimates, including, but not limited to, those related to revenue recognition. We use authoritative pronouncements, historical experience and other assumptions as the basis for making judgments. Actual results could differ from those estimates.

For further information about other critical accounting policies, see the discussion of critical accounting policies in our 2007 Form 10-K for the fiscal year ended December 31, 2007.

***Adoption of recent accounting pronouncements***

*Fair Value Measurements*

In September 2006, the Financial Accounting Standards Board (“FASB”) issued Statement of Financial Accounting Standards No. 157, “Fair Value Measurements” (“SFAS No. 157”). SFAS No. 157 provides guidance for using fair value to measure assets and liabilities. It also responds to investors’ request for expanded information about the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair valued measurements on earnings. SFAS No. 157 applies whenever standards require (or permit) assets or liabilities to be measured at fair value, and does not expand the use of fair value in any new circumstances. SFAS No. 157 is effective for financial assets and liabilities in financial statements issued for fiscal years beginning after November 15, 2007.

The Company adopted this statement for financial assets and liabilities measured at fair value effective January 1, 2008. There was no financial statement impact as a result of adoption. In accordance with the guidance of FASB Staff Position No. 157-2, the Company has postponed adoption of the standard for non-financial assets and liabilities that are measured at fair value on a non-recurring basis, until the fiscal year beginning after November 15, 2008. The adoption of FAS 157 did not have a material impact on the Company’s fair value measurements. The provisions of FAS 157 have not been applied to non-financial assets and non-financial liabilities.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities—Including an amendment of FASB Statement No. 115" ("FAS 159"). FAS 159 permits companies to measure many financial instruments and certain other items at fair value. The Company adopted FAS 159 in the first quarter of 2008; as the Company did not apply the fair value option to any of its outstanding instruments, FAS 159 did not have an impact on the Company's consolidated financial statements.

*Recent accounting pronouncements*

*Business Combinations and Non-controlling Interests*

In December 2007, the FASB released FAS 141R, *"Business Combinations"* and FAS 160, *"Non-controlling Interests in Consolidated Financial Statements."* Both standards will be effective for transactions that occur after January 1, 2009.

FAS 141R applies to all business combinations and will require the acquiring entity to recognize the assets and liabilities acquired at their respective fair value. This standard changes the accounting for business combinations in several areas. If we complete an acquisition after the effective date of FAS 141R, some of these changes could result in increased volatility in our results of operations and financial position. For example, transaction costs, which are currently capitalized in a business combination, will be expensed as incurred. Additionally, pre-acquisition contingencies (such as in-process lawsuits acquired) and contingent consideration (such as additional consideration contingent on specified events in the future) will be recorded at fair value at the acquisition date, with subsequent changes in fair value reflected in our results of operations. Under current accounting guidance, adjustments to these contingencies are reflected in the allocation of purchase price if they occur within a certain period of time after the acquisition date.

**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

Our cash and cash equivalents have been maintained only with maturities of 30 days or less. Our short-term investments have interest reset periods of 30 days or less. These financial instruments may be subject to interest rate risk through lost income should interest rates increase during their limited term to maturity or resetting of interest rates. As of March 31, 2008, we had approximately $71,000 of long-term debt bearing interest at 8%. Future borrowings, if any, would bear interest at negotiated rates and would be subject to interest rate risk. We do not believe that a hypothetical adverse change of 10% in interest rates would have a material effect on our financial position.

**Item 4. Controls and Procedures**

Disclosure Controls and Procedures

We carried out an evaluation, under the supervision and with the participation of management, including our chief executive officer and chief financial officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this quarterly report. Based upon that evaluation, our chief executive officer and our chief financial officer concluded that, as of March 31, 2008, our disclosure controls and procedures were effective to ensure that information we are required to disclose by NutraCea in reports that we file or submit under the Securities and Exchange Act of 1934, as amended, is accumulated and communicated to our management, including our principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure, and that such information is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

Changes in Internal Control Over Financial Reporting

As described more fully in our Annual Report on Form 10-K for the year ended December 31, 2007, our management determined that as of December 31, 2007 we had the following material weaknesses in our internal control over financial reporting:

1. Our procedures for hiring third-party financial and valuation experts are inadequate. We have a written policy relating to the hiring of third-party financial experts, however, we believe we need to revise this policy to (i) lower

the transaction dollar threshold before we need to report to, and seek the approval of, our Board of Directors regarding the qualifications and hiring of financial experts and (ii) require the same approval from the Board of Directors for the engagement of valuation experts as we will require for the hiring of financial experts.

2. We do not have adequate procedures to assure that significant and complex transactions are timely analyzed and reviewed. As a result, significant adjustments to the results of operations have been required at year-end and at the end of last three quarters of 2007 prior to filing our 10-K and 10-Qs for 2007, including adjustments relating to revenue recognition, valuation of certain receivables, classification of settlement expenses and goodwill impairment.

To address and remediate these material weaknesses, we implemented the following changes to our internal controls over financial reporting during the period covered by this report:

For the material weakness concerning retention of experts, we have developed the following remediation plan:

1. We have developed a written policy and procedures that document the processes relating to retention of expert service providers for assistance with valuations and significant financial transactions of NutraCea. Included in the process is an analysis to verify and document the extent of any past relationships with the service providers and to confirm the lack of apparent conflicts of interest. Since December 31, 2007, we have revised these procedures as follows:

- For transactions or valuations with aggregate amounts ranging from two to five percent of net equity (“Reporting Threshold”), management will report to the Board of Directors the retention and qualifications of selected experts.
- For transactions or valuations with aggregate values greater than five percent of net equity (“Approval Threshold”), management will report to the Board of Directors its recommendation for the retention of experts and seek approval to retain expert service providers.

Our expert retention policy in effect as of December 31, 2007 (i) did not apply to the engagement of experts for the purpose of providing valuation and (ii) maintained a Reporting Threshold of five to ten percent of net equity and an Approval Threshold of over ten percent.

2. For the material weakness concerning performing timely, comprehensive review of financial transactions, we have developed the following remediation plan that will enhance our current policies and procedures:

- Assess and evaluate the Chief Executive Officer’s authorization thresholds to enter into agreements that has been delegated by the Board of Directors and make appropriate recommendations. Additionally, we recommended that the Board of Directors expand its documentation requirements and receive analysis from our Chief Financial Officer and Chief Operating Officer when reviewing proposed transactions.
- Continue to enhance and improve month-end and quarter-end closing procedures by having reviewers analyze and monitor financial information in a consistent and thorough manner. We plan to continue to enhance and improve the documentation and review of required information associated with the preparation of our quarterly and annual filings.
- Perform SAB 104 analysis of significant revenue transactions in excess of $100,000 per customer per quarter, or over $250,000 in any one year to assess if collectability is reasonable assured and to ensure proper period revenue recognition.
- Prepare accounting memos within twenty days after the end of each quarter analyzing our allowance for doubtful accounts for all accounts receivable that exceed ten percent of our total accounts receivable.
- Prepare accounting memos to summarize all significant transactions and the accounting treatment therefore within forty days after the completion of such transactions..

Other than the items identified above, during the quarter covered by this report, there was no change in NutraCea’s internal control over financial reporting that has materially affected, or is reasonably likely to materially effect, the Company’s internal control over financial reporting.

27

**PART 2. OTHER INFORMATION**

**Item 1. Legal Proceedings**

From time to time we are involved in litigation incidental to the conduct of our business. While the outcome of lawsuits and other proceedings against us cannot be predicted with certainty, in the opinion of management, individually or in the aggregate, no such lawsuits are expected to have a material effect on our financial position or results of operations.

**Item 1A. Risk Factors**

Investors or potential investors in our stock should carefully consider the risks described below. Our stock price will reflect the performance of our business relative to, among other things, our competition, expectations of securities analysts or investors, and general economic market conditions and industry conditions. One should carefully consider the following factors in connection with any investment in our stock. Our business, financial condition and results of operations could be materially adversely affected if any of the following risks occur. Should any or all of the following risks materialize, the trading price of our stock could decline, and investors could lose all or part of their investment.

**Risks Related to Our Business**

***We have a limited operating history and have generated*** **losses in the first quarter of 2008 and for each year other than 2006.**

We began operations in February 2000 and incurred losses in each reporting period other than the second, third, and fourth quarters of 2006 and the second quarter of 2007. Our prospects for financial success are difficult to forecast because we have a relatively limited operating history. Our prospects for financial success must be considered in light of the risks, expenses and difficulties frequently encountered by companies in new, unproven and rapidly evolving markets. Our business could be subject to any or all of the problems, expenses, delays and risks inherent in the establishment of a new business enterprise, including limited capital resources, possible delays in product development, possible cost overruns due to price and cost increases in raw product and manufacturing processes, uncertain market acceptance, and inability to respond effectively to competitive developments and attract, retain and motivate qualified employees. Therefore, there can be no assurance that our business or products will be successful, that we will be able to achieve or maintain profitable operations or that we will not encounter unforeseen difficulties that may deplete our capital resources more rapidly than anticipated.

***There are significant market risks associated with our business.***

We have formulated our business plan and strategies based on certain assumptions regarding the size of the rice bran market, our anticipated share of this market, and the estimated price and acceptance of our products. These assumptions are based on the best estimates of our management; however, there can be no assurance that our assessments regarding market size, potential market share attainable by us, the price at which we will be able to sell our products, market acceptance of our products, or a variety of other factors will prove to be correct. Any future success may depend upon factors including changes in the dietary supplement industry, governmental regulation, increased levels of competition, including the entry of additional competitors, increased success by existing competitors, changes in general economic conditions, increases in operating costs including costs of production, supplies, personnel, equipment, and reduced margins caused by competitive pressures.

***We may face difficulties integrating businesses that we acquire.***

As part of our strategy, we expect to review opportunities to buy other businesses or technologies that would complement our current products, expand the breadth of our markets or enhance technical capabilities, or that may otherwise offer growth opportunities. In the event of any future acquisitions, we could:

- issue stock that would dilute current shareholders' percentage ownership;
- incur debt; or
- assume liabilities.

These purchases also involve numerous risks, including:

- problems combining the purchased operations, technologies or products;
- unanticipated costs;
- diversion of management's attention from our core business;
- adverse effects on existing business relationships with suppliers and customers;
- risks associated with entering markets in which we have no or limited prior experience; and
- potential loss of key employees of purchased organizations.

We cannot assure you that we will be able to successfully integrate any businesses, products, technologies or personnel that we might purchase in the future.

***We depend on limited number of customers.***

During 2007, we received approximately 51% of product sales revenue from six customers and approximately 15% of our revenue from one customer. During the three months ended March 31, 2008, two customers accounted for 16% of our sales. A loss of any of these customers could have a material adverse effect on our revenues and results of operations.

***The inability of our significant customers to meet their obligations to us may adversely affect our financial results.***

We are subject to credit risk due to concentration of our trade accounts receivables and notes receivables. As of March 31, 2008, two customers accounted for 51% of our $8,857,000 trade accounts receivable and four debtors accounted for 96% of $7,189,000 notes receivables reflected on our March 31, 2008 balance sheet. In addition, we acquired secured promissory notes of Vital Living, Inc. with aggregate principal amounts of $4,226,000 in connection with our entering into an asset purchase agreement with Vital Living to acquire Vital Living's assets. While we obtain personal guarantees and security interests backing these obligations when possible, many of these obligations are not guaranteed or secured. The inability of our significant customers and obligors to meet their obligations to us, or, in the case of Vital Living, the deterioration of Vital Living's financial condition or assets before we are able to consummate our asset purchase, may adversely affect our financial condition and results of operations.

***We rely upon a limited number of product offerings.***

The majority of our products are based on stabilized rice bran. Although we will market stabilized rice bran as a dietary supplement, as an active food ingredient for inclusion in our products and in other companies' products, and in other ways, a decline in the market demand for our products, as well as the products of other companies utilizing our products, could have a significant adverse impact on us.

***We are dependent upon our marketing efforts.***

We are dependent on our ability to market products to animal food producers, food manufacturers, mass merchandise and health food retailers, and to other companies for use in their products. We must increase the level of awareness of dietary supplements in general and our products in particular. We will be required to devote substantial management and financial resources to these marketing and advertising efforts and there can be no assurance that it will be successful.

***We rely upon an adequate supply of raw rice bran.***

The majority of our current products depend on our proprietary technology using unstabilized or raw rice bran, which is a by-product from milling paddy rice to white rice. Our ability to manufacture stabilized rice bran raw is currently limited to the production capability of our production equipment at Farmers' Rice Co-operative ("FRC") and Archer Daniels Midland ("ADM"), our own plants located next to the Louisiana Rice Mill in Mermentau, Louisiana and American Rice, Inc. in Freeport, Texas, and our single value-added products plant in Dillon, Montana. We currently are capable of producing enough finished products at our facilities to meet current demand. With the exception of our newly acquired rice bran oil facility in Pelotas, Brazil, our existing plants do not allow for dramatic expansion , therefore additional domestic production capacity will be needed if demand increases. While we believe our facilities should meet our production needs for 2008, we do not anticipate that they will meet our longer term supply needs. Therefore, we anticipate building new facilities to meet the forecasted demand for our products and envision we will be able to execute on this initiative. In the event we are unable to create additional production capacity to produce more stabilized rice bran products to fulfill our current and future requirements this could materially and adversely affect our business, results from operations, and financial condition.

We are pursuing other supply sources in the United States and in foreign countries and anticipate being able to secure alternatives and back-up sources of rice bran, although we have not entered into any definitive agreements other than the agreements with Farmers Rice Cooperative and Louisiana Rice Mill. However, there can be no assurance that we will continue to secure adequate sources of raw rice bran to meet our requirements to produce stabilized rice bran products. Since rice bran has a limited shelf life, the supply of rice bran is affected by the amount of rice planted and harvested each year. If economic or weather conditions adversely affect the amount of rice planted or harvested, the cost of rice bran products that we use may increase. We are not generally able to pass cost increases to our customers and any increase in the cost of stabilized rice bran products would have an adverse effect on our results of operations.

***We face risks in our wheat bran stabilization efforts.***

In January 2008, through a newly formed wholly owned subsidiary, we entered an agreement to develop and lease Wheat Bran Stabilization equipment to an Indonesian company. We cannot guarantee that our efforts to develop Wheat Bran Stabilization equipment will be successful.

***We intend to pursue significant foreign operations and there are inherent risks in operating abroad.***

An important component of our business strategy is to build rice bran stabilization facilities in foreign countries and to market and sell our products internationally. For example, we recently entered into a joint venture with an Indonesian company to produce and market our SRB products in Southeast Asia and purchased a company in Brazil that manufactures rice bran oil. There are risks in operating stabilization facilities in developing countries because, among other reasons, we may be unable to attract sufficient qualified personnel, intellectual property rights may not be enforced as we expect, power may not be available as contemplated. Should any of these risks occur, we may be unable to maximize the output from these facilities and our financial results may decrease from our anticipated levels. The inherent risks of international operations could materially adversely affect our business, financial condition and results of operations. The types of risks faced in connection with international operations and sales include, among others:

- cultural differences in the conduct of business;
- fluctuations in foreign exchange rates;
- greater difficulty in accounts receivable collection and longer collection periods;
- impact of recessions in economies outside of the United States;
- reduced protection for intellectual property rights in some countries;
- unexpected changes in regulatory requirements;
- tariffs and other trade barriers;
- political conditions in each country;
- management and operation of an enterprise spread over various countries;
- the burden and administrative costs of complying with a wide variety of foreign laws; and
- currency restrictions.

***We identified material weaknesses in our internal control over financial reporting, which could impact negatively our ability to report our results of operations and financial condition accurately and in a timely manner.***

As required by Section 404 of the Sarbanes-Oxley Act of 2002, management conducted an evaluation of the effectiveness of our internal control over financial reporting at December 31, 2007. We identified two material weaknesses in our internal control over financial reporting and concluded that, as of December 31, 2007, we did not maintain effective control over financial reporting based on criteria established in *Internal Control-Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission. For a detailed

description of these material weaknesses, see Item 4, “Controls and Procedures”, contained in this report. Each of our material weaknesses results in a reasonable possibility that a material misstatement of the annual or interim financial statements that we prepare will not be prevented or detected on a timely basis. As a result, we must perform additional work to obtain reasonable assurance regarding the reliability of our financial statements.



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If we are unsuccessful in implementing or following our remediation plan, or fail to update our internal control over financial reporting as our business evolves or to integrate acquired businesses into our controls system, we may not be able to timely or accurately report our financial condition, results of operations or cash flows or to maintain effective disclosure controls and procedures. If we are unable to report financial information in a timely and accurate manner or to maintain effective disclosure controls and procedures, we could be subject to, among other things, regulatory or enforcement actions by the SEC, securities litigation and a general loss of investor confidence, any one of which could adversely affect our business prospects and the market value of our common stock.

***We face competition.***

Competition in our targeted industries, including nutraceuticals, functional food ingredients, rice bran oils, animal feed supplements and companion pet food ingredients is vigorous, with a large number of businesses engaged in the various industries. Many of our competitors have established reputations for successfully developing and marketing their products, including products that incorporate bran from other cereal grains and other alternative ingredients that are widely recognized as providing similar benefits as rice bran. In addition, many of our competitors have greater financial, managerial, and technical resources than us. If we are not successful in competing in these markets, we may not be able to attain our business objectives.

***We* have not yet achieved positive cash flow**

We have not generated a positive cash flow from operations continuous period to period since commencing operations. We raised in private placements of equity approximately $50,000,000 in February 2007, $17,560,000 in May 2006, and $8,000,000 in October 2005. Additionally we raised in a public offering of our common stock and warrants to purchase our common stock approximately $20,000,000 in April 2008. While we believe that we have adequate cash reserves and working capital to fund current operations, our ability to meet long term business objectives may be dependent upon our ability to raise additional financing through public or private equity financings, establish increasing cash flow from operations, enter into collaborative or other arrangements with corporate sources, or secure other sources of financing to fund long-term operations. There is no assurance that external funds will be available on terms acceptable to us in sufficient amount to finance operations until we do reach sufficient positive cash flow to fund our capital expenditures. In addition, any issuance of securities to obtain such funds would dilute percentage ownership of our shareholders. Such dilution could also have an adverse impact on our earnings per share and reduce the price of our common stock. Incurring additional debt may involve restrictive covenants and increased interest costs and demand on future cash flow. Our inability to obtain sufficient financing may require us to delay, scale back or eliminate some or all of our product development and marketing programs.

***Our products could fail to meet applicable regulations which could have a material adverse affect on our financial performance.***

The dietary supplement and cosmetic industries are subject to considerable government regulation, both as to efficacy as well as labeling and advertising. There is no assurance that all of our products and marketing strategies will satisfy all of the applicable regulations of the Dietary Supplement, Health and Education Act, the Food, Drug and Cosmetic Act, the U.S. Food and Drug Administration and/or the U.S. Federal Trade Commission. Failure to meet any applicable regulations would require us to limit the production or marketing of any non-compliant products or advertising, which could subject us to financial or other penalties.

***Our success depends in part on our ability to obtain patents, licenses and other intellectual property rights for our products and technology.***

We have one patent entitled Methods for Treating Joint Inflammation, Pain and Loss of Mobility, which covers both humans and mammals. In addition, our subsidiary RiceX has five United States patents and may decide to file

corresponding international applications. RiceX holds patents to the production of Beta Glucan and to a micro nutrient enriched rice bran oil process. RiceX also holds patents to a method to treat high cholesterol, to a method to treat diabetes and to a process for producing Higher Value Fractions from stabilized rice bran. The process of seeking patent protection may be long and expensive, and there can be no assurance that patents will be issued, that we will be able to protect our technology adequately, or that competition will not be able to develop similar technology.

There currently are no claims or lawsuits pending or threatened against us or RiceX regarding possible infringement claims, but there can be no assurance that infringement claims by third parties, or claims for indemnification resulting from infringement claims, will not be asserted in the future or that such assertions, if proven to be accurate, will not have a material adverse affect on our business, financial condition and results of operations. In the future, litigation may be necessary to enforce our patents, to protect our trade secrets or know-how or to defend against claimed infringement of the rights of others and to determine the scope and validity of the proprietary rights of others. Any litigation could result in substantial cost and diversion of our efforts, which could have a material adverse affect on our financial condition and results of operations. Adverse determinations in any litigation could result in the loss of our proprietary rights, subjecting us to significant liabilities to third parties, require us to seek licenses from third parties or prevent us from manufacturing or selling our systems, any of which could have a material adverse affect on our financial condition and results of operations. There can be no assurance that a license under a third party's intellectual property rights will be available to us on reasonable terms, if at all.

***We are dependent on key employees and consultants.***

Our success depends upon the efforts of our top management team, including the efforts of Bradley D. Edson, our President and Chief Executive Officer, Todd C. Crow, our Chief Financial Officer, Leo Gingras, our Chief Operating Officer, Margie D. Adelman, our Secretary and Senior Vice President and Kody K. Newland, our Senior Vice President of Sales and Marketing. Effective May 13, 2008, our current CFO Todd Crow is resigning. Jeff Sanders becomes our CFO on May 13, 2008. Although we have written employment agreements with each of the foregoing individuals, other than Ms. Adelman, there is no assurance that such individuals will not die, become disabled, or resign. In addition, our success is dependent upon our ability to attract and retain key management persons for positions relating to the marketing and distribution of our products. There is no assurance that we will be able to recruit and employ such executives at times and on terms acceptable to us.

***Our products may require clinical trials to establish efficacy and safety.***

Certain of our products may require clinical trials to establish our benefit claims or their safety and efficacy. Such trials can require a significant amount of resources and there is no assurance that such trials will be favorable to the claims we make for our products, or that the cumulative authority established by such trials will be sufficient to support our claims. Moreover, both the findings and methodology of such trials are subject to challenge by the FDA and scientific bodies. If the findings of our trials are challenged or found to be insufficient to support our claims, additional trials may be required before such products can be marketed.

**Risks Related to Our Stock**

***Our Stock Price is Volatile.***

The market price of a share of our common stock has fluctuated significantly in the past and may continue to fluctuate significantly in the future. The high and low closing prices of a share of common stock for the following periods were:

| | High | Low |
|---|---|---|
| Three months ended March 31, 2008 | $ 1.56 | $ 0.89 |
| Twelve months ended December 31, 2007 | $ 5.00 | $ 0.75 |
| Twelve months ended December 31, 2006 | $ 2.74 | $ 0.60 |

The market price of a share of our common stock may continue to fluctuate in response to a number of factors, including:

- announcements of new products or product enhancements by us or our competitors;
- fluctuations in our quarterly or annual operating results;
- developments in our relationships with customers and suppliers;
- the loss of services of one or more of our executive officers or other key employees;
- announcements of technological innovations or new systems or enhancements used by us or our competitors;
- developments in our or our competitors intellectual property rights;
- adverse effects to our operating results due to impairment of goodwill;
- failure to meet the expectation of securities analysts' or the public; and
- general economic and market conditions.

***We have significant "equity overhang" which could adversely affect the market price of our common stock and impair our ability to raise additional capital through the sale of equity securities.***

As of May 2, 2008, 167,693,724 shares of our common stock were outstanding. Additionally, as of May 2, 2008, options and warrants to purchase approximately 50,642,963 shares of our common stock were outstanding. The possibility that substantial amounts of our outstanding common stock may be sold by investors or the perception that such sales could occur, often called "equity overhang," could adversely affect the market price of our common stock and could impair our ability to raise additional capital through the sale of equity securities in the future.

***Sales of Our Stock Pursuant to Registration Statements May Hurt Our Stock Price***

We granted registration rights to the investors in our October 2005, May 2006 and February 2007 capital stock and warrant financings. As of May 2, 2008, approximately 25,119,000 shares of our common stock remained eligible for resale pursuant to outstanding registration statements filed for these investors. In addition, we have filed a registration

statement to cover our issuance and sale of up to $125,000,000 of common stock, preferred stock, and warrants to purchase common or preferred stock. Sales or potential sales of a significant number of shares into the public markets may negatively affect our stock price.

***The Exercise of Outstanding Options and Warrants May Dilute Current Shareholders***

As of May 2, 2008, there were outstanding options and warrants to purchase approximately 50,642,963 shares of our common stock. Holders of these options and warrants may exercise them at a time when we would otherwise be able to obtain additional equity capital on terms more favorable to us. Moreover, while these options and warrants are outstanding, our ability to obtain financing on favorable terms may be adversely affected.

***We may need to raise funds through debt or equity financings in the future, which would dilute the ownership of our existing shareholders and possibly subordinate certain of their rights to the rights of new investors.***

We may choose to raise additional funds in debt or equity financings if they are available to us on terms we believe reasonable to increase our working capital, strengthen our financial position or to make acquisitions. Any sales of additional equity or convertible debt securities would result in dilution of the equity interests of our existing shareholders, which could be substantial. Additionally, if we issue shares of preferred stock or convertible debt to raise funds, the holders of those securities might be entitled to various preferential rights over the holders of our common stock, including repayment of their investment, and possibly additional amounts, before any payments could be made to holders of our common stock in connection with an acquisition of the company. Such preferred shares, if authorized, might be granted rights and preferences that would be senior to, or otherwise adversely affect, the rights and the value of our common stock. Also, new investors may require that we and certain of our shareholders enter into voting arrangements that give them additional voting control or representation on our board of directors.

***The authorization of our preferred stock may have an adverse effect on the rights of holders of our common stock.***

We may, without further action or vote by holders of our common stock, designate and issue shares of our preferred stock. The terms of any series of preferred stock could adversely affect the rights of holders of our common stock and thereby reduce the value of our common stock. The designation and issuance of preferred stock favorable to current management or shareholders could make it more difficult to gain control of our Board of Directors or remove our current management and may be used to defeat hostile bids for control which might provide shareholders with premiums for their shares.

***Compliance with corporate governance and public disclosure regulations may result in additional expenses.***

Changing laws, regulations and standards relating to corporate governance and public disclosure, including the Sarbanes-Oxley Act of 2002, and new regulations issued by the Securities and Exchange Commission, are creating uncertainty for companies. In order to comply with these laws, we may need to invest substantial resources to comply with evolving standards, and this investment would result in increased general and administrative expenses and a diversion of management time and attention from revenue-generating activities to compliance activities.

***Our officers and directors have limited liability and have indemnification rights***

Our Articles of Incorporation and by-laws provide that we may indemnify our officers and directors against losses sustained or liabilities incurred which arise from any transaction in that officer's or director's respective managerial capacity unless that officer or director violates a duty of loyalty, did not act in good faith, engaged in intentional misconduct or knowingly violated the law, approved an improper dividend, or derived an improper benefit from the transaction.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

During the quarter ended March 31 2008, NutraCea issued the following securities without registration under the Securities Act of 1933:

Common Stock

Fourteen security holders exercised options or warrants and received a total of 1,483,282 shares of common stock for an aggregate purchase price of $685,566.

Options and Warrants

We issued to ten employees options to purchase a total of 1,797,000 shares of common stock with vesting periods ranging from immediately to three years. The options expire in five years and have exercise prices per share ranging from $1.18 to $1.49.

We issued an option to purchase 100,000 shares of common stock to each of our six non-employee directors. The options vest monthly over twelve months, expire in five years, and have exercise prices per share of $1.49.

We issued to three consultants warrants to purchase a total of 1,200,000 shares of common stock with vesting periods ranging from immediately to five years or contingent upon certain performance criteria. The warrants have per share exercise prices ranging from $1.21 to $2.50 and have expiration dates from two to eight years.

All of the above issuances were made without any public solicitation to a limited number of investors, consultants, advisors, or employees, and the securities were acquired for investment purposes only. The securities were issued pursuant to the private placement exemption provided by Section 4(2) of the Securities Act of 1933.

**Item 3. Defaults Upon Senior Securities**

None

**Item 4. Submission of Matters to a Vote of Security Holders**

None

**Item 5. Other Information**

None

**Item 6. Exhibits**

The following exhibits are attached hereto and filed herewith:

| Exhibit Number | Description of Exhibit |
| --- | --- |
| 10.1 | Employment Agreement between the Company and Jeffrey Sanders. |
| 10.2 | Form of Stock Option Agreement for 2005 Equity Incentive Plan. |
| 10.3 | Form of Stock Option Agreement for Stock Options Granted to Bradley Edson, Leo Gingras and Kody Newland on January 8, 2008. |
| 10.4 | Form of Stock Option Agreement for Stock Options Granted to Todd Crow and Margie Adelman on January 8, 2008. |
| 10.5 | Form of Option Agreement for Stock Options granted to Non-Employee Directors on January 8, 2008. |
| 31.1 | Certification of Chief Executive Officer Pursuant to §302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of Chief Financial Officer Pursuant to §302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of Chief Executive Officer and Chief Financial Office Pursuant to 18 U.S.C. §1350 and §906 of the Sarbanes-Oxley Act of 2002. |

SIGNATURES

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

| | NUTRACEA |
|---|---|
| Dated: May 12, 2008 | /s/ Bradley Edson<br>Bradley Edson<br>Chief Executive Officer |
| Dated: May 12, 2008 | /s/ Todd C. Crow<br>Todd C. Crow,<br>Chief Financial Officer<br>(Principal Accounting Officer) |