NUTRACEA
Form 10-Q
November 14, 2007

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

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 September 30, 2007

o **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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Securities Exchange Act of 1934).
Large accelerated filer o Accelerated filer o Non-accelerated filer x

Indicate by check mark whether the registrant is a shell company (as defined in Rule l2b-2 of the Exchange Act).
Yes ____ 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: 142,776,599 as of November 2, 2007.

FORM 10-Q

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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, 2006. We disclaim any obligation to update any forward looking statements as a result of developments occurring after the date of this quarterly report.

PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements

NUTRACEA AND SUBSIDIARIES
CONSOLIDATED CONDENSED BALANCE SHEETS

	September 30, 2007 (Unaudited)	December 31, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 49,546,000	$ 14,867,000
Restricted cash	545,000	-
Marketable securities	459,000	368,000
Trade accounts receivable, net of allowance for doubtful accounts of $820,000 and $20,000, respectively	5,184,000	7,093,000
Inventories	1,460,000	796,000
Notes receivable, net of discount, current portion	2,346,000	1,694,000
Other current assets	1,785,000	1,383,000
Total current assets	61,325,000	26,201,000
Notes receivable, net of current portion	5,166,000	682,000
Property and equipment, net	16,488,000	8,961,000
Investment in joint venture	1,214,000	-
Other intangible assets, net	5,821,000	5,097,000
Goodwill	39,509,000	32,314,000
Total assets	$ 129,523,000	$ 73,255,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 4,567,000	$ 2,778,000
Deferred revenue	81,000	103,000
Total current liabilities	4,648,000	2,881,000
Commitments and contingencies		
Convertible, series B preferred stock, no par value, $1,000 stated value, 25,000 shares authorized, 0 and 470 shares issued and outstanding, respectively	-	439,000
Convertible, series C preferred stock, no par value, $1,000 stated value, 25,000 shares authorized, 0 and 5,468 shares issued and outstanding, respectively	-	5,051,000
Shareholders' equity:		
	177,040,000	114,111,000

Common stock, no par value, 350,000,000 shares authorized, 142,426,599 and 103,792,827 shares issued and outstanding		
Accumulated deficit	(52,333,000)	(49,305,000)
Accumulated other comprehensive income, unrealized gain on marketable securities	169,000	78,000
Total shareholders' equity	124,875,000	64,884,000
Total liabilities and shareholders' equity	$ 129,523,000	$ 73,255,000

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

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NUTRACEA AND SUBSIDIARIES
CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS
(Unaudited)

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006
Revenues:				
Product sales	$ 13,031,000	$ 12,365,000	$ 3,048,000	$ 4,433,000
Less sales returns	(1,551,000)		(1,551,000)	
Royalty and licensing fees	5,033,000	529,000	23,000	513,000
Total revenue	16,513,000	12,894,000	1,520,000	4,946,000
Cost of goods sold	6,611,000	6,968,000	1,635,000	2,535,000
Gross margin (loss)	9,902,000	5,926,000	(115,000)	2,411,000
Research and development expenses	446,000	259,000	154,000	74,000
Selling, general and administrative expenses	12,546,000	4,413,000	4,576,000	1,563,000
Professional fees	2,742,000	764,000	747,000	314,000
Total operating expenses	15,734,000	5,436,000	5,478,000	1,951,000
(Loss) income from operations	(5,832,000)	490,000	(5,593,000)	460,000
Other income (expense)				
Interest income, net	2,167,000	317,000	778,000	181,000
Gain on settlement	1,250,000	-	-	-
Loss on retirement of assets	(309,000)	-	-	-
Loss on equity investment	(286,000)	-	(36,000)	-
Total (loss) income before income tax	(3,010,000)	807,000	(4,851,000)	641,000
Income tax (benefit) expense	(18,000)		67,000	
Net (loss) income	$ (3,028,000)	$ 807,000	$ (4,784,000)	$ 641,000
Basic and diluted (loss) earnings per share:				
Basic (loss) income per share	$ (0.02)	$ 0.01	$ (0.03)	$ 0.01
Fully diluted (loss) income per share	$ (0.02)	$ 0.01	$ (0.03)	$ 0.01
Weighted average basic number of shares outstanding	131,054,000	71,685,000	141,084,000	77,377,000
Weighted average diluted number of shares outstanding	131,054,000	109,203,000	141,084,000	115,008,000

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

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

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006
Net (loss) income	$ (3,028,000)	$ 807,000	$ (4,784,000)	$ 641,000
Other comprehensive income (loss):				
Unrealized gain (loss) on marketable securities	91,000	(34,000)	-	(21,000)
Net comprehensive (loss) income	$ (2,937,000)	$ 773,000	$ (4,784,000)	$ 620,000

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

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

	Nine Months Ended	
	September 30, 2007	**September 30, 2006**
Cash flows from operating activities:		
Net (loss) income	$ (3,028,000)	$ 807,000
Adjustments to reconcile net (loss) income to net cash used in operating activities:		
Depreciation and amortization	1,453,000	871,000
Provision for doubtful accounts	800,000	-
Loss on retirement of assets	309,000	-
Stock-based compensation	1,667,000	655,000
Loss on equity investment	286,000	-
Net changes in operating assets and liabilities (net of effects of of Grainnovations, Inc. acquisition and Vital Living, Inc. consolidation):		
Trade accounts receivable	(1,545,000)	(3,452,000)
Inventories	(623,000)	(161,000)
Other current assets	(400,000)	(248,000)
Accounts payable and accrued liabilities	(485,000)	1,315,000
Net cash used in operating activities	(1,566,000)	(213,000)
Cash flows from investing activities:		
Proceeds from payments of notes receivable	3,965,000	-
Issuance of notes receivable	(5,670,000)	(1,289,000)
Investment in Grainnovation, Inc.	(2,169,000)	-
Investment in Vital Living, Inc.	(5,143,000)	-
Investment in joint venture	(1,500,000)	-
Purchases of property and equipment	(8,208,000)	(2,984,000)
Purchases of other assets	-	(1,998,000)
Purchases of other intangible assets	(802,000)	-
Net cash used in investing activities	(19,527,000)	(6,271,000)
Cash flows from financing activities:		
Proceeds from private placement financing, net of expenses	46,805,000	15,938,000
Proceeds from exercise of common stock options	8,967,000	172,000
Payment on long-term debt	-	(4,000)
Net cash provided by financing activities	55,772,000	16,106,000
Net increase in cash	34,679,000	9,622,000
Cash, beginning of period	14,867,000	3,491,000
Cash, end of period	$ 49,546,000	$ 13,113,000
Supplemental disclosures:		
Cash paid for interest	$ -	$ 2,000

Cash paid for income taxes	$	17,000	$	5,000
Non-cash disclosures of investing and financing activities:				
Accounts receivable converted to note receivable	$	3,881,000	$	-
Accounts receivable exchanged for an intangible asset	$	300,000	$	-
Common stock issued to acquire assets related to equine feed supplement business	$	-	$	450,000
Conversion of preferred stock to common stock	$	5,490,000	$	11,554,000
Settlement of accounts receivable net to, acquire intangible asset	$	284,000	$	-
Unrealized gain (loss) on marketable securities	$	91,000	$	(21,000)

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 2006 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, or FASB, Interpretation No. 46 (revised 2003), “Consolidation of Variable Interest Entities,” or FIN 46R. During the three months ended September 30, 2007 we became a member of NutraCea-Cura LLC (Note 10) which is also consolidated under FIN 46R . All inter-company accounts and transactions have been eliminated. We operate in one business segment, which is the manufacturing and distribution of nutritional supplements.

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. The pro forma disclosures previously permitted under SFAS 123 are no longer an alternative to financial statement recognition. 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 nine and three months ended September 30, 2007 and 2006 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:

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006
Consultants	$ 345,000	$ 168,000	$ 64,000	$ (22,000)
Directors	204,000	120,000	117,000	67,000
Employees	1,063,000	267,000	223,000	69,000
To directors and former director for services	55,000	100,000	-	-

outside of directors duties				
Total stock-based compensation expense	$ 1,667,000	$ 655,000	$ 404,000	$ 114,000

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The weighted average grant date fair value of the stock options granted during the nine months ended September 30, 2007 and 2006 was $2.78 and $1.31 per share, respectively. Assumptions used in the Black-Scholes option-pricing model include (1) risk-free discount rates from 4.51% to 4.84%, (2) expected option life is calculated using the short-cut method allowed by Staff Accounting Bulletin 107, (3) expected volatility ranges from 67% to 324 % and (4) zero expected dividends. For expected volatility, share-based expenses are calculated beginning in fiscal year 2007 using a share history from the October 5, 2005 date of the NutraCea/RiceX merger which results in a volatility rate of 67%. In prior periods the fair value was determined using average share prices from inception of the Company to the end of the respective reporting period which yielded volatility rates up to 324%.

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 was 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 2007 and NutraCea retained all of the Langley shares. The $1,250,000 settlement is included in the statement of operations as other income.

Per the agreement with Langley, NutraCea is able to sell 636,013 shares of Langley at any time, and the remaining 636,013 shares of Langley and the 7,000,000 shares of NutraCea were escrowed together for a 2-year period ended October 7, 2006. At the end of the period, Langley's NutraCea shares were measured for any loss in market value and if there were such a loss, NutraCea would have been required to return to Langley that pro-rata portion of its Langley shares up to the 636,013 escrowed shares.

The Langley shares are recorded at their fair market value of $368,000 at December 31, 2006 and $459,000 at September 30, 2007, with the entire amount shown as a current asset because the escrow period has passed and we may now sell all 1,272,026 shares at any time. We have recorded an unrealized gain of $91,000 in the nine months ended September 30, 2007.

Any unrealized holding gains and losses on the marketable securities are excluded from operating results and are recognized as other comprehensive income. The fair value of the securities is determined based on prevailing market prices.

4. INVENTORY

Inventories are composed of the following;

	September 30, 2007	December 31, 2006
Finished goods	$ 1,114,000	$ 533,000
Raw materials	105,000	168,000
Packaging supplies	241,000	95,000
	$ 1,460,000	$ $ 796,000

5. NOTES RECEIVABLE

At September 30, 2007, we held thirteen (13) secured promissory notes payable to the Company with aggregate outstanding amounts under these notes of $7,512,000: $2,346,000 is reported as current and $5,166,000 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 nine months ended September 30, 2007 we loaned a total of $5,670,000, (net of the conversion of $3,881,000 of accounts receivables to a promissory note), to certain strategic customers, which loans were evidenced by promissory notes, and received payments totaling $1,671,000 on existing promissory notes. During this nine month period we also accrued interest income of $139,000 and received cash payments of $115,000 for accrued interest.

In February 2007, we converted $3,516,000 of one customer's accounts receivable to a note receivable included in the above total, bearing interest at 7% and due in December 2007. In April 2007 we converted $365,000 of another customer's accounts receivable to a note receivable included in the above total, bearing interest at 10% and due in October 2007.

During the second quarter of 2007, we granted to Pacific Holdings Advisors Limited ("PAHL") an exclusive, perpetual, royalty-free right and license to use and distribute Stabilized Rice Bran ("SRB") and SRB derivative products in certain Southeast Asian countries. PAHL paid a one-time fee of $5,000,000 for these rights. PAHL paid the license fee by issuing to NutraCea an adjustable rate promissory note initially bearing interest at the rate of 4.52% that is guaranteed by the parent of PAHL. The principal and accrued interest under this promissory note is due within five years.

During August 2007 we exchanged one customer's note receivable of $300,000 for a certain trademark and associated rights to a product line (Note 10).

6. PROPERTY AND EQUIPMENT

Property and equipment consists of the following:

	September 30, 2007	December 31, 2006
Land	$ 15,000	$ 9,000
Furniture and fixtures	2,289,000	916,000
Vehicles	73,000	73,000
Software	398,000	389,000
Leasehold improvements	581,000	430,000
Property, plant and equipment	12,506,000	4,197,000
Construction in progress	2,952,000	4,392,000
Total property, plant, and equipment	18,814,000	10,406,000
Less accumulated depreciation	(2,326,000)	(1,445,000)
Total property, plant, and equipment, net	$ 16,488,000	$ 8,961,000

Depreciation expense for the nine months ended September 30, 2007 and 2006 was $995,000 and $653,000, respectively.

Depreciation expense for the three months ended September 30, 2007 and 2006 was $353,000 and $221,000, respectively.

7. OTHER INTANGIBLE ASSETS

Other intangibles consisted of the following at:

	September 30, 2007	December 31, 2006
Patents	$ 2,657,000	$ 2,540,000
Copyrights and trademarks	3,288,000	2,987,000
Non-compete agreements	650,000	-
License and supply agreement	100,000	-
Subtotal of other intangible assets	6,695,000	5,527,000
Less accumulated amortization	(874,000)	(430,000)
Total other intangible assets, net	$ 5,821,000	$ 5,097,000

Amortization expense for the nine months ended September 30, 2007 and 2006 was $444,000 and $218,000, respectively.

Amortization expense for the three months ended September 30, 2007 and 2006 was $192,000 and $102,000, respectively.

8. (LOSS) EARNINGS PER SHARE

Basic (loss) earnings per share are computed by dividing net (loss) income by the weighted average number of common shares outstanding during all periods presented. Options and warrants are excluded from the basic (loss) earnings per share calculation and are 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 September 30, 2007, options and warrants to purchase approximately 44,770,000 shares of our common stock were outstanding. These are excluded from the calculation of diluted loss per share at September 30, 2007 because their inclusion would have been anti-dilutive.

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

	Nine Months Ended September 30,		**Three Months Ended September 30,**	
	2007	**2006**	**2007**	**2006**
Net (loss) income	$ (3,028,000)	$ 807,000	$ (4,784,000)	$ 641,000
Weighted average outstanding shares of common stock	131,054,000	71,685,000	141,084,000	77,377,000
Convertible preferred stock	-	18,880,000	-	18,880,000
Common stock equivalents	-	18,638,000	-	18,751,000
Total diluted shares	131,054,000	109,203,000	141,084,000	115,008,000
(Loss) earnings per share:				
Basic	$ (0.02)	$ 0.01	$ (0.03)	$ 0.01

Diluted	$	(0.02)	$	0.01	$	(0.03)	$	0.01

The weighted average exercise price of anti-dilutive options and warrants for the nine and three months ended September 30, 2007 were $4.26 and $3.97, respectively.

9. CONCENTRATION OF CREDIT RISK

Financial instruments that potentially subject us to significant concentrations of credit risk consist primarily of trade accounts receivable for sales to major customers. We perform credit evaluations on our customers' financial condition and generally do not require collateral on 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 and nine months ended September 30, 2007 follows:

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2007	**2006**	**2007**	**2006**
Balance, beginning of period	$ 20,000	$ 20,000	$ 1 ,075,000	$ 20,000
Provision for allowance for doubtful accounts charged to operations	1,855,000	-	800,000	-
Losses charged against allowance	-	-	-	-
Recoveries of accounts previously allowed for	(1,055,000)	-	(1,055,000)	-
Balance, end of period	$ 820,000	$ 20,000	$ 820,000	$ 20,000

During the nine months ended September 30, 2007 and 2006 we recorded an allowance for doubtful accounts of $800,000 (total provisions of $1,855,000, net of recoveries of $1,055,000) and $0, respectively. During the three months ended September 30, 2007 we recorded an allowance for doubtful accounts of ($255,000), (an allowance of $800,000, net of a $1,055,000 recovery) compared to a $0 allowance for the three months ended September, 30 2006.

Our bad debt expense for the nine months ended September 30, 2007 and 2006 was $800,000 and $0, respectively. Our bad debt expense for the three months ended September 30, 2007 and 2006 was ($255,000) and $0, respectively.

For the nine months ended September 30, 2007, six customers accounted for a total of 46% of sales: 15%, 8%, 7%, 7%, 5% and 4% respectively. No other customer was responsible for more than 3% of total sales. At September 30, 2007, two customers accounted for 67% of total accounts receivable: 35%, and 32%, respectively. No other customer accounted for more than 2% of the total outstanding accounts receivable.

For the three months ended September 30, 2007, four customers accounted for a total of 30% of sales: 12%, 6%, 6%, and 6% respectively. No other customer was responsible for more than 4% of total sales.

For the nine months ended September 30, 2006, four customers accounted for a total of 75% of sales: 64%, 6%, 3%, and 2% respectively. At September 30, 2006, accounts receivable due from these four customers were 81%, 2%, 0%, and 2%, respectively, of the total outstanding accounts receivable.

For the three months ended September 30, 2006, two customers accounted for a total of 72% of sales: 64%, and 8% respectively.

10. ACQUISITIONS AND JOINT VENTURES

Infomaxx, LLC

In December 2006, our wholly-owned subsidiary Nutramercials, Inc. became a 50% member of Infomaxx, LLC (“INFMX”). In accordance with FIN 46R, INFMX was determined to be a variable interest entity and its’ financial position and operations were included in our consolidated financial statements.

In August 2007, we became the sole member of INFMX after we purchased from the other member of INFMX their 50% of INFMX’s outstanding membership interests by canceling a $300,000 note payable to NutraCea by that member of INFMX. We received along with the 50% interest, all rights to a certain trademark and product line of that member. We recorded an intangible asset of $284,000. Additionally, in order to consummate this transaction we agreed to accept the return of $275,000 of inventory from the other previous member of INFMX which we sold them in December 2006, for $1,551,000. The $1,551,000 return is recorded as a sales return on our consolidated condensed statement of operations.

NutraCea/Cura LLC

In August 2007, we formed NutraCea/Cura, LLC (“NCC”) with Cura Pharmaceuticals (“CURA”). We formed this LLC with CURA to jointly develop, and produce through third-party pharmaceutical-grade co-packers, market and sell nutraceutical and pharmaceutical products. We hold a 60% interest in NCC. Accordingly, NCC is included in our consolidated financial statements. The results of operations for the three months ended September 30, 2007 were insignificant.

Under the agreement NCC has a supply agreement with minimum purchase requirements of approximately $1,150,000 for the first year, which increase 5% a year for five years. If the minimum purchase commitments are not met in any year the make of the products may terminate the supply agreement.

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 (“holdback”) being due in payments of $235,000 and $310,000 in six months and twelve months respectively, subject to reduction in the event of breaches of representations, warranties and covenants contained in the transaction documents. The holdback is held in third-party escrow and is included in our consolidated condensed balance sheet as restricted cash and current liabilities. The investment is recorded in our financial statements included herein at the aggregate purchase price and its results of operations from the date of acquisition are reflected in our statement of operations for the periods ended September 30, 2007. In November, 2007, the second installment of $235,000 due 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 will 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 Grain Enhancements 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 is to be contributed no later than October 2007, and the remaining $1,500,000 from each member is due no later than August 2008. As of November 2, 2007 neither party to the LLC has made the October 2007 scheduled contribution as the capital infusion was not needed as of that date, and both parties are discussing deferring that contribution until a later date to be agreed upon.

Theorem was paid $750,000 and $500,000 by NutraCea and GE, respectively, for services relating to the formation of the joint venture. Through September 30, 2007, our portion of Grain Enhancements net loss was $286,000.

Our investment in Grain Enhancements is accounted for under the equity method of accounting. At September 30, 2007 the value of our investment was $1,214,000.

Summary financial information of Grain Enhancements, LLC at September 30, 2007 is:

Assets	
Cash	$ 2,464,000
Liabilities and Equity	
Accounts payable and accrued liabilities	$ 36,000
Members equity	3,000,000

Accumulated deficit		(572,000)
Total Equity		2,428,000
Total liabilities and equity	$	2,464,000

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 fourth quarter of 2007, 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 fourth quarter of 2007.

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 our 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 September 30, 2007 the financial position of VLI for the period ended September 30, 2007, and VLI's results of operations for the period from April 20, 2007 through September 30, 2007 in our statement of operations for the three and nine months ended September 30, 2007, while eliminating inter-company balances. The effect on our consolidated, condensed balance sheet at September 30, 2007 was an increase in total assets of $799,000, an increase in total liabilities of $1,439,000 and a decrease in shareholder equity of $640,000. The effect on our consolidated income statement for the nine month period was an increase in revenues of $781,000, an increase in cost of goods sold of $385,000, an increase in operating expenses of $761,000, an increase of other expenses of $275,000 and an increase in net loss of $640,000. The effect on our consolidated income statement in the three month period ended September 30, 2007 was an increase in revenues of $184,000, an increase in cost of goods sold of $120,000, an increase in operating expenses of $317,000, an increase of other expenses of $134,000 and an increase in net loss of $387,000.

11. RELATED PARTY TRANSACTIONS

Vital Living, Inc.

In conjunction with our purchase of certain securities of VLI (Note 10), we consolidated VLI financial results for the period April 20, 2007 to September 30, 2007 into our financial results for the three and nine months ending September 30, 2007. Also during three months ended end June 30, 2007, we entered into a business relationship with a new customer that is also a customer of VLI. The CEO of VLI is also a principal partner with this new customer. During the quarter ended June 30, 2007, we recorded sales of $2,080,000 to this new customer. In the three months ended September 30, 2007 there were no sales made to this customer. At September 30, 2007 we had $1,731,000 due from this customer included in our accounts receivable of $5,184,000. During the nine months ended September 30, 2007 the CEO of VLI has advanced VLI $407,000 of short-term, non-interest bearing loans which are included in accrued liabilities on our consolidated condensed balance sheet.

Sales to related customers

During the nine months ended September 30, 2007 we have made sales to a customer totaling $500,000. This customer is a shareholder holding approximately 1,389,000 shares of our common stock. At September 30, 2007, $119,000 due from this customer was included in accounts receivable.

12. COMMITMENTS AND CONTINGENCIES

Grain Enhancement LLC

In June 2007, we formed a joint venture with PAHL (Note 10) which requires us to make capital contributions to the joint venture totaling up to $5,000,000. Both members made the first capital contribution of $1,500,000 in July 2007. An additional $2,000,000 is due no later than October 2007, and the final contribution, if required, of $1,500,000 is due no later than August 2008. As of November 2, 2007 neither party to the LLC has made the October 2007 scheduled contribution as the capital infusion was not needed as of that date, and both parties are discussing deferring that contribution until a later date to be agreed upon.

Contractual Obligations

We lease corporate office space in Phoenix, AZ and warehouse facilities in Sacramento, CA. Future amounts due under these leases at September 30, 2007 are included in the following table:

Fiscal Year 2007	$ 147,000
Fiscal Year 2008	1,074,000
Fiscal Year 2009	1,393,000
Fiscal Year 2010	1,442,000
Fiscal Year 2011	1,490,000
Fiscal Year 2012	1,539,000
Thereafter	5,336,000
Total	$ 12,421,000

Total rent expense for the nine and three months ended September 30, 2007 was $672,000 and $90,000, respectively.

Total rent expense for the nine and three months ended September 30, 2006 was $85,000 and $19,000, respectively.

13. STOCKHOLDERS EQUITY

Common Stock

During the three months ended September 30, 2007:

One (1) shareholder converted two shares of Series C Convertible preferred Stock into 2,352 shares of our common stock. The preferred shares converted at a conversion rate of 1,176 shares of common stock for each preferred share.

Eighteen (18) security holders exercised options or warrants and received a total of 2,291,183 shares of common stock for an aggregate purchase price of $2,090,000.

During the three months ended June 30, 2007:

Thirty (30) security holders exercised options or warrants and received a total of 5,400,199 shares of common stock for an aggregate purchase price of $2,947,000.

During the three months ended March 31, 2007:

Four (4) security holders converted 470 shares of Series B Convertible preferred Stock into 940,000 shares of our common stock. The preferred shares converted at a conversion rate of 2,000 shares of common stock for each preferred share.

Seventeen (17) security holders converted 5,466 shares of Series C Convertible preferred Stock into 6,430,580 shares of our common stock. The preferred shares converted at a conversion rate of 1,176 shares of common stock for each preferred share.

Twenty-one (21) security holders exercised options or warrants and received a total of 3,451,959 shares of common stock for an aggregate purchase price of $3,930,000.

We issued 17,500 shares of our common stock valued at $55,000 to a former member of our board of directors as payment for past services on our board of directors.

<u>Options and Warrants</u>

During the three months ended September 30, 2007:

We issued to six (6) employees options to purchase a total of 65,000 shares of common stock with vesting periods ranging from 90 days to three years. The options expire in ten years and have exercise prices per share ranging from $1.44 to $3.22.

During the three months ended June 30, 2007:

We issued to thirteen (13) employees options to purchase a total of 276,000 shares of common stock with vesting periods ranging from immediately to three years. The options expire in ten years and have exercise prices per share ranging from $3.03 to $4.04.

We issued to six (6) outside directors options to purchase a total of 210,000 shares of common stock that vest evenly over one year. The options expire in ten years and have exercise prices per share ranging from $3.76 to $3.83.

We issued to one (1) consultant a warrant to purchase a total of 25,000 shares of common stock, with a vesting period of fifteen months. This warrant expires after three years and has an exercise price per share of $3.27.

In June 2007 we granted PAHL a warrant to purchase 1,500,000 shares of common stock at $5.25 per share. This warrant vests at 375,000 per quarter beginning July 1, 2007 except that such warrant will not be exercisable until such time as Grain Enhancements LLC has met certain conditions as defined in the agreement (Note 10).

During the three months ended March 31, 2007:

We issued to eleven (11) employees options to purchase a total of 635,000 shares of common stock with vesting periods ranging from zero to three years. The options expire in ten years and have exercise prices per share ranging from $2.45 to $3.39.

We issued to three (3) consultants three warrants to purchase a total of 290,000 shares of common stock, with vesting periods ranging from 3 months to two years. These warrants expire after three to five years and have exercise prices per share ranging from $2.38 to $3.03.

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

February 2007 Private Placement

In addition to the foregoing issuances of our securities, in February 2007 we issued common stock and warrants to twenty-three (23) investors in a private placement transaction for aggregate gross proceeds of approximately $46,805,000 after offering expenses. We issued an aggregate of 20,000,000 shares of common stock at a price of $2.50 per share and warrants to purchase an aggregate of 10,000,000 shares of our common stock at an exercise price of $3.25 per share. The placement agent for the private placement also received a warrant to purchase 1,200,000 shares of common stock at an exercise price per share of $3.25. Each of the warrants issued in the transaction has a term of five years. The fair value of these warrants to purchase 11,200,0000 shares of common stock using the Black-Scholes method is approximately $29,153,000. If exercised, the company would receive $36,400,000.

14. SUBSEQUENT EVENTS

On November 7, 2007, NutraCea entered into an agreement with Patricia McPeak, the founder and former Chairman and CEO of NutraCea, concerning their business relationship. Pursuant to the agreement, in consideration for a payment of $1 million, Nutracea acquired certain other inventions and intellectual property rights from Ms. McPeak and acquired a right of first refusal to license, manufacture and/or sell products that Ms. McPeak may formulate in the future for the retail market and for feeding programs, subject to certain exceptions and agreement on license terms. In addition Ms. McPeak agreed to assign to NutraCea her interest as a co-inventor in certain patent applications. The agreement also terminates her employment agreement with the company and contains a number of other customary provisions relating to termination of employment, and also includes a general mutual release of all claims concerning any past events or conduct. The agreement also grants Ms. McPeak the non-exclusive right to sell stabilized rice bran products formulated from NutraCea ingredients in Central and South America, and via websites owned or controlled by Ms. McPeak.

In October 2007, one shareholder exercised warrants and received a total of 350,000 shares of common stock for an aggregate purchase price of approximately $245,000.

15. IMPLEMENTATION OF RECENT ACCOUNTING PRONOUNCEMENTS

During the nine months ended September 30, 2007, we implemented the following new critical accounting policies;

In June 2006, the Financial Accounting Standards Board ("FASB") issued Interpretation No.48, *Accounting for Uncertainty in Income Taxes — An Interpretation of FASB Statement No. 109*, (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return that results in a tax benefit. Additionally, FIN 48 provides guidance on de-recognition, statement of operations classification of interest and penalties, accounting in interim periods, disclosure, and transition. This interpretation is effective for fiscal years beginning after December 15, 2006. The Company adopted FIN 48 as of January 1, 2007, as required. The adoption of FIN 48 did not have a material impact on the Company's financial position or results of operations.

In December 2006, the FASB issued Staff Position EITF 00-19-2, *Accounting for Registration Payment Arrangements* ("FSP EITF 00-19-2"), which provides guidance on the accounting for registration payment arrangements. FSP EITF 00-19-2 specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision of a financial instrument or other agreement, should be separately recognized and measured in accordance with FASB Statement No. 5, *Accounting for Contingencies*. A registration payment arrangement is defined in FSP EITF 00-19-2 as an arrangement with both of the following characteristics: (1) the arrangement specifies that the issuer will endeavor (a) to file a registration statement for the resale of specified financial instruments and/or for the resale of equity shares that are issuable upon exercise or conversion of specified financial instruments and for that registration statement to be declared effective by the Securities and Exchange Commission within a specified grace period, and/or (b) to maintain the effectiveness of the registration statement for a specified period of time (or in perpetuity); and (2) the arrangement requires the issuer to transfer consideration to the counterparty if the registration statement for the resale of the financial instrument or instruments subject to the arrangement is not declared effective or if effectiveness of the registration statement is not maintained. FSP EITF 00-19-2 is effective for registration payment arrangements and the financial instruments subject to those arrangements that are entered into or modified subsequent to December 21, 2006. For registration payment arrangements and financial instruments subject to those arrangements that were entered into prior to the issuance of FSP EITF 00-19-2, this guidance is effective for financial statements issued for fiscal years beginning after December 15, 2006, and interim periods within those fiscal years. The adoption of FSP EITF 00-19-2 on January 1, 2007 did not have a material impact on the Company's financial position or results of operations.

Recent Accounting Pronouncements

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurement" (FAS 157). This Standard defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. FAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company has not determined the effect that the adoption of FAS 157 will have on its consolidated financial position, results of operations or cash flows.

In February 2007, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for the Company's year ending September 30, 2009. The Company is currently evaluating the impact of SFAS 159 on the Company's financial statements.

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.

The following is a discussion of the consolidated financial condition of our results of operations for the three and nine months ended September 30, 2007 and 2006.

THREE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006

For the three months ended September 30, 2007, the Company's net loss was ($4,784,000), or ($0.03) per share, compared to income of $641,000 or $0.01 per share, in the same period of 2006, showing a decrease of $5,425,000. The decrease for the quarter was primarily due to a $1,385,000, or 31%, decrease in sales, a return of $1,551,000 of product we previously sold in connection with our purchase of the remaining 50% interest in INFMX (Note 10), offset by a corresponding $900,000, or 35% decrease in our cost of goods sold, an increase of $3,527,000 in operating expenses, a $36,000 charge for the equity loss on our joint venture, offset by an increase of $597,000 of interest income.

Our consolidated net revenues for the three months ended September 30, 2007 of $1,520,000 decreased $3,426,000 from the $4,946,000 consolidated revenues recorded in the same period last year. The decrease is comprised of a $1,422,000 increase in product sales, offset by a $2,807,000 decrease in infomercial sales and a decrease of $490,000 in royalty revenues as shown in the following table:

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Increase / Decrease
Product, net of discounts	$ 3,048,000	$ 1,626,000	$ 1,422,000
Infomercial	-	2,807,000	(2,807,000)
Less infomercial sales return	(1,551,000)		(1,551,000)
Net infomercial sales	(1,551,000)	2,807,000	(4,358,000)
Royalty and licensing fees	23,000	513,000	(490,000)
Total revenues	$ 1,520,000	$ 4,946,000	$ (3,426,000)

Gross margins on product sales in the quarter ended September 30, 2007 were ($115,000), or (5.0%), compared to $1,898,000, or 43%, during 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. The $2,526,000 decrease for the three months ended September 30, 2007 is comprised of the $753,000 decline corresponding to the decline in sales in the third quarter of 2007, a $1,284,000 decline associated with the return of product noted above, and a $489,000 decline in royality and licensing fees. Our gross margin for the quarter ended September 30, 2007, was 47% compared to 43% in the same period last year.

Research and Development ("R&D") expenses increased from $74,000 for the quarter ended September 30, 2006 to $154,000 for the quarter ended September 30, 2007, or an increase of $80,000. 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 $4,576,000 and $1,563,000 in the quarterly periods ended September 30, 2007 and 2006 respectively, an increase of $3,013,000, or 193%. This increase is predominately due to expanded investment in personnel, infrastructure, and sales and marketing activities to meet anticipated future demands (with the exception of bad debt expense, as described below). Specific changes in SG&A expense is detailed in the following schedule:

	Three Months Ended September 30, 2007	Three Months Ended September 30, 2006	Increase / Decrease
Payroll	$ 1,151,000	$ 420,000	$ 731,000
Employee benefits, payroll taxes, and hiring expenses	356,000	147,000	209,000
Sales and marketing	1,041,000	140,000	901,000
Allowance for bad debt expense, net	(255,000)	-	(255,000)
Operations	263,000	136,000	127,000
Travel and entertainment	180,000	146,000	34,000
Rent and facility costs	396,000	21,000	375,000
Stock based compensation	404,000	114,000	290,000
Shareholder relations	188,000	64,000	124,000
Depreciation and amortization, net of allocation to cost of goods sold	308,000	224,000	84,000
Administration, insurance, and other	544,000	151,000	393,000
Total selling, general and administrative expenses	$ 4,576,000	$ 1,563,000	$ 3,013,000

In the three months ended September 30, 2007 our provision for the allowance for bad debt expense was ($255,000) compared to $0 in the three months ended September 30, 2006. This decrease is the result of an $800,000 additional provision offset by a recovery of $1,055,000 previously provided for.

Professional fees increased $433,000 from $314,000 for the quarter ended September 30, 2006 to $747,000 for the quarter ended September 30, 2007. The higher professional fees in 2007 primarily relate to consulting fees incurred in connection with marketing and business development activities and Sarbanes-Oxley Section 404 activities. Professional fees include costs related to accounting, legal and consulting services.

Other income and expense, net, increased by $561,000 in the three months ended September 30, 2007 compared to 2006. This increase is comprised primarily of a $597,000 increase in interest income due to higher cash balances.

NINE MONTHS ENDED SEPTEMBER 30, 2007 AND 2006

For the nine months ended September 30, 2007, the Company's net loss was ($3,028,000), or ($0.02) per share, compared to net income of $807,000, or $0.01 per share, in the same period of 2006, showing a decrease of $3,835,000. The decrease for the nine month period was primarily due to a $10,297,000 increase in operating expenses, a $286,000 loss on our investment in a joint venture, and a $309,000 expense for loss on the retirement of assets when we moved our corporate offices to Phoenix, AZ, offset by a $357,000 decline in our cost of goods sold, an increase of $4,504,000 in royalty revenues, a $1,849,000 increase in interest income, and a $1,250,000 gain on the settlement of a lawsuit.

Our consolidated revenues through September 30, 2007 of $16,513,000 increased $3,619,000, or 28%, from the same period last year. The revenue increase is attributable to a $8,161,000, or 186%, increase in product sales, offset by a

decrease of $9,046,000 in infomercial sales, including a $1,551,000 sales return (Note 10), and a $4,504,000 increase in royalty and licensing revenue over the nine months ended September 30, 2006, as shown in the following schedule:

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	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006	Increase / Decrease
Product, net of discounts	$ 12,545,000	$ 4,384,000	$ 8,161,000
Infomercial	486,000	7,981,000	(7,495,000)
Less infomercial sales return	(1,551,000)	-	(1,551,000)
Net infomercial sales	(1,065,000)	7,981,000	(9,046,000)
Royalty and licensing fees	5,033,000	529,000	4,504,000
Total revenues	$ 16,513,000	$ 12,894,000	$ 3,619,000

Gross margins on sales in the nine months ended September 30, 2007 were $9,902,000, or 47%, compared to $5,396,000, or 44%, during 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. The $3,976,000 increase for the nine months ended September 30, 2007 is comprised of the $756,000 increase corresponding to the sales growth in the nine months ended September 30, 2007, offset by the $1,284,000 decline associated with the return of product noted above, and a $4,504,000 increase in royality and licensing fees.

R&D expenses increased from $259,000 for the nine months ended September 30, 2006 to $446,000 for the nine months ended September 30, 2007, or an increase of $187,000. 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.

SG&A expenses were $12,546,000 and $4,413,000 in the nine months ended September 30, 2007 and 2006 respectively, an increase of $8,133,000, or 184%. This increase is predominately due to expanded investment in personnel, infrastructure, and sales and marketing activities to meet anticipated future demands (with the exception of bad debt expense - see below). Specific changes in SG&A expense is detailed in the following schedule:

	Nine Months Ended September 30, 2007	Nine Months Ended September 30, 2006	Increase / Decrease
Payroll	$ 3,014,000	$ 1,374,000	$ 1,640,000
Employee benefits, payroll taxes, and hiring expenses	924,000	367,000	557,000
Sales and marketing	2,114,000	318,000	1,796,000
Allowance for bad debt expense	800,000	-	800,000
Operations	745,000	246,000	499,000
Travel and entertainment	673,000	326,000	347,000
Rent and facility cost	689,000	90,000	599,000
Stock based compensation	1,667,000	114,000	1,553,000
Shareholder relations	425,000	197,000	228,000
Depreciation and amortization, net of allocation to cost of goods sold	555,000	477,000	78,000
Administration, insurance, and other	940,000	904,000	36,000

Total selling, general and administrative expenses	$ 12,546,000	$ 4,413,000	$ 8,133,000

In the nine months ended September 30, 2007 our provision for the allowance for bad debt expense was $800,000 (net of $1,055,000 in recoveries) compared to $0 for the nine months ended September 30, 2006. This increase is the result of an $1,855,000 additional provision offset by a recovery of $1,055,000 previously provided for.

Professional fees increased $1,978,000 from $764,000 for the nine months ended September 30, 2006 to $2,742,000 for the nine months ended September 30, 2007. The higher professional fees in 2007 primarily relate to consulting fees incurred in connection with marketing and business development activities and a charge of $750,000 for costs associated with developing our joint venture with Grain Enhancements LLC (Note 10). Professional fees include costs related to accounting, legal and consulting services.

Other income and expense, net, increased by $2,505,000 in the nine months ended September 30, 2007 compared to 2006. This increase is comprised of a $1,850,000 increase in interest income, a $1,250,000 gain on the settlement of a lawsuit (Note 3), offset by a $309,000 charge for the loss on the retirement of assets, and a $286,000 charge for the loss on the equity investment in a joint venture (Note 10).

LIQUIDITY AND CAPITAL RESOURCES

As of September 30, 2007, our source of liquidity was cash in the amount of $49,546,000. Our cash increased by $34,679,000 in the nine months ended September 30, 2007 from our cash position of $14,867,000 at December 31, 2006.

For the first nine months of 2007, net cash used in operations was $1,566,000, compared to cash used in operations in the same period of 2006 of $213,000, an increase of $1,353,000. This increase in cash used in operations resulted primarily from our net loss of $3,028,000, plus the non-cash charges against income of $1,453,000 for depreciation and amortization, $800,000 for an increase in the provision for doubtful accounts, a $309,000 charge for the loss on the retirement of assets, a $1,667,000 charge for stock-based compensation, a $286,000 charge for the equity loss on our joint venture, and the increase in inventories of $623,000, an increase in accounts receivable of $1,545,000 (net of a conversion of a customers' accounts receivable of $3,881,000 to a short-term note receivable (Note 5), an increase of $400,000 in other current assets, and a decrease of $485,000 in accounts payable and accrued liabilities.

Cash used in investing activities in the first nine months of 2007 was $19,527,000, compared to $6,271,000 for the same period of 2006. This increase of 13,256,000 was primarily caused by $8,208,000 in expenditures for plant expansions and other fixed assets, $802,000 for the purchase of intangible assets, $2,169,000 and $5,143,000 for the purchase Grainnovation, Inc. and the investment in Vital Living, Inc., respectively, net of cash received in those transactions, the $1,500,000 investment in the GE joint venture, and a net outflow of $1,705,000 relating to loans made by us to certain customers, net of $3,881,000 of accounts receivable converted to short-term notes receivable (Note 5).

Cash provided by financing activities for the nine months ended September 30, 2007, was approximately $55,772,000, which reflects proceeds from our February 2007 private placement financing (see below) and proceeds received upon the exercise of common stock options and warrants. This is an increase of $30,867,000 from the private placement financing, and the $8,795,000 increase from the exercise of common stock options, compared to the nine months ended September 30, 2006. Our working capital position as of September 30, 2007 was $56,676,000 compared to $23,320,000 as of December 31, 2006.

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.

In April 2007, we acquired shares of convertible preferred stock and secured convertible notes of Vital Living, Inc. from the holders of those outstanding securities, for an aggregate of $5,226,000 (Note 10).

On May 1, 2007, we purchased the outstanding stock of Grainnovation, Inc. (“GI”) and certain assets used in the business of GI. The purchase enables us to produce pellets for the equine market. The purchase agreement provides for a cash purchase price of $2,150,000, and allows NutraCea to require the former shareholders of GI to repurchase from NutraCea the stock of GI if certain post-closing covenants are not satisfied by GI in the six month period following the closing of the transaction (Note 10).

In June 2007, we entered into a joint venture with PAHL to form Grain Enhancement LLC (Note 10). This joint venture required a $1,500,000 capital contribution which was made in July 2007. Additional capital contributions of $2,000,000 and $1,500,000 are due from each member in October 2007 and August 2008, respectively. As of November 2, 2007 neither party to the LLC has made the October 2007 scheduled contribution as the capital infusion was not needed as of that date, and both parties are discussing deferring that contribution until a later date to be agreed upon.

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 on-going 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 2006 Form 10-K for the fiscal year ended December 31, 2006.

Acquisitions

We account for acquisitions in accordance with Statement of Financial Accounting Standards (“SFAS”), No. 141 “Business Combinations” and accordingly apply the purchase method of accounting for all business combinations initiated after September 30, 2001 and separately identify recognized intangible assets that meet certain criteria, amortizing these assets over their determinable useful lives.

During the nine months ended September 30, 2007, we implemented the following new critical accounting policy:

In December 2003, the Financial Accounting Standards Board (“FASB”) issued SFAS Interpretation No. 46R, *Consolidation of Variable Interest Entities* (“FIN 46R). Under FIN 46R, if a business enterprise has a controlling financial interest in a variable interest entity, the assets, liabilities, and results of the activities of the variable interest entity should be included in consolidated financial statements with those of the business enterprise. An enterprise that consolidates a variable interest entity is the primary beneficiary of the variable interest entity. FIN 46R became applicable to the Company during the six months ended June 30, 2007. See footnote 10 for more information.

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Recent accounting pronouncements

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, “Fair Value Measurement” (FAS 157). This Standard defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. FAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007 and interim periods within those fiscal years. The Company has not determined the effect that the adoption of FAS 157 will have on its consolidated financial position, results of operations or cash flows.

In February 2007, the FASB issued Statement of Financial Accounting Standards (SFAS) No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective for the Company’s year ending September 30, 2009. The Company is currently evaluating the impact of SFAS 159 on the Company’s financial statements. Put in recent pronouncements

In June 2006, the FASB issued Interpretation No.48, *Accounting for Uncertainty in Income Taxes — An Interpretation of FASB Statement No. 109*, (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise’s financial statements in accordance with SFAS No. 109, “*Accounting for Income Taxes*”. FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of an uncertain tax position taken or expected to be taken in a tax return that results in a tax benefit. Additionally, FIN 48 provides guidance on de-recognition, statement of operations classification of interest and penalties, accounting in interim periods, disclosure, and transition. This interpretation is effective for fiscal years beginning after December 15, 2006. The Company adopted FIN 48 as of January 1, 2007, as required. The adoption of FIN 48 did not have a material impact on the Company’s financial position or results of operations.

In December 2006, the FASB issued FASB Staff Position EITF 00-19-2, *Accounting for Registration Payment Arrangements* (“FSP EITF 00-19-2”), which provides guidance on the accounting for registration payment arrangements. FSP EITF 00-19-2 specifies that the contingent obligation to make future payments or otherwise transfer consideration under a registration payment arrangement, whether issued as a separate agreement or included as a provision of a financial instrument or other agreement, should be separately recognized and measured in accordance with FASB Statement No. 5, *Accounting for Contingencies*. A registration payment arrangement is defined in FSP EITF 00-19-2 as an arrangement with both of the following characteristics: (1) the arrangement specifies that the issuer will endeavor (a) to file a registration statement for the resale of specified financial instruments and/or for the resale of equity shares that are issuable upon exercise or conversion of specified financial instruments and for that registration statement to be declared effective by the Securities and Exchange Commission within a specified grace period, and/or (b) to maintain the effectiveness of the registration statement for a specified period of time (or in perpetuity); and (2) the arrangement requires the issuer to transfer consideration to the counterparty if the registration statement for the resale of the financial instrument or instruments subject to the arrangement is not declared effective or if effectiveness of the registration statement is not maintained. FSP EITF 00-19-2 is effective for registration payment arrangements and the financial instruments subject to those arrangements that are entered into or modified subsequent to December 21, 2006. For registration payment arrangements and financial instruments subject to those arrangements that were entered into prior to the issuance of FSP EITF 00-19-2, this guidance is effective for financial statements issued for fiscal years beginning after December 15, 2006, and interim periods within those fiscal years. The adoption of FSP EITF 00-19-2 on January 1, 2007 did not have a material impact on the Company’s financial position or results of operations.

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 September 30, 2007, there was no long-term debt outstanding. 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

We carried out an evaluation, under the supervision and with the participation of management, including the Company's principal executive officer and principal financial officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined under Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) 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 September 30, 2007, NutraCea's disclosure controls and procedures were adequate to ensure that information required to be disclosed by NutraCea in reports filed or submitted under the Exchange Act were timely recorded, processed and reported within the time periods specified in the Securities and Exchange Commission rules and forms.

In August 2007, Perry Smith, LLP, our independent registered public accounting firm advised the audit committee of our board of directors that it identified deficiencies that existed in the design or operation of the Company's internal controls that it considered to be material weaknesses in the effectiveness of NutraCea's internal controls. The deficiencies reported by Perry Smith included the lack of a documented policy relating to the retention of experts that provide assistance to NutraCea with financial transactions and insufficient procedures to ensure timely and comprehensive analysis by management of significant accounting transactions. In the period covered by this quarterly report, NutraCea addressed these deficiencies. NutraCea implemented and documented procedures to evaluate the qualifications of, and potential conflicts with, financial experts, including requiring that NutraCea's board of directors approve the retention of financial experts if the dollar amount of the transactions for which the experts will be retained exceeds certain objective thresholds. In addition, NutraCea implemented procedures that will improve the timeliness and review of accounting issues, including earlier review of accounting and reporting issues relating to significant transactions and earlier participation by management in the analysis of the accounting impact 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 affect, the Company's internal control over financial reporting.

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 third quarter of 2007 and in each quarter before 2006.

We began operations in February 2000 and incurred losses in each reporting period until the second fiscal quarter of 2006, and we incurred losses in third fiscal 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 and 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 depend on limited number of customers.

During 2006, we received approximately 67% of product sales revenue from five customers and approximately 48% of our revenue from one customer. During the nine months ended September 30, 2007, six customers accounted for 46% of our sales. A loss of any of these customers could have a material adverse effect on our revenues and results of operations.

We rely upon a limited number of product offerings.

All 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.

All 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"), Archer Daniels Midland ("ADM"), our stage I plant in Mermentau, LA and our single value-added products plant in Dillon, Montana. Between the Dillon, Montana plant and the facilities at FRC, ADM, and Mermentau, we currently are capable of producing just enough finished products to meet current demand. The existing plants do not allow for dramatic expansion of product demand, therefore domestic production capacity is needed. Anticipating incremental demand for NutraCea products, we completed the first phase of an expansion of the Dillon, Montana facility in 2006. We have also entered into a new raw rice bran supply agreement with Louisiana Rice Mill ("LRM") in Louisiana. The supply agreement led to the construction of a new stabilization plant in Mermentau which became operational in April 2007. These facilities plus another stabilization and value-added plant scheduled to be operational by the end of 2007 should meet our production needs for 2007, but 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 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.

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.

Failure to achieve and maintain effective internal controls in accordance with Section 404 of the Sarbanes-Oxley Act could have a material adverse effect on our business and stock price.

We are evaluating our internal controls over financial reporting to allow management to report on, and our independent registered public accounting firm to attest to, our internal controls, as required by the Sarbanes-Oxley Act. We will be performing the system and process evaluation and testing (and any necessary remediation) required to comply with the management certification and auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act ("Section 404"). NutraCea is required to comply with the Section 404 requirements for its fiscal year ending December 31, 2007. While we anticipate being able to fully implement the requirements relating to internal controls and all other aspects of Section 404 by our compliance deadline, we cannot be certain as to the timing of completion of our evaluation, testing and remediation actions or the impact of the same on our operations. If we are not able to implement the requirements of Section 404 in a timely manner or with adequate compliance, we might be subject to sanctions or investigation by regulatory authorities, including the SEC. In addition, we may be required to incur a substantial financial investment to improve our internal systems and the hiring of additional personnel or consultants. Failure to achieve and maintain an effective internal control environment could have a material adverse effect on our business and stock price.

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. Although we have written employment agreements with each of the foregoing individuals 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.

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, and paid off all short and long term debt obligations. 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 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 September 30, 2007	$ 3.31	$ 1.34
Three months ended June 30, 2007	$ 5.04	$ 2.60
Three months ended March 31, 2007	$ 3.39	$ 2.21
Twelve months ended December 31, 2006	$ 2.74	$ 0.60
Twelve months ended December 31, 2005	$ 1.81	$ 0.30

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 November 2, 2007, NutraCea had 142,776,599 shares of common stock outstanding. Additionally, as of November 2, 2007, options and warrants to purchase approximately 44,363,000 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 November 2, 2007, approximately 26,220,000 shares of our common stock remained eligible for resale pursuant to outstanding registration statements filed for these investors. 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 November 2, 2007, there were outstanding options and warrants to purchase approximately 44,363,000 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.

We may engage in future acquisitions that dilute our shareholders and cause us to incur debt or assume contingent liabilities.

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.

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 September 30, 2007, NutraCea issued the following securities without registration under the Securities Act of 1933:

Common Stock

One (1) shareholder converted 2 shares of Series C Convertible preferred Stock into 2,352 shares of our common stock. The preferred shares converted at a conversion rate of 1,176 shares of common stock for each preferred share.

Eighteen (18) shareholders exercised options or warrants and received a total of 2,291,183 shares of common stock for an aggregate purchase price of $2,089,000.

Options and Warrants

We issued to six (6) employees options to purchase a total of 65,000 shares of common stock with vesting periods ranging from 90 days to three years. The options expire in ten years and have exercise prices per share ranging from $1.44 to $3.22.

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

The issuance of common stock upon conversion of preferred stock was exempt from registration pursuant to Section 3(a)(9) of the Securities Act of 1933. All other issuances above were made without public solicitation, and were acquired for investment purposes only and 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**
2.1	Asset Purchase Agreement, dated as of September 28, 2007, between NutraCea and Vital Living, Inc. (incorporated herein by reference to the registrant’s current report on Form 8-K filed on October 4, 2007).
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: November 14, 2007

/s/ Bradley Edson

Bradley Edson
Chief Executive Officer

Dated: November 14, 2007

/s/ Todd C. Crow

Todd C. Crow,
Chief Financial Officer
(Principal Accounting Officer)