STANDARD REGISTER CO
Form 10-Q
May 02, 2007

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended April 1, 2007

OR

[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from ________ to ________

Commission file number 0-01097

THE STANDARD REGISTER COMPANY

(Exact name of registrant as specified in its charter)

OHIO	**31-0455440**
(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)
600 ALBANY STREET, DAYTON OHIO	**45408**
(Address of principal executive offices)	(Zip Code)

(937) 221-1000

(Registrant s telephone number, including area code)

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

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 Exchange Act. (Check one):

Large accelerated filer [ ]

Accelerated filer [X]

Non-accelerated filer [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act):

Yes [ ] No [X]

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding as of April 1, 2007
Common stock, $1.00 par value	23,960,974 shares
Class A stock, $1.00 par value	4,725,000 shares

THE STANDARD REGISTER COMPANY

FORM 10-Q

For the Quarter Ended April 1, 2007

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PART I - FINANCIAL INFORMATION

THE STANDARD REGISTER COMPANY

CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME

(Dollars in thousands, except per share amounts)

	13 Weeks Ended	
	April 1 2007	***April 2 2006***
REVENUE		
Products	$ 208,717	$ 211,292
Services	18,714	17,229
Total revenue	227,431	228,521
COST OF SALES		
Products	140,625	136,794
Services	10,871	9,924
Total cost of sales	151,496	146,718
GROSS MARGIN	75,935	81,803
OPERATING EXPENSES		
Selling, general and administrative	66,918	66,246
Depreciation and amortization	6,655	7,327
Asset impairments	(409)	1,694
Restructuring charges	2,406	1,090
Total operating expenses	75,570	76,357
INCOME FROM CONTINUING OPERATIONS	365	5,446
OTHER INCOME (EXPENSE)		
Interest expense	(797)	(514)
Other income	68	36
Total other expense	(729)	(478)
(LOSS) INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES AND CUMULATIVE EFFECT OF A CHANGE IN ACCOUNTING PRINCIPLE	(364)	4,968
INCOME TAX (BENEFIT) EXPENSE	(175)	2,090
NET (LOSS) INCOME FROM CONTINUING OPERATIONS BEFORE CUMULATIVE	(189)	2,878

EFFECT OF A CHANGE IN ACCOUNTING PRINCIPLE		
DISCONTINUED OPERATIONS		
Loss from discontinued operations, net of taxes	(639)	(1,458)
NET (LOSS) INCOME BEFORE CUMULATIVE EFFECT OF A CHANGE IN ACCOUNTING PRINCIPLE	(828)	1,420
Cumulative effect of a change in accounting principle, net of taxes	-	78
NET (LOSS) INCOME	$ (828)	$ 1,498
BASIC AND DILUTED (LOSS) INCOME PER SHARE		
(Loss) income from continuing operations	$ (0.01)	$ 0.10
Loss from discontinued operations	(0.02)	(0.05)
Net (Loss) Income per share	$ (0.03)	$ 0.05
Dividends Paid Per Share	$ 0.23	$ 0.23
NET (LOSS) INCOME	$ (828)	$ 1,498
Net actuarial loss reclassification	4,346	-
Net prior service credit reclassification	(478)	-
Deferred cost on forward contract	-	44
Foreign currency translation adjustment	-	(54)
COMPREHENSIVE INCOME	$ 3,040	$ 1,488

See accompanying notes.

THE STANDARD REGISTER COMPANY

CONSOLIDATED BALANCE SHEETS
(Dollars in thousands)

A S S E T S	***April 1, 2007***	***December 31, 2006***
CURRENT ASSETS		
Cash and cash equivalents	$ 1,688	$ 488
Accounts and notes receivable, less allowance for doubtful		
accounts of $1,931 and $2,164	127,274	135,839
Inventories	49,092	49,242
Deferred income taxes	18,635	18,635
Prepaid expense	13,399	13,566
Total current assets	210,088	217,770
PLANT AND EQUIPMENT		
Land	2,354	2,354
Buildings and improvements	66,314	65,408
Machinery and equipment	208,421	210,617
Office equipment	157,058	155,092
Construction in progress	12,695	10,297
Total	446,842	443,768
Less accumulated depreciation	326,911	325,620
Plant and equipment, net	119,931	118,148
Net assets held for sale	-	1,191
Total plant and equipment, net	119,931	119,339
OTHER ASSETS		
Goodwill	6,557	6,557
Intangible assets, net	1,513	1,611

Deferred tax asset		84,797		86,710
Other		21,646		20,092
Total other assets		114,513		114,970
Total assets	$	444,532	$	452,079

See accompanying notes.

THE STANDARD REGISTER COMPANY

CONSOLIDATED BALANCE SHEETS
(Dollars in thousands)

LIABILITIES AND SHAREHOLDERS' EQUITY	***April 1, 2007***	***December 31, 2006***
CURRENT LIABILITIES		
Current portion of long-term debt	$ 224	$ 358
Accounts payable	34,409	36,254
Accrued compensation	17,883	28,050
Deferred revenue	1,998	1,725
Other current liabilities	27,438	34,927
Total current liabilities	81,952	101,314
LONG-TERM LIABILITIES		
Long-term debt	52,355	41,021
Pension benefit obligation	150,739	153,953
Retiree health care obligation	20,448	20,398
Deferred compensation	16,866	17,190
Other long-term liabilities	1,294	36
Total long-term liabilities	241,702	232,598
SHAREHOLDERS' EQUITY		
Common stock, $1.00 par value:		
Authorized 101,000,000 shares		
Issued 2007 - 25,914,869; 2006 - 25,845,304	25,915	25,846
Class A stock, $1.00 par value:		
Authorized 9,450,000 shares		
Issued - 4,725,000	4,725	4,725
Capital in excess of par value	61,149	60,321

Accumulated other comprehensive losses	(137,434)	(141,302)
Retained earnings	216,286	218,278
Treasury stock at cost:		
1,953,895 and 1,949,200 shares	(49,763)	(49,701)
Total shareholders' equity	120,878	118,167
Total liabilities and shareholders' equity	$ 444,532	$ 452,079

See accompanying notes.

THE STANDARD REGISTER COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in thousands)

	13 Weeks Ended April 1, 2007	*13 Weeks Ended April 2, 2006*
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (loss) income	$ (828)	$ 1,498
Cumulative effect of a change in accounting principle	-	(78)
Adjustments to reconcile net (loss) income to net cash provided by operating activities:		
Depreciation and amortization	6,819	8,811
Restructuring charges	2,406	1,213
Asset impairment	(409)	1,694
Pension and postretirement benefit expense	9,032	6,786
Share-based compensation	772	607
Other	(522)	490
Changes in operating assets and liabilities:		
Accounts and notes receivable	8,565	(4,537)
Inventories	150	767
Restructuring spending	(694)	(802)
Accounts payable and accrued liabilities	(14,550)	(9,639)
Pension and postretirement obligation	(5,781)	(4,643)
Other assets and liabilities	(320)	(1,371)
Net cash provided by operating activities	4,640	796
CASH FLOWS FROM INVESTING ACTIVITIES		
Additions to plant and equipment	(8,168)	(5,063)
Proceeds from sale of plant and equipment	141	127
Net cash used in investing activities	(8,027)	(4,936)

CASH FLOWS FROM FINANCING ACTIVITIES		
Net change in borrowings under revolving credit facility	11,355	8
Principal payments on long-term debt	(155)	(151)
Proceeds from issuance of common stock	92	287
Dividends paid	(6,683)	(6,632)
Purchase of treasury stock	(62)	-
Tax benefit from exercise of stock options	-	27
Net cash provided by (used in) financing activities	4,547	(6,461)
Effect of exchange rate changes on cash	40	(59)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	1,200	(10,660)
Cash and cash equivalents at beginning of period	488	13,609
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 1,688	$ 2,949

See accompanying notes.

THE STANDARD REGISTER COMPANY

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Dollars in thousands, except per share amounts)

NOTE 1 BASIS OF PRESENTATION

The accompanying consolidated financial statements include the accounts of The Standard Register Company and its wholly-owned subsidiaries (collectively, the Company) after elimination of intercompany transactions, profits, and balances. The consolidated financial statements are unaudited and have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required for complete annual financial statements and should be read in conjunction with the Company s audited consolidated financial statements and notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

In the opinion of management, all adjustments (consisting only of normal recurring accruals) necessary for a fair presentation have been included. The results for interim periods are not necessarily indicative of trends or of results to be expected for a full year.

Certain prior-year amounts have been reclassified to conform to the current-year presentation.

NOTE 2 RECENTLY ADOPTED AND RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

Effective January 1, 2007, the Company adopted Financial Accounting Standards Board (FASB) Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109, Accounting for Income Taxes. FIN 48 requires that the financial statement effects of a tax position taken or expected to be taken in a tax return to be recognized in the financial statements when it is more likely than not, based on the technical merits, that the position will be sustained upon examination. The cumulative effect of applying FIN 48 was $1,144 and was recorded as an adjustment to the January 1, 2007 balance of retained earnings. See Note 7 Income Taxes.

Effective January 1, 2007, the Company adopted the additional disclosure provisions of Emerging Issues Task Force (EITF) Issue No. 06-03, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement. EITF No. 06-03 permits the presentation of these taxes on either a gross basis (included in revenues and costs) or a net basis (excluded from revenues). The Company classifies sales taxes on a net basis in the Consolidated Statements of Income. Adoption of this EITF did not have an effect on the Company s Consolidated Financial Statements.

In February 2007, the FASB issued Statement of Financial Accounting Standard (SFAS) No. 159, The Fair Value Option for Financial Assets and Financial Liabilities which permits companies to voluntarily choose, at specified election dates, to measure specified financial instruments and other items at fair value on a contract-by-contract basis. Subsequent changes in fair value will be required to be reported in earnings each reporting period. The objective of this election, called the fair value option, is to improve financial reporting by providing companies with the means to reduce the volatility in reported earnings caused by measuring related assets and liabilities differently, without using the complex hedge-accounting requirements of SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities. SFAS No. 159 is effective for financial statements issued for fiscal years beginning after November 15,

2007 and therefore is effective for the Company in fiscal year 2008. The Company is currently assessing the effect of implementing this standard, which will be dependent upon the nature and extent of eligible items elected to be measured at fair value at the time of adoption.

NOTE 3 DISCONTINUED OPERATIONS

In March 2007, the Company committed to a plan to sell Digital Solutions, a reportable segment, and concluded it met the criteria to be classified as a discontinued operation held for sale under SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. This start-up venture has successfully applied digital writing technology to enable the user to directly and accurately translate handwriting on paper to digital format for input into software applications, eliminating scanning or keypunching. The software is used by customers in various business applications. Additional capital will be required to continue to develop the product and market and the Company elected to direct its investments to its core document services businesses. The sale to EXPED, LLC was completed on April 21, 2007 and the Company will record a pretax gain of approximately $1,500 in the second quarter of 2007.

On June 5, 2006, the Company sold 100% of the outstanding capital stock of InSystems Corporation (InSystems) to Whitehill Technologies, Inc. The sale of InSystems, a reportable segment since its acquisition in 2002, also met the criteria to be accounted for as discontinued operations under SFAS No. 144.

The results of operations for Digital Solutions and InSystems have been excluded from continuing operations in the accompanying Consolidated Statements of Operations. InSystems revenue included in discontinued operations for the 13-week period ended April 2, 2006 was $3,035. Revenue for Digital Solutions included in discontinued operations was $405 and $102 for the 13-week periods ending April 1, 2007 and April 2, 2006, respectively. Cash flows related to discontinued operations are not separately disclosed in the Consolidated Statements of Cash Flows. No interest expense was allocated to discontinued operations.

NOTE 4 RESTRUCTURING AND IMPAIRMENT CHARGES

The Company has undertaken restructuring actions as part of an on-going effort to improve its utilization and profitability. Previous restructuring plans are more fully described in Note 3 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006. All costs related to restructuring actions are included in restructuring charges in the accompanying Consolidated Statements of Income.

Pre-tax components of restructuring charges are as follows:

	13 Weeks Ended	
	April 1, 2007	***April 2, 2006***
2007 Restructuring Actions		
Severance and employer related costs	**$ 1,733**	$ -
Associated costs	**673**	-
Total 2007	**2,406**	-
2006 Restructuring Actions		
Severance and employer related costs	**-**	689
Associated costs	**-**	206
Total 2006	**-**	895
2004 Contract exit and termination costs	**-**	10
2003 Contract exit and termination costs	**-**	52
2001 Contract exit and termination costs	**-**	133
Total restructuring expense	**$ 2,406**	$ 1,090

2007 Restructuring

In 2007, the Company is taking steps to align its supply chain with market opportunities and customer needs. The Company plans to organize and consolidate its manufacturing and distribution capabilities to become more efficient in meeting customer needs. On January 25, 2007, the Company adopted a restructuring plan to accomplish these objectives. The actions associated with the plan are expected to be completed in 2007.

In connection with this plan, on January 26, 2007, the Company announced that it will close its facility in Middlebury, Vermont, and transfer equipment and production operations to three other plants. The Middlebury plant, which is part of the Document and Label Solutions (DLS) segment, will continue to perform limited production through May 2007.

The Company expects to record approximately $4,900 of restructuring costs in the DLS segment in 2007 related to the closing of the Middlebury plant. Restructuring costs will include $1,850 for employee related costs and $3,050 of other associated exit costs, primarily for equipment removal and relocation, employee relocation, and inventory write-offs. The Company projects estimated savings from the plant closure in the range of $4,000 to $5,000 on an annualized basis.

Pre-tax components of 2007 restructuring charges are as follows:

	Total Costs Expected to be Incurred	***Total Q1 2007 Restructuring Expense***	***Cumulative-To-Date Restructuring Expense***
Severance and employer related costs	$ 1,850	$ 1,733	$ 1,733
Associated costs	3,050	673	673
Total	$ 4,900	$ 2,406	$ 2,406

A summary of the 2007 restructuring accrual activity is as follows:

	Charged to Accrual	*Incurred in 2007*	*Balance 2007*
Severance and employer related costs	$ 1,733	$ (21)	$ 1,712
Total	$ 1,733	$ (21)	$ 1,712

2006 Restructuring

Within the DLS segment, the Company closed its Terre Haute, Indiana label production plant in 2006. The plant s productive capacity was transferred to three other plants to improve overall efficiency and lower operating costs. Costs incurred included severance and employer related costs and other associated costs directly related to the restructuring, primarily equipment removal and relocation. All of the actions were completed at the end of 2006.

2004, 2003, and 2001 Restructuring

All of the 2004, 2003, and 2001 restructuring actions are completed. Any restructuring expense recorded in 2006 for these actions was primarily related to vacated facilities, as the amount accrued was net of any expected sub-lease income and the Company was unable to sublease the facilities.

Asset Impairment and Net Assets Held for Sale

At April 1, 2007, the Middlebury plant was being marketed for sale at the direction of management, but did not meet all the criteria to be classified as held for sale in accordance with SFAS No. 144. At December 31, 2006, the Company had concluded that it was more likely than not that a plant would be closed in the DLS segment which caused the Company to perform an impairment test on the long-lived assets. This resulted in the Company recording an asset impairment charge in 2006 to adjust the carrying values to their fair value less costs to sell, considering the most recent information available including recent sales of similar properties. The market is more competitive than expected and the Company has received several offers for the purchase of the Middlebury building that are higher than originally anticipated. As a result, the Company reversed $409 of the impairment charge recorded in 2006 to adjust the building s carrying amount.

In conjunction with the closing of the Terre Haute plant, in the first quarter of 2006 the Company recorded $1,667 of asset impairments, primarily related to equipment. The carrying value of the Terre Haute building and equipment was adjusted to its estimated fair value less costs to sell, considering recent sales of similar properties and real estate valuations. Other equipment was determined to have no fair value and was disposed of. As of December 31, 2006, the Terre Haute building was classified as held for sale and was subsequently sold in January 2007.

An additional $27 of impairment charges were recorded in the International Segment in the first quarter of 2006.

NOTE 5 INVENTORIES

The components of inventories are as follows:

	April 1, 2007	***December 31, 2006***

Finished products	**$**	**43,050**	$	41,739
Jobs in process		**1,758**		3,216
Materials and supplies		**4,284**		4,287
Total	**$**	**49,092**	$	49,242

NOTE 6 OTHER CURRENT LIABILITIES

Other current liabilities consist of the following:

		April 1, 2007		***December 31, 2006***
Non-income taxes	**$**	**6,427**	$	7,062
Dividends payable		**-**		6,663
Current portion of pension and postretirement obligations		**3,954**		3,954
Other current liabilities		**17,057**		17,248
Total	**$**	**27,438**	$	34,927

NOTE 7 INCOME TAXES

The Company adopted the provisions of FIN 48 on January 1, 2007. As a result, the Company recorded a liability of $1,144 for unrecognized tax benefits, including accrued interest, which was accounted for as a reduction to the beginning balance of retained earnings. The total amount represents unrecognized tax benefits that, if recognized, would favorably affect the effective income tax rate in any future periods.

The Company and its subsidiaries file income tax returns in the U.S. federal jurisdiction and various state and Canadian jurisdictions. The Company has substantially concluded all U.S. federal income tax matters for years through 1997. No federal income tax returns are currently under examination. With few exceptions, the Company is no longer subject to state, and local, or non-U.S. income tax examinations by tax authorities for years before 2003.

The Company s continuing policy is to recognize interest and penalties related to income tax matters in tax expense. The amount of interest and penalty expense recorded for the 13-week periods ending April 1, 2007 and April 2, 2006 or accrued at April 1, 2007 was immaterial.

NOTE 8 EARNINGS PER SHARE

The number of shares outstanding for calculation of earnings per share (EPS) is as follows:

	13 Weeks Ended	
(Shares in thousands)	***April 1, 2007***	***April 2, 2006***
Weighted average shares outstanding - basic	**28,635**	28,877
Effect of potentially dilutive securities	**-**	108
Weighted average shares outstanding - diluted	**28,635**	28,985

The effects of stock options and unvested shares on diluted EPS are reflected through the application of the treasury stock method. Outstanding options to purchase approximately 1,803,000 shares at April 2, 2006 were not included in the computation of diluted EPS because the exercise prices of the options were greater than the average market price of the shares; therefore, the effect would be anti-dilutive. Due to the loss from continuing operations for the 13-week period ending April 1, 2007, no outstanding options were included in the diluted EPS computation because they would automatically result in anti-dilution.

NOTE 9 SHARE BASED COMPENSATION

The terms and conditions of outstanding awards previously granted are more fully described in Note 12 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

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Total share-based compensation expense by type of award is as follows:

	13 Weeks Ended	
	April 1 2007	***April 2, 2006***
Restricted stock awards, service based	**$ 345**	$ 366
Restricted stock awards, performance based	**330**	168
Stock options	**97**	73
Total share-based compensation expense	**772**	607
Tax effect on share-based compensation expense	**306**	238
Net effect included in continuing operations	**$ 393**	$ 296
Net effect included in discontinued operations	**$ 73**	$ 73

Stock Options

The weighted average fair value of stock options granted in the first quarter of 2007 was estimated at $2.51 per share, using the Black-Scholes option-pricing model. The assumptions used to calculate fair value include a weighted-average: risk-free interest rate of 4.3%; dividend yield of 7.0%; expected life of 4 years; and expected volatility of 37.6 %. As of April 1, 2007, there was a total of $1,801 of share-based compensation related to stock options that will be amortized to expense over a weighted-average remaining service period of 2 years.

A summary of the Company s stock option activity and related information for 2007 is as follows:

	Number of Shares	***Weighted-Average Exercise Price***
Outstanding at December 31, 2006	**2,339,930**	**$ 19.60**
Granted	**396,000**	**13.07**
Exercised	**(1,000)**	**12.63**
Canceled	**(89,956)**	**21.27**
Outstanding at April 1, 2007	**2,644,974**	**$ 18.57**
Exercisable at April 1, 2007	**1,895,110**	**$ 20.35**

Restricted Stock Awards

The Company awarded restricted stock to certain of its employees in 2007 that vest based on service requirements. The fair value of the service-based restricted stock awards granted was based on the closing market price of the

Company s common stock on the date of award and is being amortized to expense over a vesting period of 4 years.

A summary of the Company s restricted stock activity and related information for 2007 is as follows.

	Number of Shares	***Weighted-Average Grant Date Fair Value***	
Nonvested at December 31, 2006	**345,932**	**$**	**14.05**
Granted	**31,420**		**13.07**
Vested	**(62,250)**		**15.32**
Canceled	**(2,800)**		**13.85**
Nonvested at April 1, 2007	**312,302**	**$**	**13.70**

NOTE 10 PENSION PLANS

The Company has a qualified defined benefit plan and a nonqualified supplementary benefit plan that provides supplemental pension payments in excess of qualified plan payments. In addition, the Company has a noncontributory supplemental nonqualified retirement plan for elected officers and a supplemental retirement agreement with its President and Chief Executive Officer under which he is entitled to receive supplemental retirement benefits upon attainment of certain age and employment requirements. These plans are more fully described in Note 13 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

Net periodic benefit cost includes the following components:

	13 Weeks Ended	
	April 1, 2007	***April 2, 2006***
Service cost of benefits earned	**$ 2,215**	$ 2,059
Interest cost on projected benefit obligation	**7,210**	6,857
Expected return on plan assets	**(7,116)**	(7,284)
Amortization of prior service costs	**90**	90
Amortization of net loss from prior periods	**7,026**	6,010
Total	**$ 9,425**	$ 7,732

The Company does not have a minimum funding requirement in 2007. The Company made $5,000 of voluntary contributions to the qualified pension plan in the first quarter of 2007 and $4,000 in the same period of 2006.

NOTE 11 POSTRETIREMENT BENEFITS OTHER THAN PENSION

In addition to providing pension benefits, the Company provides certain healthcare benefits for eligible retired employees as described in Note 14 to the Consolidated Financial Statements included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

Postretirement benefit cost includes the following components:

	13 Weeks Ended	
	April 1, 2007	***April 2, 2006***
Service cost	**$ -**	$ -
Interest cost	**307**	297
Amortization of prior service cost	**(884)**	(884)
Amortization of net loss from prior periods	**184**	154

Total	**$**	**(393)**	$	(433)

The funding policy is to pay claims as they occur. Payments for postretirement health benefits, net of retiree contributions, were approximately $258 and $506 for the first quarter of 2007 and 2006, respectively.

NOTE 12 SEGMENT REPORTING

The Document Systems operating segment previously included in Other now meets the quantitative thresholds for reportable segments. Segment information for 2006 has been revised from previously reported information to reflect the current presentation. The segments are managed and reported internally primarily by the type of products they produce and the services they provide.

Document and Label Solutions

Document and Label Solutions offers document printing and label solutions including custom-printed documents; document design; labels; secure document solutions; warehouse, freight, and distribution services; business supplies; and conversion management. Document and Label Solutions consists of five business units that have been aggregated for segment reporting purposes.

POD Services

The types of products and services POD Services offers include high-end digital color or black/white, short-run, quick print production (print-on-demand), billing and statement solutions, one-to-one marketing communications (variable print-on-demand), Web-based information request fulfillment, and customer information kits (cards, policies, statements, manuals, etc.) POD Services consists of two business units that have been aggregated for segment reporting purposes.

Document Systems

Document Systems generates revenue from licensing the rights to software products, revenue from maintenance and other customer support services, and revenue from professional services associated with the licensing of software. In additional Document Systems generates revenue from the sale of related hardware equipment such as printers.

Information about the Company s operations by segment for the 13-week periods ended April 1, 2007 and April 2, 2006 is as follows:

		Document and Label Solutions	***POD Services***	***Document Systems***	***Other***	***Total***
Revenue from external customers	**2007**	**$ 140,788**	**$ 70,181**	**$ 6,149**	**$ 10,313**	**$ 227,431**
	2006	148,780	65,212	5,271	9,258	228,521
	2007	**$ 2,491**	**$ 7,511**	**$ 1,119**	**$ (1,521)**	**$ 9,600**
Operating income (loss)	2006	9,119	4,465	1,207	(426)	14,365
Total assets	**2007**	**$ 225,811**	**$ 75,552**	**$ 6,253**	**$ 8,378**	**$ 315,994**

Reconciling information between reportable segments and the Company s consolidated financial statements is as follows:

	13 Weeks Ended	
	April 1, 2007	***April 2, 2006***
Operating income	**$ 9,600**	$ 14,365
Restructuring and asset impairment	**(1,997)**	(2,784)

Amortization of prior period pension losses	**(7,026)**	(6,010)
Other unallocated pension	**94**	(427)
Corporate and other unallocated	**(261)**	853
LIFO adjustment	**(45)**	(551)
Total other expense, primarily interest	**(729)**	(478)
(Loss) income from continuing operations before income taxes	**$ (364)**	$ 4,968
Total Assets	**$ 315,994**	
Corporate and unallocated	**128,538**	
Total consolidated assets	**$ 444,532**	

Item 2 -

MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS *(Dollars in Millions, Except Per Share Amounts)*

FORWARD-LOOKING INFORMATION

This report includes forward-looking statements covered by the Private Securities Litigation Reform Act of 1995. A forward-looking statement is neither a prediction nor a guarantee of future events or circumstances, and those future events or circumstances may not occur. All statements regarding our expected future financial condition, revenues or revenue growth, projected costs or cost savings, cash flows and future cash obligations, dividends, capital expenditures, business strategy, competitive positions, growth opportunities for existing products or products under development, and objectives of management are forward-looking statements that involve certain risks and uncertainties. In addition, forward-looking statements include statements in which we use words such as anticipates, projects, expects, plans, intends, believes, estimates, targets, and other similar expressions that indicate tre future events. These forward-looking statements are based on current expectations and estimates; we cannot assure you that such expectations will prove to be correct. The Company undertakes no obligation to update forward-looking statements as a result of new information, since these statements may no longer be accurate or timely.

Because such statements deal with future events, actual results for fiscal year 2007 and beyond could differ materially from our current expectations depending on a variety of factors including, but not limited to, the risk factors discussed in Item 1A to Part I of the Company s Form 10-K for the year ended December 31, 2006.

OVERVIEW

The Company We are a leading document services provider that helps our customers manage, control and source their document and print-related spending. We primarily serve the healthcare, financial services, and manufacturing industries.

We are a document services company entrusted by our customers to manage business-critical documents with a variety of products and professional services. Our strategy is to provide a full spectrum of solutions including printing solutions, label solutions, print-on-demand services, document automation, outsourcing and managed services, and professional services.

Our Enterprise Document Management approach includes analysis of where, how - and even if - documents should be printed. This document study includes everything from forms, stationery and reports to four-color marketing collateral and also addresses what is printed internally as well as externally. By improving the efficiency of these processes and applying appropriate sourcing strategies, customers are able to save on their entire document-related supply chain costs.

Our solutions give customers the tools to manage the entire lifecycle of their documents from concept to delivery. We make a measurable difference for our customers by helping them achieve their desired business outcomes by assisting them with reducing costs; transitioning to more efficient processes; effectively managing their risks and meeting their regulatory and industry requirements; and driving their business growth.

Our operations include three reportable segments: Document and Label Solutions (DLS), Print-on-Demand (POD) Services, and Document Systems.

Our Business Challenges The market for many of our traditional printed products is very price competitive. In order to maintain or improve our margins in these segments, we must execute our plans to gain market share, improve productivity, and increase the sale of related value-added software and services.

Paper mill operating rates were reported in the 92%-93% range during 2006, which served to support increases in paper prices. The expectation is that mills will continue to reduce capacity during 2007 in an attempt to offset expected weakness in overall paper demand and pricing. The paper companies have announced price increases on cut sheet papers, to become effective in the market in May 2007. If the increases hold up, it is possible that this increase may spread to roll papers, although at this time no increase has been attempted.

Despite a competitive marketplace, we have traditionally been successful in recovering all or most of the increases in paper costs. Recovery ordinarily occurs over a period of several quarters. We would expect to increase our selling prices to our customers to recover paper cost increases that take place in 2007.

It is likely that the increasing use of reverse auctions and other bidding tools will gain in popularity and may lower the prices of our printed products.

Our pension plan became underfunded in late 2002, primarily as a result of lower interest rates and weak stock market returns in 2001 and 2002. The amortization of these and other actuarial losses has resulted in significant expense in subsequent years equivalent to $0.54 per share in 2006 and $0.15 per share in the first quarter of 2007. We have continued to make voluntary cash contributions to our qualified pension plan, averaging approximately $17.4 million annually over the last five years; we plan to make voluntary contributions in 2007 of approximately $20 million.

Our Focus Our objective is to continue to improve the sales trend in our core document business by taking market share in targeted accounts and vertical markets where we have a strong reputation and value proposition. We will continue to reduce costs and improve productivity in order to stay cost competitive.

We plan to address the large and growing market to provide digital print-on-demand output, including color and variable print. Services that provide the customer with added convenience, design capability and control over the process are expected to be a strong differentiator. We plan to step up the level of investment in our POD Services business in order to ensure that we catch the building market momentum in this important growth segment. This will translate into higher capital expenditures and selling, general and administrative expenses in the coming quarters.

We intend to continue to bring our customers products and services that improve their ability to cost-effectively capture, manage and move information. Over time, services will become an increasing share of our revenue stream.

On January 25, 2007, the Company adopted a restructuring to organize and consolidate its manufacturing and distribution capabilities to become more efficient in meeting customer needs. The actions associated with the plan are expected to be completed in 2007.

We expect to continue to focus on maintaining our current strong financial condition.

CRITICAL ACCOUNTING POLICIES

In preparing these unaudited financial statements and accounting for the underlying transactions and balances, we applied the accounting policies disclosed in the Notes to the Consolidated Financial Statements contained in our Annual Report on Form 10-K for the year ended December 31, 2006. Preparation of these unaudited financial statements requires us to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Although we believe our estimates and assumptions are reasonable, they are based on information presently available and actual results may differ significantly from those estimates.

We believe that some of the more critical estimates and related assumptions are in the areas of pension and postretirement healthcare benefits, impairment of long-lived assets, deferred taxes, inventories, contingent liabilities, and share-based compensation. For a detailed discussion of these critical accounting estimates, see the Management Discussion and Analysis included in our Annual Report on Form 10-K for the year ended December 31, 2006.

We have discussed the development and selection of the critical accounting policies and the related disclosures included herein with the Audit Committee of the Board of Directors.

Pension Benefit Plans

Included in our financial results are significant pension obligations and benefit costs and credits which are measured using actuarial valuations. The use of actuarial models requires us to make certain assumptions concerning future events that will determine the amount and timing of the benefit payments.

Our defined benefit pension plans permit retirees to receive a lump sum payment upon retirement. When the total lump sum payments for a year exceed total service and interest costs recognized for that year, we are required to record a non-cash charge, referred to as a pension settlement, to record in earnings a pro-rata portion of the actuarial

losses. Based on information currently available to us, we expect to record a non-cash settlement charge in 2007 related to our non-qualified supplementary benefit plan. This non-cash charge would not affect total equity, as the amount will be reclassified from comprehensive income.

Deferred Taxes

Effective January 1, 2007, the Company adopted Financial Accounting Standards Board (FASB) Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109, Accounting for Income Taxes. FIN 48 requires that the financial statement effects of a tax position taken or expected to be taken in a tax return are to be recognized in the financial statements when it is more likely than not, based on the technical merits, that the position will be sustained upon examination. As a result, the Company recorded a liability of $1.1 million for unrecognized tax benefits, including accrued interest, which was accounted for as a reduction to the beginning balance of retained earnings.

Significant management judgment is required in evaluating tax positions taken or to be taken in our tax returns. We evaluate all available evidence to determine whether it is more likely than not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The $1.1 million represents unrecognized tax benefits that, if recognized, would favorably affect the effective income tax rate in any future periods.

RESULTS OF OPERATIONS

Discontinued Operations

In March 2007, the Company committed to a plan to sell Digital Solutions, a reportable segment, and concluded it met the criteria to be classified as a discontinued operation held for sale under SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. This start-up venture has successfully applied digital writing technology to enable the user to directly and accurately translate handwriting on paper to digital format for input into software applications, eliminating scanning or keypunching. The software is used by customers in many business applications. Additional capital will be required to continue to develop the product and market and the Company elected to direct its investments to its core document services businesses. The sale to EXPED, LLC was completed on April 21, 2007.

On June 5, 2006, the Company sold 100% of the outstanding capital stock of InSystems Corporation (InSystems) to Whitehill Technologies, Inc. The sale of InSystems, a reportable segment since its acquisition in 2002, also met the criteria to be accounted for as discontinued operations under SFAS No. 144.

The results of operations have been excluded from continuing operations in the accompanying Consolidated Statements of Operations. Cash flows related to discontinued operations are not separately disclosed in the Consolidated Statements of Cash Flows. Revenue, and results of operations for these discontinued operations appear in the table below.

		2007		***2006***
Revenue				
InSystems	$	-	$	3.0
Digital Solutions		0.4		0.1
Total	$	0.4	$	3.1
Loss from Discontinued Operations, net of tax				
InSystems	$	-	$	(0.7)
Digital Solutions		(0.6)		(0.8)
Total	$	(0.6)	$	(1.5)

Continuing Operations

The discussion that follows provides information which we believe is relevant to an understanding of our consolidated results of operations and financial condition, supplemented by a discussion of segment results where appropriate. The discussion and analysis should be read in conjunction with the accompanying consolidated financial statements and notes thereto.

The discussion includes non-GAAP financial measures that exclude asset impairments, restructuring charges, and pension loss amortization. Generally, a non-GAAP financial measure is a numerical measure of a company s performance, financial position, or cash flows where amounts are either excluded or included not in accordance with generally accepted accounting principles (GAAP). We believe that the non-GAAP financial measures presented will enhance the understanding of our results of operations due to the non-operational nature of the identified items and the significant and varying effect they have on our reported results from period to period. This presentation is consistent with the manner in which our Board of Directors internally evaluates performance and establishes incentives. This non-GAAP information is not meant to be considered in isolation or as a substitute for results prepared in accordance with accounting principles generally accepted in the United States.

Unless otherwise noted, references to 2007 and 2006 refer to the 13-week periods ended April 1, 2007 and April 2, 2006.

Consolidated Overview

Consolidated revenue in the first quarter of 2007 was $227.4 million, down 0.5% from the prior year. Revenue for our DLS segment was down 5.4%, reflecting a continuing decline in the use of traditional business forms. Conversely, POD Services revenue was up 7.6%, Document Systems revenue rose 16.7%, and revenue for our other segments, primarily Commercial Print, were up a collective 11.4%. The revenue composition for the first quarter continued the shift away from traditional long-run printed documents and toward on-demand, digitally-produced documents, sophisticated software applications, and high value-added services.

Consolidated pretax income from continuing operations decreased from $5.4 million in the first quarter of 2006 to $0.4 million in the current quarter. Restructuring, impairment, and amortization of past pension net losses were substantial in both periods. We evaluate our financial performance primarily on operating income before restructuring, impairment, and pension loss amortization. On this basis, pretax income from continuing operations was $9.4 million in the current quarter versus $14.2 million in the prior year, as indicated in the table below.

	2007	2006	Change
Income from Continuing Operations	**$ 0.4**	**$ 5.4**	**$ 5.0**
Asset impairments	(0.4)	1.7	2.1
Restructuring charges	2.4	1.1	(1.3)
Amortization of prior period pension losses	7.0	6.0	(1.0)
Total Pre-tax Operating Income, excluding the above	**$ 9.4**	**$ 14.2**	**$ 4.8**

The $4.8 million decrease above is attributed primarily to a $5.9 million drop in the gross margin due to a revenue decrease from a major account in mid-2006 and higher DLS manufacturing costs primarily related to the restructuring action now underway. Total Company expenses for 2007, including depreciation and amortization, and selling, general, and administrative expenses were lower than the same quarter of the prior year.

Revenue, Gross Margin, and Operating Income (Loss) by Segment

We evaluate each of our segments on the same basis-prior to restructuring, impairment, and amortization of past pension losses. For segment reporting, we also exclude LIFO inventory adjustments. The actual cost of sales and depreciation are recorded for each segment and a selling, general and administrative expense (SG&A) allocation is made based on an evaluation of each segment s utilization of our selling, support, and engineering resources.

The tables below present revenue, gross margin, and income (loss) from operations for each of our reportable segments. The Document Systems operating segment previously included in Other, now meets the quantitative thresholds for reportable segments.

	2007	% Change	**2006**
Revenue			
Document & Label Solutions	$ **140.7**	-5.4%	$ **148.8**
Print On Demand Services	**70.2**	7.6%	**65.2**
Document Systems	**6.1**	16.7%	**5.3**
Other	**10.4**	11.4%	**9.2**
Total Segments	$ **227.4**	-0.5%	$ **228.5**

	2007	% Revenue	**2006**	% Revenue
Gross Margin *				

Document & Label Solutions	$	**42.2**	30.0%	$	**51.3**	34.5%
Print On Demand Services		**29.1**	41.4%		**26.2**	40.2%
Document Systems		**2.8**	45.9%		**2.9**	54.7%
Other		**1.8**	17.3%		**2.0**	21.7%
Total Segments	$	**75.9**	33.4%	$	**82.4**	36.1%

		2007	% Revenue		**2006**	% Revenue
Operating Income (Loss) *						
Document & Label Solutions	$	**2.5**	1.8%	$	**9.1**	6.1%
Print On Demand Services		**7.5**	10.7%		**4.5**	6.9%
Document Systems		**1.1**	18.0%		**1.2**	22.6%
Other		**(1.5)**	-14.4%		**(0.4)**	-4.3%
Total Segments*	$	**9.6**	4.2%	$	**14.4**	6.3%
LIFO Adjustments	$	**-**		$	**(0.6)**	
Other Unallocated		**(0.2)**			**0.4**	
Consolidated	$	**9.4**		$	**14.2**	

*Segment gross margin and operating income (loss) before unallocated items. See reconciliation to consolidated net (loss) income on page 19.

Document & Label Solutions

Total DLS revenue in the first quarter of 2007 was $140.7 million, down $8.1 million or 5.4% compared to the same period of 2006. Label revenue was $31.6 million, down 1.6%, and traditional forms, supplies, and related services that comprise the balance of DLS were $109.1 million, down 6.8%. The decrease in traditional business forms reflects the effects of software and Internet technologies that substitute for some paper documents, continuing pricing pressures, plus the migration from longer-run traditional offset print to on-demand digitally printed documents.

Overall DLS unit sales were down approximately 8% while average selling prices were about 2.4% higher, the latter related to the recovery of higher paper costs.

DLS gross margin in the first quarter of 2007 was down $9.1 million, or 4.5 percentage points, in relation to revenue versus the first quarter 2006. It is noteworthy that the first quarter 2006 had a particularly strong mix of business, which produced the highest gross margin of 2006. Notwithstanding this fact, the quarter s 30% gross margin was relatively weak when compared to the 32.8% average recorded for all of 2006. The decline in unit sales is estimated to account for about $5.5 million of the decrease in the gross margin. Other contributing factors included high material, overtime, quality, and maintenance related in major part to the closure of the Middlebury Plant announced in January of this year. The restructuring plan is expected to generate $4 to $5 million in annual savings when completed.

The $6.6 million decline in DLS operating profit versus last year resulted from the above decline in gross margin, mitigated by lower depreciation and allocated operating expenses.

POD Services

POD Services revenue was up $5.0 million, or 7.6%, on the strength of gains in digital printed business documents, marketing communications, statement printing, and services. Services, which increased 26.3% in the quarter, include kitting, custom programming, design, and facilities management.

This quarter s increase continues the trend of growth in this segment which reported 8.4% growth for all of 2006. Management continues to believe that there are good growth opportunities in this segment and is stepping up the Company s investment in digital production capacity, enabling workflow software, and related service offerings.

The gross margin increased by $2.9 million in 2007 compared to the comparable quarter of 2006. As a percentage of revenue, the gross margin was 41.4% versus 40.2% in the prior year. The improvement reflects the increase revenue and associated plant absorption, plus the success of various cost reduction initiatives.

Operating profit was up $3.0 million to $7.5 million, or 10.7% of revenue, attributed primarily to the improved gross margin.

Document Systems

Document Systems reported revenue of $6.1 million, up 16.7 % compared to the first quarter 2006. Document Systems develops and markets software that automates the printing of documents within the customer s place of business. Hospitals are a primary market for this software and the application coexists nicely with other applications in hospitals that are moving to automate patient records and other paper intensive processes. This segment also provides professional services, software maintenance, and hardware.

The quarter s gross margin and operating profit were 45.9% and 18.0% of revenue, respectively, which provide the income necessary for continued software development and other strategic initiatives.

Paper Costs

The paper companies have announced price increases on cut sheet papers, to become effective in the market in May 2007. It is possible that this increase may spread to roll papers, although at this writing no increase has been attempted. We plan to adjust our target selling prices to our customers in an effort to recoup these cost increases. We have generally been able to pass through these paper costs increases, although it often takes several quarters owing to the custom nature of our products and our contractual relationships with many of our customers.

2007 Revenue

We continue to believe that the Company will report overall revenue growth for 2007 in the low to mid single-digit range.

Selling, General, and Administrative (SG&A) Expenses

Total SG&A expense was $66.9 million in the quarter, compared to $66.2 million in the prior year. The amortization of past years pension losses was $7.0 million in the current quarter versus $6.0 million in the first quarter 2006. This amortization relates primarily to stock market declines in 2001 and 2002 which lowered pension assets, plus lower interest rates in that same period that raised the pension liability. Excluding this amortization, SG&A expense was slightly down in the quarter.

Depreciation & Amortization

Depreciation and amortization was lower in the quarter - $6.7 million this quarter versus $7.3 million a year ago. This decrease reflects a strategic shift away from an asset intensive business model to one based increasingly on services. Our capital spending in the 2007 first quarter was higher than last year s run-rate and primarily reflects increased spending to support the POD business plan. Capital spending is expected to be in the $25 million to $28 million range for 2007 and depreciation is expected to be approximately $27 million.

Interest Expense

Interest expense was $0.8 million in the quarter, compared to $0.5 million last year. The increase relates primarily to higher debt balances carried during the 2007 first quarter versus the same period of 2006.

Income (Loss) from Continuing Operations

The following table reconciles income from continuing operations before restructuring, asset impairment, and pension loss amortization to income (loss) from continuing operations and net income on a GAAP basis.

	Effect On Income	
	2007	***2006***
Segment Operating Income	**$ 9.6**	**$ 14.4**
LIFO adjustment	-	(0.6)
Corporate and other unallocated	(0.2)	0.8
Other unallocated pension	-	(0.4)
	9.4	**14.2**
Reconciliation to Net (Loss) Income		
Restructuring and asset impairments	(2.0)	(2.8)
Amortization of prior period pension losses	(7.0)	(6.0)

Income on Continuing Operations	**0.4**	**5.4**
Interest and other income (expense)	(0.8)	(0.5)
Pre-tax (Loss) Income	**(0.4)**	**4.9**
Income tax adjustments		
Income Taxes	(0.2)	2.0
Net (Loss) Income on Continuing Operations	**(0.2)**	**2.9**
Discontinued Operations	(0.6)	(1.5)
Cumulative Effect of Change in Accounting Principle	-	0.1
Net (Loss) Income	**$ (0.8)**	**$ 1.5**

EPS on Continuing Operations Attribution

Restructuring and impairment	$ .25; MARGIN-RIGHT: 0pt" align="justify">	

Not applicable.

Item 2. DESCRIPTION OF PROPERTY.

We currently lease 15,680 square feet of office, laboratory and warehouse space located at 1241 and 1261 Hawk's Flight Court, El Dorado Hills, California, a 2,000 square foot office facility at 1901 Conant Avenue, Burly, Idaho, a 1264 square foot office facility at 6991 East Camelback Road, Scottsdale, Arizona and a 17,000 square foot warehouse facility at 1755 Enterprise Boulevard, West Sacramento, California. Our subsidiary, RiceX Nutrients, Inc., owns a 15,700 square foot production facility in Dillon, Montana. The lease for the El Dorado Hills facility expires in April 2007. In April 2007 we will move our corporate headquarters to 5090 North 40th Street, Phoenix, Arizona where we have entered into a five year lease for the 26,147 square-foot office.

We believe that our facilities are adequate for our anticipated needs through 2007 but we anticipate the Company will need to add additional space for 2008. The properties are adequately covered by insurance. We plan to build another production facility in 2007 to meet anticipated needs in 2008.

Item 3. LEGAL PROCEEDINGS.

As previously disclosed, NutraCea commenced a lawsuit on September 8, 2006 against Langley Park Investments, PLC, a United Kingdom Corporation ("Langley") in the United States District Court for the Eastern District of California, Sacramento Division. The factual basis underlying that case involved a private-placement transaction in which NutraCea exchanged 7 million restricted shares of its common stock for 1,272,026 ordinary shares of Langley common stock (the "Langley Shares"), half of which were immediately saleable by NutraCea and half of which were placed in escrow subject to certain conditions. After the commencement of the litigation, the parties entered into a Pre-Settlement/Escrow Agreement, pursuant to which they agreed that the proceeds from Langley's sale of certain NutraCea shares, totaling $2.5 million, would be deposited into an escrow account. The matter has now been settled. Pursuant to the settlement, NutraCea will receive $1.25 million from the $2.5 million held in escrow (Langley will receive the remainder), and NutraCea will retain all of the Langley Shares.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS.

Not applicable.

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PART II

Item 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

PRICE RANGE OF COMMON STOCK

Our common stock currently trades on the OTC Bulletin Board ("OTCBB") exchange under the symbol "NTRZ.OB". The following table sets forth the range of high and low closing sales prices for our common stock as reported on the OTCBB for the periods indicated below. The quotations below reflect inter-dealer prices, without retail mark-up, markdown or commission, and may not represent actual transactions.

NUTRACEA COMMON STOCK	Low	High
Year Ended December 31, 2006		
Fourth Quarter	$ 1.30	$ 2.74
Third Quarter	$ 0.80	$ 1.38
Second Quarter	$ 0.60	$ 1.45
First Quarter	$ 0.65	$ 1.42
Year Ended December 31, 2005		
Fourth Quarter	$ 0.65	$ 1.17
Third Quarter	$ 0.39	$ 1.81
Second Quarter	$ 0.39	$ 0.65
First Quarter	$ 0.30	$ 0.67

HOLDERS

As of March 2, 2007, there were approximately 303 holders of record of our common stock.

DIVIDENDS

We have never declared or paid any cash dividends on our common stock. We currently anticipate that we will retain all future earnings for the expansion and operation of our business and do not anticipate paying cash dividends in the foreseeable future.

RECENT SALES OF UNREGISTERED SECURITIES

During the three months ended December 31, 2006, we issued the following securities without registration under the Securities Act of 1933:

Common Stock:

Four stockholders converted 2,680 shares of Series B Convertible Preferred Stock into 5,360,000 shares of our common stock. The preferred shares converted at a conversion rate of 2,000 shares of common stock for each preferred share. No additional consideration was paid to convert the preferred shares.

Twelve stockholders converted 5,238 shares of Series C Convertible Preferred Stock into 6,162,341 shares of our common stock. The preferred shares converted at a conversion rate of approximately 1,176 shares of common stock for each preferred share. No additional consideration was paid to convert the preferred shares.

Ten individuals exercised warrants and received a total of 5,335,064 shares of our common stock for the aggregate exercise price of $5,611,588.

Options and Warrants:

We issued to six employees options to purchase an aggregate 370,000 shares of commons stock, which start to vest 90 days after their date of employment and vest over two years. The options expire 10 years from the dates of grant and have a per share exercise price ranging from $1.39 to $2.38.

We issued to a medical advisor to the board of directors an option to purchase 240,000 shares of common stock. The shares will vest monthly over a 12 month period. The option expires three years from the date of the grant and has a per share exercise price of $1.63. The medical advisor resigned for personal reasons prior to the completion of his term and 120,000 of the option shares that were unvested at the time of his resignation have been cancelled.

We issued to a consultant a warrant to purchase 25,000 shares of common stock. The shares will vest over a five month period. The warrant expires three years from the date of the grant and has a per share exercise price of $2.30.

We issued to three entities incentive and performance warrants to purchase 275,000 shares of common stock. The shares will vest at various intervals when certain benchmarks are achieved. The warrants expires three years from the date of the grant and have a per share exercise price ranging from $2.31 to $2.38.

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 any public solicitation, to a limited number of consultants and shareholders and were acquired for investment purposes only. The securities were issued pursuant to the private placement exemption provided by Section 4(2) of the Securities Act of 1933.

Sales of unregistered securities during the first three quarters of 2006 have previously been reported in quarterly reports on Form 10-QSB or current reports on Form 8-K that we have filed with the Securities and Exchange Commission.

SHARE REPURCHASES

We did not repurchase any of our securities in 2006.

Item 6. SELECTED FINANCIAL DATA

The following unaudited selected historical information has been derived from the audited consolidated financial statements of NutraCea. The consolidated financial information as of December 31, 2006 and 2005 and for each of the three years in the period ended December 31, 2006 are derived from our audited consolidated financial statements included elsewhere in this Form 10-K. The information set forth below should be read in conjunction with the financial statements, related Notes thereto, and the section entitled “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included elsewhere in this Form 10-K.

Annual Summary

Selected financial information represents annual results. Due to the acquisition of The RiceX Company on October 4, 2005, the following represents annual results for NutraCea and three months of operations for RiceX for 2005 information.

Statements of Operations Data: (In thousands except per share data)

	Years ended December 31,				
	2006	2005	2004	2003	2002
Revenues	$ 18,090	$ 5,564	$ 1,225	$ 1,536	$ 1,286
Costs and expenses	17,043	8,558	24,776	9,763	4,392
Income (loss) from operations	1,047	(2,994)	(23,551)	(8,227)	(3,106)
Other income (expense)	538	(878)	(24)	(4,309)	(3,356)
Net income (loss)	$ 1,585	$ (3,872)	$ (23,575)	$ (12,536)	$ (6,462)
Basic net income (loss) per common share	$ 0.02	$ (0.10)	$ (1.18)	$ (2.05)	$ (0.29)
Diluted net income (loss) per common share	$ 0.02	n/a	n/a	n/a	n/a
Weighted average number of shares outstanding	76,696	38,615	19,906	6,107	22,071

Balance Sheet data: (In thousands)

	As of December 31,				
	2006	2005	2004	2003	2002
Cash, cash equivalents, restricted cash and investments	$ 15,235	$ 3,636	$ 2,112	$ 100	$ 35
Total assets	73,255	47,464	3,338	541	556
Current liabilities	2,881	1,261	441	1,028	1,628
Long-term debt	-	9	1,635	-	-
Deficit accumulated during the development stage	(49,305)	(50,890)(1)	(44,928)	(21,345)	(8,683)
Total stockholders' equity (deficit)	$ 66,884	$ 38,893	$ 1,167	$ (487)	$ (3,123)

The Company adopted Securities and Exchange Commission, Staff Accounting Bulletin No. 108 in 2006. As a result, the Company increased accumulated deficit at December 31, 2005 by $2,090,000. See Note 3 to the audited financial statements.

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATION

Executive Summary

Year ended December 31, 2006 was a busy and exciting year for NutraCea and a remarkable period of growth for our company. During the year, we passed several key financial milestones; entered new distribution agreements that underscored the substantial demand for our core product, stabilized rice bran; and marked a number of operating achievements that positioned NutraCea for success in 2007 and beyond.

We at NutraCea:

- Increased our performance
- Surpassed our revenue targets
- Achieved profitability for the first time in our seven year history.

We are proud that we were able to set these new benchmarks, which clearly validate our business model and highlight the success of our strategies, to utilize our production capacity more efficiently and to focus on driving sales of high-end derivative products.

Another important 2006 achievement was our expansion of our Dillon, Montana plant, our facility where we produce our high margin fiber and solubles. During the year, we expanded the Dillon plant's capacity by 100 percent, while executing the project on schedule and under budget. Our Dillon expansion has enabled us to double our annual production capacity of solubles and fiber to 900 tons each, a quantity that will help us to address rising demand for our products within several different market segments.

In addition, during 2006 we expanded our humanitarian efforts teaming with Raising Malawi, Feed the Children and the Government of Malawi, Africa. This program will feed thousands of children and the health progress will be monitored and documented to track the benefits of this nutritional supplement for children.

Results of Operations

The following is a detailed discussion of our consolidated financial condition as of December 31, 2006 and 2005 and the results of operations for fiscal years ended December 31, 2006, 2005 and 2004, which should be read in conjunction with, and is qualified in its entirety by, the consolidated financial statements and notes thereto included elsewhere in this report. The consolidated financial statements (see Part II - Item 8. FINANCIAL STATEMENTS) represents annual results for NutraCea.

YEAR ENDED DECEMBER 31, 2006 AND DECEMBER 31, 2005

For the year ended December 31, 2006, our net income was $1,585,000, or $0.02 per share, compared to a loss of $3,872,000, or $0.10 loss per share, in 2005, showing an improvement of $5,457,000. The improvement for the year ended December 31, 2006 was primarily due to increased revenue by $12,526,000, offset by increased cost of sales of $6,252,000, resulting in an increase in gross margins of $6,274,000 for 2006 compared to 2005. The favorable increase of $5,457,000 was primarily due to increased total revenues combined with new product sales and new license and royalty fees. There were positive trends in our infomercial products, domestic animal product lines primarily sold to the equine market and our domestic functional foods and nutraceutical product lines. Assuming the merger with RiceX was effective for the entire year of 2005, the unaudited pro forma condensed combined consolidated net loss for year ended December 31, 2005 would have been $7,506,000 (NutraCea year ended December 31, 2005 net loss $3,567,000, RiceX year ended December 31, 2005 net loss $3,994,000 and $55,000 intercompany adjustment).

Consolidated revenues for the year ended December 31, 2006 were $18,090,000, an increase of $12,526,000, or 225%, from consolidated revenues of $5,564,000 in 2005. The increased revenue was a result of increased volume in all categories, including a $5,044,000 increase in the infomercial market, a $2,500,000 increase in the equine market, and a $2,000,000 increase in sales of the nutraceutical products. Also contributing to our revenue increase was license fees, royalties and other income in the amount of $985,000. Assuming the merger with RiceX was effective for the entire year of 2005, the unaudited pro forma condensed combined consolidated revenues for year ended December 31, 2005 would have been $8,082,000 (NutraCea year ended December 31, 2005 consolidated revenues $4,569,000, RiceX year ended December 31, 2005 consolidated revenues $3,838,000 and $325,000 intercompany adjustment).

Cost of goods sold increased $6,252,000 from $2,878,000 in 2005 to $9,130,000 in 2006 due primarily to the significant increase in product sold in 2006. Gross margins increased $6,274,000 to $8,960,000 in 2006, from $2,686,000 in 2005. This 233% increase was due to new sales in the infomercial market and increased sales in the equine market and nutraceutical markets. Assuming the merger with RiceX was effective for the entire year of 2005, the unaudited pro forma condensed combined consolidated gross margins for the year ended December 31, 2005 would have been $4,351,000 (NutraCea year ended December 31, 2005 gross margins at $2,046,000 and RiceX year ended December 31,2005 gross margins at $2,305,000).

Research and Development (R&D) expenses increased $186,000 in 2006 to $377,000 due to increased product development costs.

Sales, General and Administrative (SG&A) expenses increased $2,170,000 from $3,862,000 in 2005 to $6,032,000 in 2006. The increase was mostly due to added employee-related, travel, office, commission, and other general operating expenses. Included in SG&A category is stock-based compensation for employees, directors and consultants. Stock-based compensation decreased $142,000 from $868,000 in 2005 to $726,000 in 2006. Stock-based compensation expenses decreased $420,000 from $1,511,000 in 2005 to $1,091,000 in 2006. These non-cash charges relate to issuances of common stock and common stock warrants and options in 2006 and 2005. The higher issuances of restricted stock, options and warrants during 2005 was deemed necessary by management to retain and compensate officers, directors, consultants and employees while conserving cash assets that would otherwise have been expended for these purposes.

Professional fees decreased $123,000 from $1,627,000 in 2005 to $1,504,000 in 2006. In 2006, professional expenses were associated with consultants, accounting, SOX 404 compliance, legal, investor relations and stock-based compensation expenses. We incurred investor relations costs of $251,000 in 2006 compared to $307,000 in 2005, a decrease of $56,000 associated with an investor relations firm and fees associated with SEC filing requirements. Stock-based compensation on stock and warrant issues to consultants for services decreased $278,000 from $643,000 in 2005 to $365,000 in 2006

Interest expense decreased by $889,000 to $7,000 in 2006 due to the payoff of a note of $2,400,000 at 7% interest compounded quarterly on October 4, 2005. Interest expense in 2006 primarily consisted of interest on a loan for equipment.

Income tax expense is reported in selling, general and administrative expenses and consists of $5,000, $2,400 and $2,400 for the years ended December 31, 2006, 2005 and 2004, respectively.

Deferred taxes arise from temporary differences in the recognition of certain expenses for tax and financial reporting purposes. At December 31, 2006 and 2005, management determined that realization of these benefits is not assured and has provided a valuation allowance for the entire amount of such benefits. At December 31, 2006, net operating loss carryforwards were approximately $25,018,000 for federal tax purposes that expire at various dates from 2011 through 2020 and $12,230,000 for state tax purposes that expire in 2010 through 2015.

The Company has an unrecorded income tax benefit of $14,100,000 resulting from the exercise of options during 2006. This benefit can only be recognized if the net operating losses are used in future periods or if net operating losses expire, and will be recorded in equity.

Utilization of net operating loss carry forwards may be subject to substantial annual limitations due to the “change in ownership” provisions of the Internal Revenue Code of 1986, as amended, and similar state regulations. The annual limitation may result in expiration of net operating loss carry forwards before utilization.

YEAR ENDED DECEMBER 31, 2005 AND DECEMBER 31, 2004

Due to the merger of NutraCea with RiceX which occurred in the fourth quarter of 2005, the results of operations discussed below may not be comparable to future operations of the combined entity.

We had a net loss of $3,872,000 for the year ended December 31, 2005, or $0.10 loss per share, compared to a net loss of $23,583,000 for 2004, or $1.18 loss per share. The net loss reduction of $19,710,000 was primarily due to reduced issuances of common stock, stock option and warrants that result in non-cash expenses, increased total revenues, and new business development in the infomercial market. There were positive trends in our domestic animal product lines primarily sold to the equine market and our domestic functional foods and nutraceutical product lines.

Consolidated revenues for the year ended December 31, 2005 were $5,564,000, an increase of $4,339,000, or 354% on a comparative basis to the year ended December 31, 2004. The 354% increase was primarily a result of new sales in the infomercial market of $3,012,000 which began in September 2005. We had sales in the nutraceutical equine market of $1,071,000, sales in other nutraceutical markets of $323,000, and technology income of $100,000 in 2005. Also contributing to our revenue increase was fourth quarter sales of approximately $1,058,000 by The RiceX Company, which we acquired at the beginning of the fourth quarter of 2005.

Cost of goods sold increased from $600,000 in 2004 to $2,878,000 in 2005 due primarily to the significant increase in product sold in 2005. Gross margins increased $2,061,000 to $2,686,000 in 2005, from $625,000 in 2004. This 330% increase was due to new sales in the infomercial market, increased sales in the equine market and nutraceutical markets, and the addition of gross margins attributable to The RiceX Company.

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R&D expenses increased $64,000 in 2005 to $191,000 due to increased product development costs.

SG&A expenses decreased $7,782,000 from $11,644,000 in 2004 to $3,862,000 in 2005. The decrease related primarily to share-based compensation. Share-based compensation decreased $8,847,000 from $9,715,000 in 2004 to $868,000 in 2005. These non-cash charges are related to issuances of common stock and common stock warrants and options awarded in 2005 compared to 2004. During 2004, these non-cash expenses relating to the issuance of 5.5 million restricted shares of common stock to the Company's former Chief Executive Officer for services rendered and repayment of debt; the value of restricted shares and shares covered by the Company's S-8 registration statement issued to officers, directors and consultants for services; and the value of options and warrants issued to various employees and consultants. The increased issuance of restricted stock, options and warrants during 2004 was deemed necessary by management to retain and compensate officers, directors, consultants and employees while conserving cash assets that would otherwise have been expended for these purposes.

Professional fees decreased $10,778,000 from $12,405,000 in 2004 to $1,627,000 in 2005. The decrease related primarily to share-based compensation. Share-based compensation on stock and warrant issues to consultants for services decreased $10,640,000 from $11,283,000 in 2004 to $643,000 in 2005.

Interest expense increased by $868,000 to $896,000 in 2005 due to interest and discount related to a note payable of $2,400,000 at 7% interest compounded quarterly. On October 4, 2005, principle of $2,400,000 and $137,000 interest was paid in full. A non-cash discount in the amount of $759,000 was amortized in 2005.

The provision of income taxes for the years ended December 31, 2005 and 2004 consists of the $2,400 for minimum state income taxes.

Deferred taxes arise from temporary differences in the recognition of certain expenses for tax and financial statement purposes. At December 31, 2005, management determined that realization of these benefits is not assured and has provided a valuation allowance for the entire amount of such benefits. At December 31, 2005, net operating loss carry forwards were approximately $23,000,000 for federal tax purposes that expire at various dates from 2011 through 2025 and $19,700,000 for state tax purposes that expire in 2010 through 2015.

Utilization of net operating loss carry forwards may be subject to substantial annual limitations due to the "change in ownership" provisions of the Internal Revenue Code and similar state regulations. The annual limitation may result in expiration of net operating loss carry forwards before utilization.

LIQUIDITY AND CAPITAL RESOURCES

Our cash and cash equivalents were $14,867,000, $3,491,000 and $1,928,000 at December 31, 2006, 2005 and 2004, respectively.

For the year ended December 31, 2006, net cash used in operations was $629,000, compared to net cash used in operations in the same period of 2005 of $3,378,000, an improvement of $2,749,000. This improvement in cash used by operations resulted from our increase in sales and gross margins offset by our increase total operating expenses as noted above. Cash used in investing activities for the year ended December 31, 2006 was $9,698,000, compared to $63,000 for the same period of 2005. This increase was caused by our current plant expansion projects and the acquisition of other assets. Cash provided from financing activities for the year ended December 31, 2006 was $21,703,000 and is attributed to our private placement financing (see below), proceeds from exercise of stock options and the repayment of long-term debt in the amount of $15,000. Our working capital position was $23,320,000, $5,206,000 and $284,000 as of December 31, 2006, 2005 and 2004, respectively.

On May 12, 2006, we sold an aggregate of 17,560 shares of our Series C Convertible Preferred Stock at a price of $1,000 per share in a private placement transaction. This private placement of securities generated aggregate gross proceeds of approximately $17,560,000 ($15,934,000 net after offering and related expenses). The preferred shares can be converted to shares of our common stock at a conversion rate of approximately 1,176 shares of common stock for each preferred share issued in the transaction. Additionally, the investors were issued warrants to purchase an aggregate of 10,329,412 shares of our common stock at an exercise price of $1.35 per share. The warrants have a term of five years and are immediately exercisable. An advisor for the financing received a customary fee based on aggregate gross proceeds received from the investors and a warrant to purchase 500,000 shares of common stock at an exercise price per share of $1.35 and a term of five years.

On October 4, 2005, we sold an aggregate of 7,850 shares of our Series B Convertible Preferred Stock at a price of $1,000 per share in a private placement transaction. This private placement of securities generated aggregate gross proceeds of approximately $7,301,000 (approximately $7,300,000 after offering expenses). The preferred shares can be converted to shares of common stock at a conversion rate of 2,000 shares of common stock for each preferred share issued in the transaction. Additionally, we issued in this transaction warrants to purchase an aggregate of 7,850,000 shares of common stock at an exercise price of $0.70 per share. The warrants have a term of five years and are immediately exercisable. An advisor for the financing received a customary fee based on aggregate gross proceeds received from the investors and a warrant to purchase 1,099,000 shares of common stock at an exercise price per share of $0.50 and a term of five years.

On February 15, 2007, we sold an aggregate of 20,00,000 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 (approximately $47,000,000 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. The warrants have a term of five years and are immediately exercisable. An advisor for the financing received a customary fee based on aggregate gross proceeds received from the investors and a warrant to purchase 1,200,000 shares of common stock at an exercise price per share of $3.25 and a term of five years.

Domestic Initiatives

We began an initiative to expand our Dillon, Montana plant to increase production capacity to meet the growing market demand for our value-added products made from stabilized Rice Bran. We ordered additional equipment and expanded the Dillon Montana facility. The first phase expansion of Dillon has increased our NutraCea Solubles and NutraCea Fiber Complex capacity by more than 100%. An additional 50% capacity increase will follow in 2007 through a phase II expansion of Dillon. We intend to construct an additional processing facility in Louisiana during 2007 to produce the value-added product of NutraCea Solubles, Dextrinized Rice Bran and NutraCea Fiber Complex in an effort to meet expected customer demands for these products.

We have existing financial liquidity from cash on hand and current cash flow to complete the expansion. Strong market interest in our proprietary stabilized Rice Bran derivatives has prompted the need for increased manufacturing capability and is consistent with our goal of meeting growing customer demands and a new awareness of our products' value. This increase in manufacturing capacity is the most efficient and economical means of boosting capacity as quickly as possible to meet the increasing demands of the marketplace.

We have entered into a raw rice bran supply agreement with Louisiana Rice Mill LLC, or LRM. The agreement quadruples our current annual supply of raw rice bran in the United States. In addition, we announced the construction of our stabilization facility at the LRM rice milling facility in Mermentau, Louisiana. Under the terms of the agreement, LRM will supply raw rice bran from its rice milling operations to NutraCea. The supply agreement is intended to provide as much as 30,000 tons annually to our current supply of raw bran, which will be processed through our exclusive proprietary stabilization system to produce stabilized rice bran for both the human and animal nutrition markets. We have the ability to fund this project with existing cash resources. The new facility at LRM is expected to be completed and operational by April 2007.

The Company has also entered into a second raw rice bran supply agreement with another Louisiana rice milling company and engineering and permitting work is currently underway. The second Louisiana plant will include both rice stabilization technology and value-added products technology. The second plant is expected to begin operations during the second half of 2007. Again, NutraCea has the ability to fund this project with existing cash resources..

International Initiatives

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On September 13, 2005, we entered into an agreement with a Dominican Republic rice mill whereby the two companies agreed to form a joint venture. The terms of the agreement allows us the option to install equipment to produce annually at least 5,000 metric tons of stabilized rice bran in the Dominican Republic, or in the alternative produce the product in the United States and ship the raw ingredients to the Dominican Republic and package it in final form there. The joint venture will be equally owned by the two companies and will commercially sell stabilized rice bran products through retail and government in the Dominican Republic and Haiti. NutraCea has shipped product directly rather than utilize the joint venture since the company ha chosen not to build a processing facility in the Dominican Republic at this time.

On October 25, 2005, we signed an agreement with an industrial consortium in Colombia to study the creation of a joint entity to share equally in the profits generated from sales of our products in the Colombian market. Under the agreement, the Colombian consortium is to provide 50% of all the financing necessary to construct the plants (with us providing the remaining 50% of the financing) and is to be responsible for providing all the necessary land and space required for the implementation of the plants to be constructed. The Colombian consortium would be responsible for providing all of the sales and distribution as part of its contribution to the joint entity. We continue efforts to execute a formal definitive agreement; however, we have not entered into a definitive agreement as of March 30, 2007.

On October 28, 2005, we entered into a binding letter of intent with an Ecuadorian company to study arriving at a definitive agreement for a working arrangement that will allow the Ecuadorian company the right to utilize our proprietary ingredients and value-added processing in their multi-faceted food business, which includes animal feed, poultry and cereals. We are currently servicing this company with product shipped from the United States although we have not entered into a definitive agreement as of March 30, 2007, as we have chosen not to locate facilities in Equidor at this time.

In November 2005, NutraCea signed a Supply and Distribution Agreement with T. Geddes Grant, a Jamaican Corporation. The agreement requires us to deliver a customized formulated and fortified RiSolubles mix to T. Geddes Grant. The agreement requires that T. Geddes Grant purchase certain minimums during the agreement in order for them to maintain exclusivity under the terms of the agreement. As of the filing date, we have not shipped product to T. Gaddes Grant.

On December 19, 2006, NutraCea began distributing product to thousands of orphans through Community Based Organizations in Malawi as part of an extraordinary collaborative effort with Feed the Children, Raising Malawi and The Malaria Solution Foundation. The mission was to provide direct physical assistance, long-term sustainability and support to many of Malawi's two million orphans and vulnerable children. Approximately ten thousand children at the Consol Homes-Raising Malawi Orphan Care Center received our product to help improve their overall nutrition. The initial product distribution was made possible through funding raised by The Malaria Solution Foundation with a purchase and donation of NutraCea's products.

There can be no assurance that these international initiatives will be achieved in part or whole, however management continues its efforts to formalize its relationship within these countries to further its business activities.

OFF BALANCE SHEET ARRANGEMENTS

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 risks, 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.

CONTRACTUAL OBLIGATIONS

As part of the normal course of business, the Company incurs certain contractual obligations and commitments which will require future cash payments. The following tables summarize the significant obligations and commitments.

($ in thousands)	Total	2007	2008	2009	2010	2111	2112
			Payments Due by Period				
Long-term debt	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Capital lease	-	-	-	-	-	-	-
Operating leases	4,031	605	729	750	775	801	371
Purchase obligations	-	-	-	-	-	-	-
Total contractual obligations	$ 4,031	$ 605	$ 729	$ 750	$ 775	$ 801	$ 371

CRITICAL ACCOUNTING POLICIES

A summary of our significant accounting policies is included in Note 2, Part II - Item 8, FINANCIAL STATEMENTS. We believe the application of these accounting policies on a consistent basis enables us to provide timely and reliable financial information about our earnings results, financial condition and cash flows.

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make judgments, estimates and assumptions regarding uncertainties that affect the reported amounts presented and disclosed in the financial statements. Management reviews these estimates and assumptions based on historical experience, changes in business conditions and other relevant factors that they believe to be reasonable under the circumstances. In any given reporting period, actual results could differ from the estimates and assumptions used in preparing our financial statements.

Critical accounting policies are those that may have a material impact on our financial statements and also require management to exercise significant judgment due to a high degree of uncertainty at the time the estimate is made. Management has discussed the development and selection of our accounting policies, related accounting estimates and the disclosures set forth below with the Audit Committee of our Board of Directors. We believe our critical accounting policies include those addressing revenue recognition, allowance for doubtful accounts, and inventories.

Revenue Recognition

Revenues from product sales are recognized when products are shipped and when the risk of loss has transferred to the buyer. Deposits are deferred until either the product has shipped or conditions relating to the sale have been substantially performed.

Allowance for Doubtful Accounts

We continuously monitor collections from our customers and maintain an allowance for doubtful accounts based upon our historical experience and any specific customer collection issues that we have identified. While such credit losses have historically not exceeded our expectations and the provisions established, there is a risk that credit losses in the future will exceed those that have occurred in the past, in which case our operating results would be adversely affected.

Valuation of long-lived assets

Long-lived assets, consisting primarily of property and equipment, patents and trademarks, and goodwill, comprise a significant portion of our total assets. Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that their carrying values may not be recoverable. Recoverability of assets is measured by a comparison of the carrying value of an asset to the future net cash flows expected to be generated by those assets. The cash flow projections are based on historical experience, management’s view of growth rates within the industry, and the anticipated future economic environment.

Factors we consider important that could trigger a review for impairment include the following:

(a) significant underperformance relative to expected historical or projected future operating results,

(b) significant changes in the manner of its use of the acquired assets or the strategy of its overall business, and

(c) significant negative industry or economic trends.

When we determine that the carrying value of patents and trademarks, long-lived assets and related goodwill and enterprise-level goodwill may not be recoverable based upon the existence of one or more of the above indicators of impairment, it measures any impairment based on a projected discounted cash flow method using a discount rate determined by its management to be commensurate with the risk inherent in its current business model.

Marketable Securities

Marketable securities are marked to market at each period end. Any unrealized gains and losses on the marketable securities are excluded from operating results and are recorded as a component of other comprehensive income (loss). If declines in value are deemed other than temporary, losses are reflected in Net income (loss).

Inventory

Inventory is stated at the lower of cost (first-in, first-out) or market and consists of nutraceutical products. While we have an inventory of these products, any significant prolonged shortage of these ingredients or of the supplies used to enhance these ingredients could materially adversely affect the our results of operations.

Property and Equipment

Property and equipment are stated at cost. We provide for depreciation using the straight-line method over the estimated useful lives as follows:

Furniture and equipment	5-7	years
Automobile	5	years
Software	3	years
Leasehold improvements	2.4-7	years
Property and equipment	7-10	years

Expenditures for maintenance and repairs are charged to operations as incurred while renewals and betterments are capitalized. Gains or losses on the sale of property and equipment are reflected in the statements of operations.

Fair Value of Financial Instruments

For certain of our financial instruments, including cash, accounts receivable, inventory, prepaid expenses, accounts payable, accrued salaries and benefits, deferred compensation, accrued expenses, customer deposits, due to related party, notes payable - related party and note payable, the carrying amounts approximate fair value due to their short maturities.

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

year ended December 31, 2006 reflect the impact of adopting SFAS 123(R). In accordance with the modified prospective method, the consolidated financial statements for prior periods have not been restated to reflect, and do not include, the impact of SFAS 123(R). For stock-based compensation grants to consultants, we recognize as compensation expense the fair value of such grants, recognized over the related service period. Prior to 2006, we recorded stock-based compensation grants to employees based on the excess of the estimated fair value of the common stock on the measurement date over the exercise price.

Item 7A. 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 December 31, 2006, 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 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Index to Consolidated Financial Statements

Report of Perry-Smith LLP, Independent Registered Public Accounting Firm

Report of Malone & Bailey, PC, Independent Registered Public Accounting Firm

Consolidated Balance Sheets as of December 31, 2006 and 2005

Consolidated Statements of Operations for the three years ended December 31, 2006

Consolidated Statement of Comprehensive Income (Losses) for the three years ended December 31, 2006

Consolidated Statement of Changes in Stockholder Equity for the three years ended December 31, 2006

Consolidated Statements of Cash Flows for the three years ended December 31, 2006

Notes to Consolidated Financial Statements

The financial statements and financial information required by Item 8 are set forth below on pages F-1 through F-30 of this report.

Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE.

None.

Item 9A. CONTROLS AND PROCEDURES.

Disclosure Controls and Procedures.

We carried out an evaluation, under the supervision and with the participation of management, including our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our 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 annual report. Based upon that evaluation, our principal executive officer and our principal financial officer concluded that, as of December 31, 2006, our disclosure controls and procedures were effective 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.

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Changes in Internal Control Over Financial Reporting.

There was no change in our internal control over financial reporting that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Item 9B. OTHER INFORMATION.

None.

PART III

Item 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Information required by this Item with respect to directors and compliance with Section 16(a) of the Securities Exchange Act of 1934 may be found in the sections captioned “ELECTION OF DIRECTORS” and “SECTION 16(a) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE” appearing in the definitive Proxy Statement to be filed no later than 120 days after the end of the 2006 fiscal year and to be delivered to stockholders in connection with the Annual Meeting of Shareholders expected to be held in May, 2007 (the “2007 Proxy Statement”). Such information is incorporated herein by reference. Information required by this Item with respect to executive officers has been included in Part I of this report:

Code of Business Conduct and Ethics

The Board has adopted a Code of Business Conduct and Ethics that applies to all directors, officers and employees of NutraCea. NutraCea will provide any person, without charge, a copy of this Code. Requests for a copy of the Code may be made by writing to NutraCea at 1261 Hawk’s Flight Court, El Dorado Hills, California 95762, Attention: Chief Financial Officer.

Item 11. EXECUTIVE COMPENSATION

Information with respect to this Item may be found in the section captioned “Executive Compensation” appearing in the forthcoming 2007 Proxy Statement and is incorporated herein by reference.

Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Information with respect to this Item may be found in the section captioned “Security Ownership of Certain Beneficial Owners and Management” appearing in the forthcoming 2007 Proxy Statement and is incorporated herein by reference.

Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

Information with respect to this Item may be found in the section captioned “Certain Relationships and Related Transactions” appearing in the 2007 Proxy Statement and is incorporated herein by reference.

Item 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Information with respect to this Item may be found in the section captioned “Principal Accountant Fees and Services” appearing in the 2007 Proxy Statement and is incorporated herein by reference.

PART IV

Item 15. EXHIBITS, FINANCIAL STATEMENT SCHEDULES

(a) Exhibits.

Exhibit Number	Exhibit Description
2.01(1)	Plan and Agreement of Exchange.
2.02(2)	Agreement and Plan of Merger and Reorganization, dated as of April 4, 2005, by and among the NutraCea, The RiceX Company and Red Acquisition Corporation.
3.01.1(3)	Restated and Amended Articles of Incorporation as filed with the Secretary of State of California on December 13, 2001.
3.01.2(4)	Certificate of Amendment of Articles of Incorporation as filed with the Secretary of State of California on August 4, 2003.
3.01.3(5)	Certificate of Amendment of Articles of Incorporation as filed with the Secretary of State of California on October 31, 2003.
3.01.4(4)	Certificate of Amendment of Articles of Incorporation as filed with the Secretary of State of California on September 29, 2005
3.02(6)	Certificate of Designation of the Rights, Preferences, and Privileges of the Series A Preferred Stock as filed with the Secretary of State of California on December 13, 2001.
3.03(7)	Certificate of Determination, Preferences and Rights of Series B Convertible Preferred Stock as filed with the Secretary of State of California on October 4, 2005.
3.04(8)	Certificate of Determination, Preferences and Rights of Series C Convertible Preferred Stock as filed with the Secretary of State of California on May 10, 2006.
3.05(23)	Bylaws of NutraCea.
4.01(7)	Form of warrant issued to subscribers in connection with NutraCea's October 2005 private placement.
4.02(8)	Form of warrant issued to subscribers in connection with NutraCea's May 2006 private placement.
4.03(25)	Form of warrant issued to subscribers in connection with NutraCea's February 2007 private placement

10.01(9)	NutraCea 2003 Stock Compensation Plan
10.02(4)	NutraCea 2005 Equity Incentive Plan
10.03(7)	Securities Purchase Agreement, dated September 28, 2005, by and among NutraCea and the investors named therein.
10.04(7)	Registration Rights Agreement, dated September 28, 2005, by and among NutraCea and the investors named therein.

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10.05(8)	Securities Purchase Agreement, dated May 12, 2006, by and among NutraCea and the investors named therein.
10.06(8)	Registration Rights Agreement, dated May 12, 2006, by and among NutraCea and the investors named therein.
10.07(10)±	Private Label Supply Agreement and Strategic Alliance between NutraCea and ITV Global.
10.08(4)	Employment Agreement between NutraCea and Patricia McPeak.
10.09(4)	Restricted Stock Agreement between NutraCea and Patricia McPeak
10.10(11)	Executive Employment Agreement between NutraCea and Bradley D. Edson.
10.11(11)	Executive Employment Agreement between NutraCea and Margie D. Adelman.
10.12(4)	Executive Employment Agreement between The RiceX Company and Todd C. Crow.
10.13(4)	Amendment No. 1 to Employment Agreement between NutraCea, Todd C. Crow and The RiceX Company.
10.14(4)	Executive Employment Agreement between The RiceX Company and Ike E. Lynch.
10.15(4)	Amendment No. 1 to Employment Agreement between NutraCea, Ike E. Lynch and The RiceX Company.
10.16(12)	Form of Affiliate Agreement between certain affiliates of RiceX and NutraCea dated April 4, 2005
10.17(11)±	W.F. Young Distribution Agreement.
10.18(11)±	W.F. Young Technology Agreement.
10.19(13)	Stock Purchase Agreement between NutraCea and Langley Park Investments PLC
10.20(4)±	Production Facility Development and Rice Bran Supply and Purchase Agreement dated September 13, 2005 between NutraCea and Food Trading Company Dominicana, S.A.
10.21(4)±	Assignment dated April 12, 2005 from W.F. Young, Inc. to NutraCea
10.22(4)±	Distribution Agreement dated April 12, 2005 between W.F. Young, Inc. and NutraCea
10.23(4)	Manufacturing Agreement dated April 12, 2005 between W.F. Young, Inc. and NutraCea

10.24(4)±	Supply and Distribution Agreement dated November 4, 2005 between NutraCea and T. Geddes Grant.
10.25(14)	Commercial Lease and Deposit Receipt between Roebbelen Land Company and The RiceX Company dated December 23, 1991.
10.26(14)	First Amendment of Lease between Roebbelen Land Company and The RiceX Company dated January 19, 1994.
10.27(14)	Second Amendment of Lease between Roebbelen Land Company and The RiceX Company dated July 11, 1996.
10.28(14)	Third Amendment of Lease Agreement between Roebbelen Land Company and The RiceX Company dated February 1, 1998.

10.29(14)	Lease Agreement between Roebbelen Land Company and The RiceX Company dated July 11, 1996.
10.30(14)	First Amendment of Lease between Roebbelen Land Company and The RiceX Company dated September 1996.
10.31(14)	Second Amendment of Lease Agreement between Roebbelen Land Company and The RiceX Company dated February 1, 1998.
10.32(15)	Agreement on Exclusive Distribution in Europe between The RiceX Company and KREGLINGER EUROPE N.V. dated October 1, 2002.
10.33(16)±	Stabilized Rice Bran Processing, Sales, and Marketing Agreement between Farmers' Rice Cooperative and The RiceX Company dated May 1, 2002.
10.34(17)	The RiceX Company 1997 Stock Option Plan
10.35(14)	Form of Directors Stock Option Agreement for The RiceX Company.
10.36(14)	Form of Non-statutory Stock Option Agreement not issued under The RiceX Company 1997 Stock Option Plan, governing options granted to The RiceX Company employees.
10.37(18)	Form of non-statutory Stock Option Agreement issued under The RiceX Company 1997 Stock Option Plan between The RiceX Company and The RiceX Company employees dated October 1, 1999.
10.37(18)	Form of non-statutory Stock Option Agreement issued under The RiceX Company 1997 Stock Option Plan between The RiceX Company and Ike Lynch dated November 1, 1999. Identical Agreements with Daniel McPeak, Jr. and Todd C. Crow.
10.39(19)	Form of Board Member Non-statutory Stock Option Agreement issued under The RiceX Company 1997 Stock Option Plan between The RiceX Company and the Board Members of the RiceX Company dated February 22, 2001, September 23 and 29, 2001.
10.40(16)	Form of Non-statutory Stock Option Agreement issued under The RiceX Company 1997 Stock Option Plan between The RiceX Company and employees dated January 2, 2000.
10.41(20)	Form of Non-statutory Stock Option Agreement issued September 23, 2002 between The RiceX Company and the members of The RiceX Company's Board of Directors.
10.42(20)	Form of Non-statutory Stock Option Agreement issued July 1, 2004 between The RiceX Company and Edward McMillan.
10.43(21)	Form of Non-statutory Stock Option Agreement issued October 18, 2004 between The RiceX Company and two members of The RiceX Company Board

	Directors.
10.44(22)	Form of Non-statutory Stock Option Agreement issued under the 1997 Stock Option Plan between The RiceX Company and certain non-employee RiceX Directors dated March 31, 2005.
10.45(22)	Form of Non-statutory Stock Option Agreement issued under the 1997 Stock Option Plan between The RiceX Company and certain employees of RiceX dated March 31, 2005.
10.46(4)	Form of Option Assumption Agreement between NutraCea and Option Holders relating to assumed Options granted under The RiceX Company 1997 Stock Option Plan.

10.47(4)	Form of Option Assumption Agreement between NutraCea and Option Holders relating to assumed non-plan RiceX Options.
10.48(4)	Form of Option Assumption Agreement between NutraCea and former Directors of The RiceX Company.
10.49(4)	Form of Resale Restriction Agreement entered into between NutraCea and each of Todd C. Crow and Ike E. Lynch.
10.50(4)	Form of Resale Restriction Agreement entered into between NutraCea and each of James Lintzenich, Edward McMillan and Steven Saunders.
10.51(4)	Form of Resale Restriction Agreement entered into between NutraCea and each of Bradley Edson, Patricia McPeak, Margie Adelman, Eliot Drell and David Bensol.
10.52(10)	Warrant Agreement between NutraCea and Steven Saunders dated February 27, 2006.
10.53(24)	Form of non-statutory Stock Option Agreement between NutraCea and the non-employee members of the Board of Directors dated May 23, 2006.
10.54(25)	Securities Purchase Agreement, dated February 15, 2007, by and among NutraCea and the investors named therein.
10.55(25)	Registration Rights Agreement, dated February 15, 2007, by and among NutraCea and the investors named therein.
10.56	Executive Employment Agreement between NutraCea and Kody Newland.
21.01	List of subsidiaries.
23.1	Consent of Malone & Bailey, PC, Independent Registered Public Accounting Firm.
23.2	Consent of Perry-Smith LLP, Independent Registered Public Accounting Firm.
24.1	Power of Attorney (See signature page.)
31.1	Certification by CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification by CEO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification by CEO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification by CFO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

± Confidential treatment granted as to certain portions.

(1) incorporated herein by reference to exhibits previously filed on Registrant's Current Report on Form 8-K, filed on November 19, 2001.

(2) incorporated herein by reference to exhibits previously filed on Registrant's Current Report on Form 8-K, filed on April 4, 2005.

(3) incorporated herein by reference to exhibits previously filed on Registrant's Annual Report on Form 10-KSB, filed on April 16, 2002.

(4) incorporated herein by reference to exhibits previously filed on Registrant's Registration Statement on Form SB-2, filed on November 18, 2005.

(5) incorporated herein by reference to exhibits previously filed on Registrant's Quarterly Report on Form 10-QSB, filed on November 19, 2003.

(6) incorporated herein by reference to exhibits previously filed on Registrant's Registration Statement on Form SB-2, filed on June 4, 2002.

(7) incorporated herein by reference to exhibits previously filed on Registrant's Current Report on Form 8-K, filed on October 4, 2005.

(8) incorporated herein by reference to exhibits previously filed on Registrant's Current Report on Form 8-K, filed on May 15, 2006.

(9) incorporated herein by reference to exhibits previously filed on Registrant's Registration Statement on Form S-8, filed on November 18, 2003.

(10) incorporated herein by reference to exhibits previously filed on Registrant's Quarterly Report on Form 10-QSB, filed on May 15, 2006.

(11) incorporated herein by reference to exhibits previously filed on Registrant's Annual Report on Form 10-KSB, filed on March 31, 2005.

(12) incorporated herein by reference to exhibits previously filed on The RiceX Company's Report on Form 8-K, filed on April 4, 2005.

(13) incorporated herein by reference to exhibits previously filed on Registrant's Current Report on Form 8-K, filed on September 14, 2004.

(14) incorporated herein by reference to exhibits previously filed on The RiceX Company's Registration Statement No. 000-24285, filed on May 18, 1998.

(15) incorporated herein by reference to exhibits previously filed on The RiceX Company's Report on Form 10-KSB, filed on March 31, 2003.

(16) incorporated herein by reference to exhibits previously filed on The RiceX Company's Report on Form 10-QSB, filed on August 12, 2002.

(17) incorporated herein by reference to exhibits previously filed on The RiceX Company's Registration Statement Number Statement No. 000-24285, filed on May 18, 1998.

(18) incorporated herein by reference to exhibits previously filed on The RiceX Company's Report on Form 10-KSB, filed on March 30, 2000.

(19) incorporated herein by reference to exhibits previously filed on The RiceX Company's Report on Form 10-QSB, filed on August 10, 2001.

(20) incorporated herein by reference to exhibits previously filed on The RiceX Company's Report on Form 10-QSB, filed on November 15, 2003.

(21) incorporated herein by reference to exhibits previously filed on The RiceX Company's Report on Form 10-KSB, filed on March 30, 2005.

(22) incorporated herein by reference to exhibits previously filed on The RiceX Company's Report on Form 10-QSB, filed on May 16, 2005.

(23) incorporated herein by reference to exhibits previously filed on Registrant's Registration Statement on Form SB-2, filed on June 12, 2006.

(24) incorporated herein by reference to exhibits previously filed on Registrant's Quarterly Report on Form 10-QSB, filed on August 14, 2006.

(25) incorporated herein by reference to exhibits previously filed on Registrant's Current Report on Form 8-K, filed on February 20, 2007.

SIGNATURES

In accordance with Section 13 or 15 (d) of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NUTRACEA

Date: March 30, 2007

By: /s/ Bradley D. Edson

Bradley D. Edson,
Chief Executive Officer

Power of Attorney

Each person whose signature appears below constitutes and appoints each of Bradley D. Edson and Todd C. Crow, true and lawful attorney-in-fact, with the power of substitution, for him in any and all capacities, to sign amendments to this Report on Form 10-K, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, hereby ratifying and confirming all that said attorneys-in-fact, or his substitute or substitutes, may do or cause to be done by virtue thereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, this report has been signed by the following persons in the capacities and on the dates indicated.

Signature	Title	Date
Principal Executive Officer:		
/s/ Bradley D. Edson Bradley D. Edson	President, Chief Executive Officer and Director	March 30, 2007
Principal Financial Officer and Principal Accounting Officer:		
/s/ Todd C. Crow Todd C. Crow	Chief Financial Officer	March 30, 2007
Additional Directors:		
/s/ David Bensol David Bensol	Director	March 30, 2007
/s/ James C. Lintzenich James C. Lintzenich	Director	March 30, 2007

/s/ Edward L. McMillan Edward L. McMillan	Director	March 30, 2007
 Patricia McPeak	Director	March 30, 2007
/s/ Steven W. Saunders Steven W. Saunders	Director	March 30, 2007
/s/ Kenneth L. Shropshire Kenneth L. Shropshire	Director	March 30, 2007

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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REPORT OF INDEPENDENT REGISTERED
PUBLIC ACCOUNTING FIRM

Board of Directors
NutraCea and subsidiaries
El Dorado Hills, California

We have audited the accompanying consolidated balance sheet of NutraCea and subsidiaries (the "Company") as of December 31, 2006, and the related consolidated statements of operations, comprehensive income (loss), changes in stockholders' equity, and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of the Company as of December 31, 2006, and the consolidated results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Perry-Smith LLP

Perry-Smith LLP
Sacramento, California

March 30, 2007

**REPORT OF INDEPENDENT REGISTERED
PUBLIC ACCOUNTING FIRM**

Board of Directors
NutraCea and subsidiaries
El Dorado Hills, California

We have audited the accompanying consolidated balance sheet of NutraCea as of December 31, 2005 and the related statements of operations, comprehensive loss, changes in stockholders' equity, and cash flows for each of the two years then ended. These financial statements are the responsibility of NutraCea's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of NutraCea as of December 31, 2005, and the results of its operations and its cash flows for each of the two years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Malone & Bailey, PC

MALONE & BAILEY, PC
www.malone-bailey.com
Houston, Texas

March 15, 2006

NUTRACEA AND SUBSIDIARIES
Consolidated Balance Sheets

	As of December 31,	
	2006	**2005**
ASSETS		
Current assets:		
Cash and cash equivalants	$ 14,867,000	$ 3,491,000
Marketable securities	368,000	145,000
Trade accounts receivables, net	7,093,000	2,515,000
Inventories	796,000	594,000
Notes receivable, current portion	1,694,000	-
Deposits and other current assets	1,383,000	82,000
Total current assets	26,201,000	6,827,000
Restricted marketable securities	-	145,000
Notes receivable, net of current portion	682,000	-
Property and equipment, net	8,961,000	5,493,000
Patents and trademarks, net of accumulated amortization of $439,000 and $119,000	5,097,000	2,418,000
Goodwill	32,314,000	32,581,000
Total assets	$ 73,255,000	$ 47,464,000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued liabilities	$ 2,778,000	$ 1,247,000
Notes payable, current portion	-	6,000
Due to related parties	-	3,000
Deferred revenue	103,000	5,000
Total current liabilities	2,881,000	1,261,000
Long-term liabilities:		
Notes payable, net of current portion	-	9,000
Total liabilities	2,881,000	1,270,000
Commitments and contingencies		
Convertible, series B preferred stock, no par value, $1,000 stated value 25,000 shares authorized, 470 and 7,850 shares issued and outstanding	439,000	7,301,000
Convertible, series C preferred stock, no par value, $1,000 stated value 25,000 shares authorized, 5,468 and 0 shares issued and outstanding	5,051,000	-
Shareholders' equity:		
Common stock, no par value, 200,000,000 shares authorized, 103,792,827,000 and 67,102,079 shares issued and outstanding	114,111,000	89,783,000
Accumulated deficit	(49,305,000)	(48,800,000)
	78,000	(2,090,000)

Accumulated other comprehensive income, unrealized gain (loss) on marketable securities				
Total shareholders' equity		64,884,000		38,893,000
Total liabilities and shareholders' equity	$	73,255,000	$	47,464,000

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The accompanying notes are an integral part of these financials

NUTRACEA AND SUBSIDIARIES
Consolidated Statement of Operations

	For the years ended December 31,		
	2006	2005	2004
Revenues			
Net product sales	$ 17,105,000	$ 5,545,000	$ 1,010,000
Royalty, label and licensing fees	985,000	19,000	215,000
Total revenue	18,090,000	5,564,000	1,225,000
Cost of goods sold	9,130,000	2,878,000	600,000
Gross profit	8,960,000	2,686,000	625,000
Research and development expenses	377,000	191,000	127,000
Selling, general and administrative expenses	6,032,000	3,862,000	11,644,000
Professional fess	1,504,000	1,627,000	12,405,000
Total operating expenses	7,913,000	5,680,000	24,176,000
Income (loss) from operations	1,047,000	(2,994,000)	(23,551,000)
Other income (expense)			
Interest income	545,000	18,000	5,000
Interest expense	(7,000)	(896,000)	(28,000)
Net income (loss)	1,585,000	(3,872,000)	(23,574,000)
Cumulative preferred dividends	-	-	(8,000)
Net income (loss) available to common shareholders	$ 1,585,000	$ (3,872,000)	$ (23,582,000)
Net income (loss) per share:			
Basic	$ 0.02	$ (0.10)	$ (1.18)
Diluted	$ 0.02	(0.10)	(1.18)

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The accompanying notes are an integral part of these financials

NUTRACEA AND SUBSIDIARIES
Consolidated Statement of Comprehensive Income (Loss)

	For the years ended December 31,		
	2006	**2005**	**2004**
Net Income (loss) available to common shareholders	$ 1,585,000	$ (3,872,000)	$ (23,582,000)
Other comprehensive loss:			
Unrealized gain (loss) on marketable securities	78,000	(78,000)	(2,012,000)
Net and comprehensive income (loss)	$ 1,663,000	$ (3,950,000)	$ (25,594,000)

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The accompanying notes are an integral part of these financials

NUTRACEA AND SUBSIDIARIES
Consolidated Statement of Changes in Stockholders' Equity

	Convertible, Redeemable Series A, B, C Preferred		Common Stock			Other		
	Shares	Amount	Shares	Amount	Deferred Compensation	Comprehensive Loss	Accumulated Deficit	Total
Balance, January 1, 2004	670,000	$ 351,000	11,773,842	$ 20,980,000	$ (122,000)	$ -	$ (21,345,000)	$ (487,00
Amortization of deferred compensation					57,000			57,00
Common stock cancelled			(50,000)					
Common stock issues for								
accounts payable			168,626	58,000				58,00
marketable securities			7,000,000	2,380,000				2,380,00
patent incentive plan			180,000	239,000				239,00
services rendered			4,407,950	3,470,000				3,470,00
settlements			5,780,000	8,839,000				8,839,00
Common stock repurchased			(344,956)	(230,000)				(230,00
Preferred dividends converted to common stock		(6,000)	5,759	6,000				6,00
Preferred stock converted to common stock	(540,000)	(348,000)	630,000	348,000				348,00
Preferred stock dividends		9,000					(9,000)	(9,00
Preferred stock dividends paid		(48,000)						
Preferred stock repurchased	(130,000)							
Reclass of options to preferred stock		63,000		(63,000)				(63,00
Reversal of stock options				(49,000)	49,000			
Stock options cancelled								
Stock options exercised for			6,579,323	2,776,000				2,776,00

cash								
Stock options issued for								
notes payable				786,000				786,00
services rendered				8,583,000				8,583,00
Other comprehensive loss						(2,012,000)		(2,012,00
Net loss							(23,574,000)	(23,574,00
Balance, December 31, 2004	-	$ 21,000	36,130,544	$ 48,123,000	$ (16,000)	$ (2,012,000)	$ (44,928,000)	$ 1,167,00
Amortization of deferred compensation					81,000			81,00
Common stock issues for								
consultants service rendered			1,904,805	907,000				907,00
patent incentive plan			30,000	13,000				13,00
officers and directors			70,000	30,000				30,00
settlements			97,000	98,000				98,00
Preferred stock issued	7,850	7,301,000						7,301,00
RiceX acquisition		(21,000)	28,272,064	40,029,000				40,029,00
Stock options/warrants exercised for								
cash			531,000	104,000				104,00
cashless			66,666					
Stock options/warrants issued for								
consultants				349,000				349,00
employees				130,000	(65,000)			65,00
Other comprehensive loss						(78,000)		(78,00
Net loss							(3,872,000)	(3,872,00
Balance, December 31, 2005 as originally reported	7,850	7,301,000	67,102,079	89,783,000	-	(2,090,000)	(48,800,000)	38,893,00
						2,090,000	(2,090,000)	

Implementation of SAB 108								
Beginning balance, January 1, 2006 as adjusted	7,850	7,301,000	67,102,079	89,783,000	-	-	(50,890,000)	$ 38,893,00
Common stock issues for consultants service rendered			29,999	30,000				30,00
Preferred stock issued, net of expense	17,560	15,934,000						
Preferred stock conversions								
series B	(7,380)	(6,862,000)	14,760,000	6,862,000				6,862,00
series C	(12,092)	(10,883,000)	14,225,854	10,883,000				10,883,00
Asset acquisition			297,108	350,000				350,00
RiceX options cancelled				(642,000)				(642,00
Stock options/warrants exercised for								
cash			5,635,064	5,784,000				5,784,00
cashless			1,742,723					
Stock options/warrants issued for								
consultants				375,000				375,00
employees and directors				686,000				686,00
Other comprehensive income (loss)						78,000		78,00
Net income							1,585,000	1,585,00
Balance, December 31, 2006	5,938	5,490,000	103,792,827	114,111,000	-	78,000	(49,305,000)	64,884,00

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The accompanying notes are an integral part of these financials

NUTRACEA AND SUBSIDIARIES
Consolidated Statement of Cash Flows

	For the years ended December 31,		
	2006	**2005**	**2004**
Cash flow from operating activities:			
Net income (loss)	$ 1,585,000	$ (3,872,000)	$ (23,582,000)
Adjustments to reconcile net income (loss) to net cash from operating activities:			
Depreciation and amortization	1,150,000	1,091,000	38,000
Non-cash issuances of common stock		1,017,000	12,366,000
Non-cash issuance of stock, options and warrants	1,091,000	510,000	9,306,000
Modifications of options and warrants, non-employees		-	63,000
Modifications of options and warrants, employees		-	(49,000)
Net changes in operating assets and liabilities:			
(Increase) decrease in			
Trade accounts receivable	(4,578,000)	(2,094,000)	23,000
Inventories	(202,000)	107,000	(234,000)
Deposits and other current assets	(1,301,000)	(106,000)	(16,000)
Increase (decrease) in:			
Accounts payable, accrued liabilities	1,531,000	140,000	(79,000)
Advances from related parties	(3,000)	(71,000)	56,000
Deferred compensation	-	-	106,000
Customer deposits	98,000	(100,000)	-
Net cash used in operating activities	(629,000)	(3,378,000)	(2,002,000)
Cash flows from investing activities:			
Notes receivables	(2,376,000)	-	-
Purchase of The RiceX Company, net of $546,148 cash received		33,000	-
Purchase of property and equipment	(4,682,000)	(14,000)	(117,000)
Purchase of other assets	(2,640,000)	(82,000)	(56,000)
Net cash used in investing activities	(9,698,000)	(63,000)	(173,000)
Cash flows from financing activities:			
Proceeds from notes payable, net		-	1,635,000
Private placement financing, net	15,934,000	7,301,000	-
Principle payments on notes payable, net of discount	(15,000)	(2,402,000)	-
Payment of preferred dividends		-	(48,000)
Repurchase of preferred and common stock		-	(360,000)
Proceeds from exercise of common stock options and warrants	5,784,000	105,000	2,776,000
Net cash provided by financing activities	21,703,000	5,004,000	4,003,000
Net increase (decrease) in cash and cash equivalents	11,376,000	1,563,000	1,828,000
Cash and cash equivalents, beginning of period	3,491,000	1,928,000	100,000

Cash and cash equivalents, end of period	$	14,867,000	$	3,491,000	$	1,928,000
Cash paid for interest	$	3,000	$	137,000	$	1,000
Cash paid for income taxes	$	5,000	$	2,400	$	2,400
Non-cash disclosures:						
Purchase of Langley PLC shares with common stock	$	-	$	-	$	2,380,000
Payments for patents with common stock	$	-	$	13,000	$	239,000
Conversions of preferred stock to common stock	$	17,835,000	$	-	$	354,000
Common stock issued to acquire assets related to equine feed supplement business	$	350,000	$	-	$	-
Adjustment to allocation of RiceX purchase price of property and equipment	$	375,000	$	-	$	-
Reduce goodwill for RiceX options cancelled	$	642,000	$	-	$	-
Change in fair value of marketable securities	$	78,000	$	-	$	-

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The accompanying notes are an integral part of these financials

NUTRACEA AND SUBSIDIARIES
Notes to Consolidated Financial Statements

NOTE 1 - ORGANIZATION AND LINE OF BUSINESS

General

We are 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") based on stabilized rice bran, rice bran derivatives and the rice bran oils.

On October 4, 2005, we consummated the acquisition of The RiceX Company (“RiceX”) pursuant to the terms of an Agreement and Plan of Merger, dated April 4, 2005. RiceX survived the merger as a wholly-owned subsidiary of NutraCea. RiceX stockholders received .076799 of NutraCea common stock for each share of RiceX common stock. RiceX shareholders received 28,272,064 shares of NutraCea common stock, valued at $29,120,000 and NutraCea assumed the outstanding RiceX options and warrants to purchase 11,810,496 shares NutraCea common stock, valued at $11,422,000.

In December of 2006, a wholly-owned subsidiary of NutraCea, Nutramercials, became a member of Infomaxx, LLC. Upon formation of the LLC, each party received a 50% voting interest. The purpose of Infomaxx is to create and promote infomercials for the marketing of NutraCea’s and the other member’s products. All product net revenues will be spilt with Nutramercials expecting to receive 55% of net revenues. As of December 31, 2006, $464,042 of assets and $200,000 of liabilities have been included in our audited consolidated balance sheet as a result of determining Informaxx, LLC is a variable interest entity in accordance with FIN 46 (R), “Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51”

Due to the acquisition of RiceX, and the subsequent reorganization, NutraCea and its subsidiaries are operating as one segment.

Our corporate offices are located at 1261 Hawk's Flight Court, El Dorado Hills, California 95762. Our corporate offices are scheduled to be moved to Phoenix, Arizona on or about the first week of April 2007 (see Note 9).

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation - The consolidated financial statements include the accounts of NutraCea and its wholly-owned subsidiaries, NutraCea Technologies Incorporated, NutraGlo® Incorporated, The RiceX Company, as well as Nutramercial’s interest in Infomaxx, LLC (collectively, the "Company"). All significant inter-company accounts and transactions are eliminated in consolidation.

Revenue Recognition - We derive our revenue primarily from product sales. Product is shipped when an approved purchase order is received. Products shipped by us are generally sold FOB Origin, with the customer taking title to the product once it leaves our plant via common carrier. At this point, the price to the customer is fixed and determinable, and collectibility is reasonably assured. On occasion, we receive purchase orders for multiple product deliveries. In these situations, each delivery is individually evaluated to determine appropriate revenue recognition. Each delivery is generally considered to be a separate unit of accounting for the purposes of revenue recognition and, in all instances, persuasive evidence of an arrangement, delivery, pricing and collectibility must be determined or accomplished, as applicable, before revenue is recognized. In addition, if the purchase order includes customer acceptance provisions, no revenue is recognized until customer acceptance occurs. Revenue is accounted for at the point of shipment FOB

Origin, unless accompanied by a memorandum of understanding detailing the requirement of customer acceptance in order to transfer title, in which case revenue is recognized at the time of such acceptance.

Occasionally, we will grant exclusive use of our labels by customers in specific territories in exchange for a nonrefundable fee. Under *EITF 00-21, Revenue Recognition with Multiple Deliverables,* each label licensing provision is considered to be a separate unit of accounting. Each grant is then individually evaluated to determine appropriate revenue recognition in accordance with *Staff Accounting Bulletin No. 104, Revenue Recognition (SAB 104))*, SAB 104 requires that four basic criteria must be met before revenue can be recognized: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred; (3) the selling price is fixed and determinable; and (4) collectibility is reasonably assured. Determination of criteria (3) and (4) are based on management's judgments regarding the fixed nature of the selling prices of the products delivered and the collectibility of those amounts. Provisions for allowances and other adjustments are provided for in the same period the related sales are recorded. If all criteria are met, revenue is recognized in the period in which the sale occurred and recorded in the financial statements as label fees.

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Our royalty fees are generally recognized when it is probable that an economic benefit will flow to us, the amount of the benefit can be reliably measured and collectibility is reasonably assured.

Cash and Cash Equivalents - We consider all highly liquid investments purchased with an original maturity of three months or less at the time of purchase to be cash equivalents. As of December 31, 2006, the Company maintains its cash and cash equivalents with a major investment firm and a major bank. At December 31, 2006, we have $1,000,000 in the form of an irrevocable letter of credit for one year as a security deposit for our new corporate headquarters in Phoenix, AZ.

Cash Concentration **-** We maintain its cash in bank accounts, which at times may exceed federally insured limits. We have not experienced any losses on such accounts.

Short-Term Investments - As part of our cash management program, we maintain a portfolio of commercial paper. The securities are investment grade (AAA) and maturity in thirty days.

Accounts Receivable - Accounts receivable consists of amounts due from customers for product sales, net of an allowance for losses. We determine the allowance for doubtful accounts by reviewing each customer account and specifically identifying any potential for loss. The allowance for doubtful accounts at December 31, 2006 and 2005 is $20,000. Uncollected accounts are written off after the customer has been past due in excess of twelve months. Past due status is determined based on contractual terms. Actual losses related to collection of accounts receivable for the years ended December 31, 2006, 2005 and 2004 were insignificant.

Marketable Securities - Marketable securities are marked to market at each period end. Any unrealized gains and losses on the marketable securities are excluded from operating results and are recorded as a component of Other Comprehensive Income (Loss). If declines in value are deemed other than temporary, losses are reflected in Net Income (Loss).

Inventory - Inventory is stated at the lower of cost (first-in, first-out) or market and consists of stabilized rice bran manufactured by RiceX, and nutraceutical products manufactured by NutraCea. We employ a full absorption procedure using standard cost techniques. The standards are customarily reviewed and adjusted annually. While the Company has an inventory of these products, any significant prolonged shortage of these ingredients or of the supplies used to enhance these ingredients could materially adversely affect the Company's results of operations.

Property and Equipment - Property and equipment are stated at cost. The Company provides for depreciation using the straight-line method over the estimated useful lives as follows:

Furniture and equipment	3-7	years
Automobile	5	years
Software	3	years
Leasehold improvements	2.4-7	years
Property and equipment	7-10	years

Expenditures for maintenance and repairs are charged to operations as incurred while renewals and betterments are capitalized. Gains or losses on the sale of property and equipment are reflected in the statements of operations.

Impairment of Long-Lived Assets **-** We assess the carrying value of long-lived assets which includes property, plant and equipment, intangible assets and goodwill annually or whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include the following:

- significant adverse change in legal factors or in the business climate;

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- unanticipated competition
- a loss of key personnel
- significant changes in the manner of our use of the asset;
- significant negative industry or economic trends; and
- our market capitalization relative to net book value.

Annually and upon the existence of one or more of the above indicators of impairment, we would test such assets for a potential impairment. The carrying value of a reporting unit, including goodwill, is considered impaired when the fair value is less than the asset's carrying value. In that event, an impairment loss is recognized based on the amount by which the carrying value exceeds the fair market value. Fair market value is determined primarily using quoted market prices and cash flow projections. We have determined that there is no impairment as of December 31, 2006 and 2005.

Patents and Trademarks - In addition to patents filed and acquired directly by the Company, the Company owns several patents, which were acquired from independent third parties and a related party. All costs associated with the patents are capitalized. Patents acquired from related parties are recorded at the carryover basis of the transferor. The Company paid cash as consideration for all patents and trademarks acquired, except the Via-Bran registered trademark, which was acquired for 21,409 shares of common stock valued at $21,000.

In conjunction with the RiceX acquisition, NutraCea has been assigned five U.S. patents relating to the production or use of Nutraceutical or HVF products. The patents include:

(1) Patent Number 5,512,287 "PRODUCTION OF BETA-GLUCAN AND BETA-GLUCAN PRODUCT," which issued on April 30, 1996;

(2) Patent Number 5,985,344 "PROCESS FOR OBTAINING MICRONUTRIENT ENRICHED RICE BRAN OIL," which issued on November 16, 1999;

(3) Patent Number 6,126,943 "METHOD FOR TREATING HYPERCHOLESTEROLEMIA, HYPERLIPIDEMIA, AND ATHEROSCLEROSIS," which issued on October 3, 2000;

(4) Patent Number 6,303,586 B1 "SUPPORTIVE THERAPY FOR DIABETES, HYPERGLYCEMIA AND HYPOGLYCEMIA," which issued on October 15, 2001; and

(5) Patent Number 6,350,473 B1 "METHOD FOR TREATING HYPERCHOLESTEROLEMIA, HYPERLIPIDEMIA AND ATHEROSCLEROSIS," which issued on February 26, 2002.

We plan to apply for additional patents in the future as new products, treatments and uses are developed.

Patents and trademarks are stated at cost. Amortization is computed on the straight-line method based on estimated useful lives as follows:

Patents (Domestic)	17	years
Patents (International)	20	years
Trademarks (Domestic)	10	years
Trademarks (International)	7	years

Deferred Compensation - Deferred compensation at December 31, 2005 represents the intrinsic value of options previously issued to employees that have not been vested. All such options have vested as of December 31, 2005.

Fair Value of Financial Instruments - The fair value of the Company's financial instruments approximated carrying value at December 31, 2006, 2005 and 2004. The Company's financial instruments include cash, marketable securities and accounts receivables for which the carrying value amount approximates fair value due to the short maturity of the instrument.

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Research and Development **-** Research and development expenses include internal and external costs. Internal costs include salaries and employment related expenses and allocated facility costs. External expenses consist of costs associated with product development. All such costs are charged to expense as incurred.

Stock and Warrants Issued to Third Parties - If none of the Company's agreements have a disincentive for nonperformance, the Company records a charge for the fair value of the stock and the portion of the warrants earned from the point in time when vesting of the stock or warrants becomes probable. The fair value of certain types of warrants issued to customers is recorded as a reduction of revenue to the extent of cumulative revenue recorded from that customer.

Stock-Based Compensation - Management estimates the fair value of each option award as of the date of grant using a Black-Scholes-Merton option pricing model. Expected volatility is based on the historical volatility of the Company's common stock. The expected term represents the period that the stock-based awards are expected to be outstanding. The risk free interest rate for the expected term of the option is based on the U.S. Treasury yield curve in effect at the time of grant. The expected dividend yield was not considered in the option pricing formula because the Company has not paid cash dividends historically and had no plans to do so at the grant date. In addition to these assumptions, management makes estimates regarding pre-vesting forfeitures that will impact total compensation expense recognized under the Plan.

As of January 1, 2006, we adopted the provisions of Statement of Financial Accounting Standards ("SFAS") No. 123 (R), *Accounting for Stock-Based Compensation*. Under the provisions of SFAS 123 (R), we are required to measure the cost of services received in exchange for an award of equity instruments based on the grant-date fair value of the award. That cost is recognized over the period during which services are provided in exchange for the award, known as the requisite service period (usually the vesting period). The Company applied the alternative transition method in calculating its pool of excess tax benefits available to absorb future tax deficiencies as provided by FSP FAS 123(R)-3, *Transition Election Related to Accounting for the Tax Effects of Share-Based Payment Awards*. Prior to January 1, 2006, the Company accounted for those insstruments under the recognition and measurement provisions of APB "Opinion" No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations, as permitted by FASB Statement No 123, *Accounting for Stock-Based Compensation*.

We have made the transition to SFAS 123 (R) using the modified prospective method. Under the modified prospective method, SFAS 123 (R) is applied to new awards and to awards modified, repurchased, or cancelled after January 1, 2006. Additionally, compensation cost for the portion of awards for which the requisite service has not been rendered (such as unvested options) that are outstanding as of January 1, 2006 are being recognized over the period that the remaining requisite services are rendered. The compensation cost relating to unvested awards at January 1, 2006 is based on the grant-date fair value of those awards. Under this method of implementation, no restatement of prior periods has been made.

As a result of adopting Statement 123 (R) on January 1, 2006, the Company's net income for the year ended December 31, 2006 is $1,907,711 lower than if it had continued to account for share-based compensation under Opinion 25. Basic and diluted earnings per share for the year ended December 31, 2006 would have been $(0.26), if the Company had not adopted Statement 123 (R), compared to reported basic and diluted earnings per share of $(0.29). Diluted earnings per share would not have cha nged. We have not recorded income tax benefits related to equity-based compensation expense as deferred tax assets are fully offset by a valuation allowance. As a result, the implementation of SFAS 123 (R) did not impact the Statement of Cash Flows for the year ended December 31, 2006.

The following table illustrates the effect on net loss and loss per share if the Company had applied the fair value recognition provisions of Statement 123 to options granted under the company's stock option plans for the years ended December 31, 2005 and 2004. For purposes of this pro forma disclosure, the value of the options is estimated using a Black-Scholes option-pricing model and amortized to expense over the options' vesting periods.

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	For the years ended December 31,			
		2005		2004
Net loss, reported:	$	(3,872,000)	$	(23,583,000)
Deduct: stock-based compensation expense included in reported net loss, net of $0 related tax benefits		1,511,000		20,998,000
(Add): stock-based compensation determined under fair value based method for all awards, net of $0 related tax benefits		(387,000)		(2,372,000)
Pro forma net loss	$	(2,748,000)	$	(4,957,000)
Basic loss per common share (basic and diluted):				
As reported	$	(0.10)	$	(1.18)
Pro forma	$	(0.07)	$	(0.25)

Shipping and Handling Expenses - All expenses relating to shipping and handling are expensed and reported as selling expenses.

Advertising Expense - The Company expenses all advertising costs, including direct response advertising, as they are incurred. Advertising expense for 2006, 2005 and 2004 was $307,000, $8,000 and $22,000, respectively.

Income Taxes - The Company accounts for its income taxes by recording a deferred tax asset or liability for the recognition of future deductible or taxable amounts and operating loss and tax credit carryforwards. Deferred tax expense or benefit is recognized as a result of timing differences between the recognition of assets and liabilities for book and tax purposes during the year.

Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Deferred tax assets are recognized for deductible temporary differences and operating loss, and tax credit carryforwards. A valuation allowance is established, when necessary, to reduce that deferred tax asset if it is “more likely than not” that the related tax benefits will not be realized.

Net Income (Loss) per Common Share - Basic earnings per share is computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common and potentially dilutive shares outstanding during the period. Potentially dilutive shares consist of the incremental common shares issuable upon the exercise of stock options and warrants. Potentially dilutive shares are excluded from the computation if their effect is antidilutive. We had a net loss for 2005 and 2004 presented herein; therefore, none of the stock options and warrants outstanding during each of the periods presented, as discussed in Notes 12 and 13, were included in the computation of diluted loss per share as they were antidilutive. For 2006, the dilutive effect of 5,873,738 net share outstanding options, 14,666,449 net share outstanding warrants, 940,000 convertible Series B preferred stock, and 6,430,368 convertible Series C preferred stock is calculated using the treasury stock method. Additionally, 2,083,114 net shares outstanding warrants and options there is no dilutive effect because the average market price of the common stock during the period is less than the exercise price of the

warrants and options for 2006.

Estimates -The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Concentrations of Credit Risk and Major Customers - On August 24, 2005, NutraCea signed an agreement with a direct response marketing company to market and sell products through infomercials. The agreement is for two years and may be extended for an additional year. The agreement covers pricing of specific products at wholesale prices which will be private labeled for direct sale by the marketing company. During the term of the agreement, NutraCea will not sell its products through any other infomercials so long as the marketing company maintains minimum quarterly orders beginning October 1, 2005 of $500,000. Additionally, NutraCea granted the company an option to purchase 250,000 shares of restricted common stock at a price of $1.275 per share. The options vest 50,000 shares upon payment in full of the contract quarter minimum purchase orders during the term of the agreement. At December 31, 2006, 100,000 options are fully vested. For the year ended December 31, 2005, sales to this customer totaled $3,013,000 or 54% of total sales and receivables were $1,910,000, or 76% of total receivables. For the year ended December 31, 2006, sales to this customer totaled $8,057,000 or 48% of total sales and receivables were $3,516,000, or 49% of total receivables.

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Reclassifications - Certain reclassifications have been made to the prior year statement of operations to conform to the current year presentation.

Recently Issued Accounting 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 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 will adopt FIN 48 as of January 1, 2007, as required. The Company has determined that there is no impact in adopting FIN 48.

In September 2006, the SEC staff issued Staff Accounting Bulletin No. 108 (SAB 108), “Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements,” which addresses how uncorrected errors in previous years should be considered when quantifying errors in current-year financial statements. SAB 108 requires companies to consider the effect of all carry over and reversing effects of prior-year misstatements when quantifying errors in current-year financial statements and the related financial statement disclosures. SAB 108 must be applied to annual financial statements for the first fiscal year ending after November 15, 2006. The impact of adopting SAB 108 is in Note 3.

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. We have not determined the effect that the adoption of FAS 157 will have on our consolidated results of operations, financial condition or cash flows.

NOTE 3 - IMPLEMENTATION OF STAFF ACCOUNTING BULLETIN NO. 108

In preparing the financial statements for the year ended December 31, 2006, we undertook an evaluation of uncorrected misstatements arising in prior years for the purpose of implementing Staff Accounting Bulletin No. 108 (SAB 108). We identified an uncorrected misstatement arising 2004, which at the time was considered to be immaterial relative to the net loss incurred for the period. We believe that this uncorrected misstatement resulted from the incorrect classification and recording of an investment's decline in market value as a temporary impairment with a corresponding increase in other comprehensive loss. In accordance with the provisions of SAB 108, we have decreased accumulated other comprehensive loss at January 1, 2006 by $2,090,000 and we have increased our accumulated deficit at January 1, 2006 by $2,090,000 to recognize the other than temporary nature of the investment impairment.

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NOTE 4 - MARKETABLE SECURITIES

On September 8, 2004, NutraCea purchased 1,272,026 shares of Langley Park Investment Trust, PLC, a United Kingdom closed-end mutual fund, which is actively traded on a London Stock Exchange. NutraCea paid with 7,000,000 shares of its own common stock. Per the Agreement, NutraCea may 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 are escrowed for a 2-year period. At the end of the period, Langley's NutraCea shares are measured for any loss in market value and if so, NutraCea must give up that pro-rata portion of its Langley shares up to the escrowed 636,013 shares.

As of December 31, 2006, the NutraCea shares had not lost any value. However, the Langley shares are marked down to their fair market value of $368,000. At December 31, 2005, the Langley shares were valued at their fair market value of $290,000.

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

On September 8, 2006, the Company filed a complaint in the United States District Court for the Eastern District of California, Sacramento Division, against Langley for, among other causes of action, securities fraud, breach of contract and rescission relating to this transaction, The company also filed a placeholder complaint in the State of New York to preserve its rights relative to venue and jurisdictional issues. The Company is seeking rescission of the Stock Purchase Agreement and return of all of the Company's shares issued to and held by Langley, in addition to injunctive relief to prevent the transfer of the shares held by Langley. The Company is also seeking compensatory damages representing the loss in value as well as attorneys' fees and costs incurred in the litigation.

On March 27, 2007, NutraCea and Langley settled this matter. Pursuant to the settlement, NutraCea will receive $1,250,000 from Langley and NutraCea will retain all 1,272,026 shares of Langley common stock.

NOTE 5 - PROPERTY AND EQUIPMENT

Property and equipment consisted of the following at December 31:

		2006		**2005**
Land	$	9,000	$	5,000
Furniture and equipment		916,000		697,000
Automobile		73,000		73,000
Software		389,000		367,000
Leasehold improvements		430,000		396,000
Property and plant		4,197,000		4,511,000
Construction in progress		4,392,000		0
Subtotal		10,406,000		6,049,000
Less accumulated depreciation		1,445,000		556,000
Total	**$**	**8,961,000**	**$**	**5,493,000**

Depreciation expense was $839,000, $241,000 and $315,000 for 2006, 2005 and 2004 respectively.

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NOTE 6 - PATENTS AND TRADEMARKS

Patents and trademarks consisted of the following at December 31:

	2006	2005
Patents	$ 2,540,000	$ 2,457,000
Trademarks	2,787,000	80,000
Subtotal	5,327,000	2,537,000
Less Accumulated Amortization	430,000	119,000
Total	**$ 4,897,000**	**$ 2,418,000**

Amortization expense was $302,000 and $70,000 for 2006 and 2005, respectively. Amortization expense for the next five years will be approximately $1,555,000.

NOTE 7 - NOTES RECEIVABLE

At December 31, 2006, we have seven secured promissory notes outstanding to the Company with an aggregate amount of $2,376,000, $1,694,000 reported as current and $682,000 reported as long-term. These secured promissory notes bear interest at annual rates of either five (5%) or eight (8%) with the principals and all accrued interest due and payable to us at dates ranging from February 2007 to October 2012.

We determined the note receivable of 5% to bear an interest rate that is lower than the current market rate. Therefore, we have recorded a discount on this note of $5,500, assuming market rate of 8.5%, and is accreting this discount using the effective interest method over the life of the note.

NOTE 8 - NOTES PAYABLE

In December 2004 we executed three promissory notes to third party investors totaling $2,400,000. The notes were for a one year term, bear interest at 7% interest compounded quarterly and were secured by all of our assets. The holders were issued warrants to purchase a total of 2,400,000 shares of our common stock at an exercise price of $0.30 per share. The warrants are immediately exercisable and expire in seven years from the date of issuance. A discount on the debt of $786,000 was recorded for these warrants and was being amortized over the life of the notes. At October 4, 2005, the principle and interest on the three promissory notes were paid in full.

NOTE 9 - INCOME TAXES

Income tax expense is reported in selling, general and administrative expenses and consists of $5,000, $2,400 and $2,400 for the years ended December 31, 2006, 2005 and 2004, respectively.

Deferred tax assets (liabilities) are comprised of the following at December 31:

	2006	2005
Net operating loss carryforward	$ 14,860,000	$ 10,330,000
Marketable securities	801,000	833,000
Stock options and warrants	-	587,000

Other	39,000	14,000
Intangible assets	(275,000)	10,000
Property and equipment	(1,341,000)	(1,790,000)
	14,084,000	9,984,000
Less valuation allowance	(14,084,000)	(9,984,000)
	$ -	$ -

Deferred taxes arise from temporary differences in the recognition of certain expenses for tax and financial reporting purposes. At December 31, 2006 and 2005, management determined that realization of these benefits is not assured and has provided a valuation allowance for the entire amount of such benefits. At December 31, 2006, net operating loss carryforwards were approximately $25,018,000 for federal tax purposes that expire at various dates from 2011 through 2020 and $12,230,000 for state tax purposes that expire in 2010 through 2015.

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The Company has an income tax benefit of $14,100,000 resulting from the exercise of options and warrants during 2006. This benefit can only be recognized if the net operating losses are used in future periods or if net operating losses expire and will be recorded in equity.

Utilization of net operating loss carryforwards may be subject to substantial annual limitations due to the “change in ownership” provisions of the Internal Revenue Code of 1986, as amended, and similar state regulations. The annual limitation may result in the expiration of substantial net operating loss carryforwards before utilization.

The provision for income taxes differs from the amount computed by applying the U.S. federal statutory tax rate (34%) to income taxes as follows for the year ended December 31:

	2006	2005	2004
Income tax expense (benefit) at federal statutory rate	$ 541,000	$ (1,316,000)	$ (8,017,000)
Increase (decrease) resulting from:			
State franchise tax expense (benefit), net of federal tax effect	92,000	(224,000)	(1,368,000)
Change in valuation allowance	(608,000)	(3,202,000)	8,584,000
Other, net	(25,000)	32,000	801,000
RiceX acquisition	-	4,710,000	-
	$ -	$ -	$ -

NOTE 10 - COMMITMENTS AND CONTINGENCIES

Employment contracts

Minimum future payments for key employees as of December 31are as follows:

2007	$ 1,126,000
2008	272,000
Total	**$ 1,398,000**

Generally, if we terminate these agreements without cause or the employee resigns with good reason, as defined, we will pay the employees' salaries, bonuses, and benefits payable for the remainder of the term of the agreements.

Leases

We lease our office, laboratory and warehouse space in El Dorado Hills, California under a lease agreement with Roebbelen that expires in February 2007 and requires monthly payments of $6,442. We also lease warehouse spaces in West Sacramento, California which expire in July of 2007 for $5,440 per month. RiceX leases office space in Burley, Idaho at a rate of $550 per month, expiring in May of 2009.

On November 14, 2006, NutraCea signed a 63-month lease with Transwestern for 26,147 square fee of office space at 5090 North 40th Street, Phoenix, Arizona in anticipation of moving our corporate headquarters to Phoenix, Arizona in early 2007. The monthly lease payments escalate from $58,830.75 to $67,546.42 during the lease term.

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Future minimum payments under these leases at December 31, 2006 were as follows:

Year Ending December 31,		
2007	$	605,000
2008		729,000
2009		750,000
2010		775,000
2011		801,000
2012		371,000
Total	**$**	**4,031,000**

Rent expense was $124,000, $111,000 and $65,000 for the years ended December 31, 2006, 2005 and 2004, respectively.

Litigation

On July 16, 2002, the Company was summoned to answer a Complaint filed by Faraday Financial, Inc. (“Faraday”) in District Court, County of Salt Lake, Utah (Case No. 020906477). The Complaint alleges that the Company issued convertible promissory notes totaling $450,000 and a promissory note totaling $50,000. On December 13, 2001, Faraday entered into a settlement agreement with the Company, whereby Faraday agreed to cancel the promissory notes in exchange for 735,730 shares of preferred stock. Faraday claims that the settlement agreement required that the Company effect a registration statement covering the preferred stock by June 30, 2002, which the Company failed to do, and demands the Company immediately forfeit to Faraday 735,730 shares of common stock owned by the Chief Executive Officer of the Company. Faraday has filed its fourth claim for relief for a judgment against the Company for $500,000, plus accrued, but unpaid interest, attorneys’ fees and costs, and other such costs. A Settlement Agreement was executed on December 10, 2003. In consideration for the mutual releases, Faraday converted 735,730 preferred into 735,730 common shares and $90,000 of accrued preferred dividends into 1,201,692 common shares. Within the next year, if Faraday cannot realize $552,000 and approximately $10,000 in legal expenses from the sale of the common shares, NutraCea will make up any deficiency. If stock sale exceeds $562,000, Faraday is entitled to keep any excess. Subsequent to December 31, 2003, the Company issued an additional 250,000 shares to Faraday. Concurrently, with the executed Settlement Agreement, a joint stipulated motion to stay all proceedings was filed with the Court. After all the above conditions are met, if Faraday has not lifted the stay within 18 months of December 10, 2003, NutraCea shall deliver to Faraday an executed stipulation for dismissal with prejudice of the Complaint and Counterclaim. In 2005, we issued the final 97,000 shares, valued at $98,000, to Faraday to settle in full the executed Settlement Agreement.

NutraCea commenced a lawsuit on September 8, 2006 against Langley Park Investments, PLC, a United Kingdom Corporation (“Langley”) in the United States District Court for the Eastern District of California, Sacramento Division. The factual basis underlying that case involved a private-placement transaction in which NutraCea exchanged 7 million restricted shares of its common stock for 1,272,026 ordinary shares of Langley common stock (the “Langley Shares”), half of which were immediately saleable by NutraCea and half of which were placed in escrow subject to certain conditions. After the commencement of the litigation, the parties entered into a Pre-Settlement/Escrow Agreement, pursuant to which they agreed that the proceeds from Langley’s sale of certain NutraCea shares, totaling $2.5 million, would be deposited into an escrow account. The matter has now been settled. Pursuant to the settlement, NutraCea will receive $1.25 million from the $2.5 million held in escrow (Langley will receive the remainder), and

NutraCea will retain all of the Langley Shares.

In addition to the matter discussed above, 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.

NOTE 11- THE RICEX ACQUISITION

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On October 4, 2005, NutraCea merged with RiceX. The stockholders of RiceX received 28,272,064 shares of NutraCea common stock in exchange for 100% of the shares of RiceX common stock, and NutraCea assumed the outstanding options and warrants to purchase 11,810,496 shares of RiceX common stock.

On October 4, 2005, certain investors purchased an aggregate of 7,850 shares of Series B Convertible Preferred Stock at a price of $1,000 per share. Additionally, the investors were issued warrants to purchase an aggregate 7,850,000 shares of common stock at an exercise price of $0.70 per share. An advisor for the financing received a customary fee based on aggregate gross proceeds received from the investors and a warrant to purchase 1,099,000 shares of common stock at an exercise price per share of $0.50 per share.

The acquisition was accounted for using the purchase method of accounting. The purchase price allocation included within these Consolidated Financial Statements is based on a purchase price of $40,542,000 calculated as follows:

NutraCea shares issued		28,272,064
Price per share (NutraCea closing price, October 4, 2005)	$	1.03
Aggregate value of NutraCea common stock consideration	$	29,120,000
Value of the RiceX warrants and options assumed		11,422,000
Total consideration	$	40,542,000
Fair value of identifiable net assets acquired:		
Estimate of fair value adjustment of property, plant and equipment	$	5,600,000
Acquired other net tangibles assets		611,000
Estimate of fair value adjustment of RiceX intellectual property		2,000,000
Goodwill		32,331,000
Total	**$**	**40,542,000**

The purchase price allocation is based on estimates and assumptions. This information is presented for informational purposes only.

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The accompanying unaudited pro forma condensed combined consolidated statement of operations for the year ended December 31, 2005 is presented for illustrative purposes only and does not give effect to any cost savings, revenue synergies or restructuring costs which may result from the integration of NutraCea and RiceX's operations. In addition, actual results may be different from the projections set forth in this unaudited pro forma condensed combined consolidated statement of operations.

Unaudited Pro Forma Condensed Combined Consolidated
Statement of Operations
Year Ended December 31, 2005

	HISTORICAL		PRO FORMA		
Income Statement	NutraCea	RiceX	Adjustment		Combined
Revenues					
Net sales	$ 4,569,000	$ 3,838,000	$ (325,000)	(a)	$ 8,082,000
Total Revenues	$ 4,569,000	$ 3,838,000	$ (325,000)		$ 8,082,000
COGS	$ 2,523,000	$ 1,533,000	$ (325,000)	(b)	$ 3,731,000
Gross Profit	$ 2,046,000	$ 2,305,000	$ -		$ 4,351,000,
Sales, General and Administrative	$ 2,853,019	$ 5,085,000	$ (55,000)	(c)	$ 7,883,019
Research and Development	$ 262,000	$ 267,000			$ 529,000
Stock Option and Warrant Expense	$ 1,511,000	$ -			$ 1,511,000
Investor Relations	$ -	$ 41,000			$ 41,000
Professional Fees	$ 109,000	$ 914,029			$ 1,023,029
Loss From Operations	$ (2,689,019)	$ (4,002,029)	$ (55,000)		$ (6,636,048)
		$ -	$ -		$ -
Interest Income		$ 10,000	$ -		$ 10,000
Interest Expense	$ (878,000)				$ (878,000)
Provision for income tax	$ -	$ (2,000)			$ (2,000)
Total other income (expense)	$ (878,000)	$ 8,000	$ -		$ (870,000)
Net Loss	$ (3,567,019)	$ (3,994,029)	$ 55,000		$ (7,506,048)
Cumulative Preferred dividends	$ -	$ -			$ -
	$ (3,567,019)	$ (3,994,029)	$ 55,000		$ (7,506,048)

Net Loss Available to Common Shareholders						
Basic and Diluted Loss per share	$	(0.10)	(0.01)		$	(0.11)
Basic Shares Outstanding		38,830,015	28,272,064	(d)		67,102,079

(a) Represents the elimination of intercompany sales
(b) Represents the elimination of intercompany cost of sales
(c) Represents the elimination of intercompany rent expense of sublease
(d) Represents the net change in total combined common stock outstanding

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NOTE 12 - PREFERRED AND COMMON STOCK

Convertible, Redeemable Series A Preferred Stock

Our Series A preferred stock was convertible at the option of the holder at $1 per share into our common stock, subject to certain anti-dilution provisions. In addition, the Series A preferred stock will automatically convert into common stock in the event of a qualified public trading benchmark, which is defined as (i) the common stock is listed on a national exchange at twice its conversion price or (ii) the common stock is quoted on the over-the-counter bulletin board at an average bid price of at least $1.25 per share over any 30-day trading period. At December 31, 2004, all the outstanding preferred stock was either repurchased or converted under option (ii) above.

During the year ended December 31, 2004, we:

Repurchased 130,000 shares of preferred stock for $130,000;

Converted 540,000 shares of preferred stock into 630,000 shares of common stock valued at $348,000; and,

Issued 5,759 shares of common stock in payment of preferred stock dividends due in the amount of $6,000.

Convertible, Series B Preferred Stock

On October 4, 2005, certain investors purchased an aggregate of 7,850 shares of Series B Convertible Preferred Stock at a price of $1,000 per share pursuant to the Purchase Agreement. The preferred shares can be converted to shares of common stock at a conversion rate of 2,000 shares of common stock for each preferred share issued in the transaction. Additionally, pursuant to the Purchase Agreement, the investors were issued warrants to purchase an aggregate 7,850,000 shares of common stock at an exercise price of $0.70 per share, valued at $7,690,000. The warrants have a term of five years and are immediately exercisable.

An advisor for the financing received a customary fee based on aggregate gross proceeds received from the investors and a warrant to purchase 1,099,000 shares of common stock at an exercise price per share of $0.50 per share valued at $1,086,000.

During the year ended December 31, 2006, fourteen Series B shareholders converted 7,380 shares of preferred stock into 14,760,000 shares of common stock. The preferred shares converted at a conversion rate of 2,000 shares of common stock for each preferred shares.

Convertible, Series C Preferred Stock

On May 12, 2006, we sold an aggregate of 17,560 shares of our Series C Convertible Preferred Stock at a price of $1,000.00 per share in connection with a private placement for aggregate gross proceeds of approximately $17,560,000 ($15,934,000 net after offering and related expenses). The Series C preferred shares can be converted to shares of our common stock at a conversion rate of approximately 1,176 shares of common stock for each preferred share. Additionally, the investors were issued warrants to purchase an aggregate of 10,329,412 shares of our common stock at an exercise price of $1.35 per share. The warrants have a term of five years and are immediately exercisable.

Halpern Capital, Inc. acted as advisor and placement agent for the financing and received a customary fee based on aggregate gross proceeds received from the investors and a warrant to purchase 500,000 shares of NutraCea's common stock at an exercise price per share of $1.35. The warrants have a five-year term and are immediately exercisable.

During the year ended December 31, 2006, thirty Series C Shareholders converted 12,092 shares of preferred stock into 14,225,854 shares of common stock. The preferred shares converted at a conversion rate of 1,176 shares of common stock for each preferred shares.

Common Stock

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On March 25, 2004, we established the NutraCea Patent Incentive Plan, which grants 15,000 shares of common stock to each named inventor on each granted patent, which is assigned to NutraCea. Under the terms of this plan during the year ended December 31, 2004, NutraCea issued 180,000 shares of common stock valued at $239,000. During the year ended December 31, 2005, the Company issued 30,000 shares of common stock valued at $13,000.

During the year ended December 31, 2004, we:

Issued 280,000 shares of common stock to two consultants in settlement of contractual agreements valued at $478,000;

Issued 5,500,000 shares of common stock valued at $8,360,000 to Patricia McPeak, our former Chief Executive Officer for services and cancellation of indebtedness;

Repurchased 344,956 shares of common stock valued at $230,000 from Patricia McPeak the former Chief Executive Officer of NutraCea pursuant to a repurchase agreement;

Converted preferred dividends in the amount of $6,000 into 5,759 shares of common stock;

Issued 3,767,950 shares of common stock to consultants for services rendered valued at $2,542,000;

Issued 640,000 shares of common stock to officers and directors for services rendered valued at $928,000;

Issued 168,626 shares of common stock to vendors in payment of accounts payable totaling $58,000;

Issued 6,579,323 shares of common stock pursuant to the exercise of stock options for cash totaling $2,776,000; and

Converted 540,000 shares of preferred stock to 630,000 shares of common stock pursuant to the Mandatory Conversion paragraph of the Private Placement Memorandum dated November 9, 2001.

On September 8, 2004, NutraCea and Langley Park Investments PLC (“Langley”) signed a Stock Purchase Agreement under which NutraCea agreed to sell 7,000,000 shares of its common stock to Langley. The transaction will close at the time that Langley’s shares are trading on the London Stock Exchange for anticipated consideration to NutraCea (i) immediately following the closing of approximately $1,190,000 U.S.D. in Langley stock, and (ii) additional consideration of that number of Langley shares which, as of the closing, will have a value of approximately $1,190,000 (the “Langley Shares”). NutraCea has agreed to hold the Langley Shares in escrow for two years from the date of closing. After the two-year holding period, the Langley Shares will be subject to possible reduction in number if NutraCea’s common shares are trading at a value of less than $0.34 U.S.D. After such reduction, if any, the remaining Langley Shares may be sold by NutraCea at their then current value. Pursuant to the Purchase Agreement, Langley has agreed that it will not sell, transfer or assign any or all of the NutraCea shares for a period of two years following the closing without the prior written consent of NutraCea, which consent may be withheld by NutraCea in its sole discretion.

During the year ended December 31, 2005, we:

Issued 1,904,805 shares of common stock to seven consultants for services rendered, valued at $907,000;

Issued 70,000 shares of common stock to two officers and directors, valued at $30,000;

Issued a total of 30,000 shares of common stock to two consultants under the Patent Incentive Plan, valued at $13,000; and

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Issued 97,000 shares of common stock, valued at $98,000, to Faraday, which was the last required payment to Faraday under the Settlement Agreement dated December 10, 2003.

During the year ended December 31, 2006, we:

Issued 29,999 shares of common stock to a consultant for services rendered, valued at $30,000;

Issued 1,742,723 shares of common stock for the cashless exercise of options/warrants.

NOTE 13 - STOCK OPTIONS AND WARRANTS

Expense for stock options and warrants issued to consultants is calculated at fair value using the Black-Scholes valuation method.

On October 31, 2003, the Board of Directors approved and adopted the 2003 Stock Compensation Plan and authorized the President of the Company to execute a registration statement under the Securities Act of 1933 for 10,000,000 shares of common stock. As of December 31, 2005, 9,966,208 shares of common stock and no options have been granted under the 2003 Stock Compensation Plan. As of December 31, 2006, 9,996,207 shares of common stock and no options have been granted under the 2003 Stock Compensation Plan.

The expense, if any, of stock options issued to employees is recognized over the shorter of the term of service or vesting period. The expense of stock options issued to consultants or other third parties are recognized over the term of service. In the event services are terminated early or no specific future performance is required by the Company, the entire amount is recognized.

During the year ended December 31, 2004, we:

Issued 6,998,493 warrants with exercise prices between $0.001 and $5.00 per share to consultants, which were valued at $7,762,000, which expire at varying times between six months and five years;

Issued 25,000 employee stock options with an exercise price of $0.20, which expire in five years;

Issued 8,000,000 stock options to two officers with an exercise price of $0.30, expiring in 10 years, valued at $800,000; and

Issued 2,400,000 warrants with an exercise price of $0.30, in conjunction with notes payable issued by us during the quarter. The warrants are immediately exercisable and expire seven years from the date of issuance. A total of $786,000 of accrued debt discount expense was recorded relating to the issue of these warrants and was amortized over the term of the notes payable.

During the year ended December 31, 2005, we:

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Assumed 11,810,496 options and warrants with exercise prices between $0.15 and $1.66 per share relating to the acquisition of RiceX. The warrants expire at varying times between 9 months and 10 years;

Issued 1,305,000 options and warrants to purchase common stock to ten consultants valued at $349,000; The warrants expire from three-five years, and have exercise prices between $0.30 and $1.275 per share;

Issued 1,099,000 warrants to purchase common stock, valued at $1,086,000, for commissions to the underwriter relating to the private placement of Series B preferred stock. The warrants have an exercise price of $0.50 and expire in five years;

Issued 7,850,000 warrants to purchase common stock to 17 investors in conjunction with the Series B preferred stock private placement, valued at $7,690,000, exercisable for $0.70 and expiring in five years;

Issued 2,200,000 options to 3 employees, which are exercisable between $0.30 and $0.46 per share, expiring in ten years;

Exercised 531,000 options and warrants for common stock for cash in the amount of $105,000; and,

Issued 66,666 shares of common stock in exchange for 100,000 options and warrants for a cashless exercise.

During the year ended December 31, 2006, we:

Issued 17,560 shares of our Series C Convertible Preferred Stock at a price of $1,000 per share in connection with a private placement for aggregate gross proceeds of approximately $17,560,000 ($15,934,000 net, after offering and related expenses).

Issued 10,329,411 warrants to purchase common stock to 33 investors in conjunction with the series C preferred private placement, valued at $13,524,000, immediately exercisable for $1.35 and expiring in five years;

Issued 500,000 warrants to purchase common stock, valued at $655,000, for commissions relating to private placement of series C preferred stock. The warrants are immediately exercisable at $1.35 and expire in five years;

Issued a total of 1,600,000 options to purchase common stock to 17 employees, non-employee directors and a medical advisor to the board of directors, vesting from immediately to 2 years, expiring in 3-10 years, with exercise prices of $1.00 to $2.50 per share;

Issued a total of 700,000 warrants to purchase common stock to 12 consultants, vesting from immediately to performance contingencies, expiring in 3-4 years, with exercise prices of $1.00 to $2.40 per share;

Canceled and/or expired 869,150 options and warrants, including 626,030 RiceX options.

Exercised 5,635,064 options and warrants for common stock for cash in the amount of $5,784,000; and

Issued 1,842,723 shares of common stock in exchange for 2,520,000 options and warrants for a cashless exercise.

Issued 297,108 shares of common stock in connection with our equine feed assets purchase, valued at $350,000;

Issued 5,635,064 shares of common stock for the exercise of options and warrants for cash in the amount of $5,784.000;

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Notes to Consolidated Financial Statements

The Company's stock options and warrants outstanding, exercisable, exercised and forfeited are as follows:

	Options Employee, Directors		Warrants Consultants, Investors	
Stock option and warrant transactions:	Weighted Average Exercise Price	Number of shares	Weighted Average Exercise Price	Number of shares
Outstanding balance January 1, 2004	$ 0.56	764,700	$ 0.98	3,196,819
Granted	$ 0.30	8,025,000	$ 0.62	9,598,493
Expired or canceled	$ -	-	$ 4.94	(220,833)
Exercised	$ 0.01	(500,000)	$ 0.43	(6,479,323)
Outstanding balance December 31, 2004	$ 0.34	8,289,700	$ 0.85	6,095,156
Exercisable balance December 31, 2004	$ 0.34	8,289,700	$ 0.85	5,846,156
Outstanding balance January 1, 2005	$ 0.34	8,289,700	$ 0.85	6,095,156
Granted	$ 0.31	2,200,000	$ 0.67	10,554,000
Expired or canceled	$ -	-	$ 0.01	(135,004)
Exercised	$ -	-	$ 0.12	(531,000)
Assumed	$ 0.36	8,047,765	$ 0.69	3,762,742
Outstanding balance December 31, 2005	$ 0.34	18,537,465	$ 0.75	19,745,894
Exercisable balance December 31, 2005	$ 0.35	16,837,465	$ 0.74	19,115,894
Outstanding balance January 1, 2006	$ 0.34	18,537,465	$ 0.75	19,745,894
Granted	$ 1.36	1,600,000	$ 1.35	11,629,411
Expired or canceled	$ 0.32	(693,244)	$ 0.54	(175,906)
Exercised	$ -	-	$ 0.65	(8,155,064)
Outstanding balance December 31, 2006	$ 0.43	19,444,221	$ 1.03	23,044,335
Exercisable balance December 31, 2006	$ 0.35	17,589,504	$ 1.01	22,443,726

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The Company determines fair value at grant date using the Black-Scholes option pricing model that takes into account the stock price at the grant date, the exercise price, and the expected life of the option, the volatility of the underlying stock and the expected dividend yield and the risk-free interest rate over the expected life of the option.

The weighted average assumptions used in the pricing model are noted in the table below. The expected term of options is derived using the simplified method, which is based on the average period between vesting term and expiration term of the options. The risk free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of the grant. Expected volatility is based on the historical volatility of the Company's stock over a period commensurate with the expected term of the options. The Company believes that historical volatility is indicative of expectations about its future volatility over the expected term of the options.

For options granted after January 1, 2006, and valued in accordance with FAS 123R, the Company expenses the fair value of the option on a straight-line basis over the vesting period for each separately vesting portion of the award. The Company estimates forfeitures and only recognizes expense for those shares expected to vest. Based upon historical evidence, the Company has determined that an expected forfeitures rate ranging from 5% to 10%.

In the years ended December 31, 2005 and 2004, the fair value of compensation expense relating to non-employees stock option grants was estimated on the date of the grant in accordance with FAS123, using The Black-Scholes option-pricing model and the following weighted average assumptions:

	2006	2005	2004
Weighted average fair value of options granted	$ 1.35	$ .54	$ .69
Risk-free interest rate (2005 & 2004)		2.0%	2.0%
Federal reserve treasury rates (2006)	3.83-5.08%		
Expected life (years)	2-5	2-10	3-8
Expected volatility	124-305%	112-166%	77-251%
Expected dividends	0	0	0

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A summary of option activity under our equity-based compensation plans as of December 31, 2006, and changes during the year then ended is presented below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at January 1 , 2006	38,283,359	$ 0.55	4.99	$ 7,556,000
Granted	13,229,411	$ 1.35		
Exercised	8,155.064	$ 0.65		
Forfeited/Expired	869,150	$ 0.36		
Outstanding at December 31, 2006	42,488,556	$ 0.76	4.86	$ 79,111,000
Exercisable at December 31, 2006	40,033,230	$ 0.72	4.35	$ 74,147,000

Shares issued to non-employees reflected in the table above include 19,745,894 outstanding at January 1, 2006, 11,629,411 granted, 175,906 forfeited or canceled, and 8,155,064 exercised during the year ended December 31, 2006, resulting in 23,044,335 shares outstanding and 22,443,721 exercisable at December 31, 2006.

The weighted-average grant-date fair value of options granted during 2006 was $1.35. The weighted-average grant-date fair value of options calculated in accordance with FAS 123 granted during 2005 and 2004 was $0.67 and $0.47, respectively. The total intrinsic value of options exercised during the years ended December 31, 2006, 2005, and 2004 was $6,329,380, $575,364, and $1,297,178 respectively. The total fair value of options vested during the years ended December 21, 2006, 2005, and 2004 was $733,000, $479,000, and $7,762,000, respectively.

Non-vested shares relating to non-employees reflected include 630,000 shares outstanding at January 1, 2006, 432,500 shares granted, 181,886 vested shares, 280,000 forfeited or expired shares during the year ended December 31, 2006, resulting in 600,614 non-vested shares outstanding at December 31, 2006.

As of December 31, 2006, there was $1,799,000 of total unrecognized compensation cost related to non-vested options granted under the plans. That cost is expected to be recognized over a weighted average period of one year.

Cash received from warrant and stock options exercises for the years ended December 31, 2006, 2005, and 2004 was $5,784,000, $105,000, and $2,776,000, respectively.

There is no tax effect on the exercise of options in the statement of cash flows because the Company has a full valuation allowance against its deferred income tax assets.

The Black-Scholes option valuation model requires the input of highly subjective assumptions, including the expected life of the stock-based award and stock price volatility. The assumptions listed above represent management's best estimates, but these estimates involve inherent uncertainties and the application of management judgment. As a result, if other assumptions had been used, the Company's recorded stock-based compensation expense could have been materially different from that previously reported in proforma disclosures. In addition, the Company is required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. If the Company's actual forfeiture rate is materially different from the estimate, the share-based compensation expense could be materially different.

NOTE 13 - RELATED PARTY TRANSACTIONS

In November 2004, the Board of Directors resolved to purchase a new automobile valued at $73,000 for use by Patricia McPeak, the former Chief Executive Officer. Ms. McPeak waived a car allowance in exchange for use of the automobile.

In 2004, two directors received 100,000 shares of common stock each, to serve as the Chairman of the Medical Advisory Board and the Corporate Medical Director.

Also, in 2004, a director-owned partnership received 300,000 shares of common stock and options to purchase 300,000 shares of common stock, exercisable at $1.00, with 100,000 options vesting immediately and the remaining 200,000 options vesting at 50,000 options per year.

In the first quarter of 2005, 70,000 shares of common stock, valued at $30,000, were issued to two directors.

In April 2005, a direct response marketing company agreed to compensate our former Chief Executive Officer, Patricia McPeak, whereby she will receive a royalty per unit sold resulting from infomercials that will demonstrate specific products of ours. Pursuant to this agreement, Ms. McPeak should have earned approximately $1,176,000 and $270,000 in 2006 and 2005, respectively from this direct marketing company. The agreement provides for royalty payments to be made for two years by the direct response marketing company and is not an obligation of ours.

In February 2006, we issued a warrant to purchase 100,000 shares of common stock to a member of our Board of Directors for services rendered. The warrant expires in five years, has an exercise price of $1.00 per share, and was

charged to stock, stock option and warrant expense in the amount of $100,000.

In May 2006, we issued to each of our six non-employee directors an option to purchase 35,000 shares (totaling 210,000 option shares). The options expire in ten years, have an exercise price of $1.14 per share, vest on a twelve-month prorated basis and were charged to stock, option and warrant expense in the amount of $119,000 for the year ending December 31, 2006.

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In May 2006, we issued 381,996 shares of common stock to a customer in an asset purchase agreement related to their trademarks associated with the equine market valued at $450,000.

In December 2006, we issued 75,000 warrant shares of common stock to a member our limited liability company, contingent upon certain performance. A portion of these warrants were deemed to be probable of vesting. The value of the 25,000 probable vesting warrant shares was $16,000 and had an exercise price of $2.38. They will expire in December of 2009.

NOTE 14 - 401(K) PROFIT SHARING PLAN

At the time of the merger with RiceX, we adopted RiceX's 401(k) profit sharing plan (the "Plan") for the exclusive benefit of eligible employees and their beneficiaries. Substantially all employees are eligible to participate in the Plan. Safe harbor contributions to the Plan are a mandatory 3% of the qualified employees' gross salary, whether or not the employee is a participant in the Plan. Also, in addition to any safe harbor contributions, the Company may contribute to the Plan matching contributions, discretionary profit sharing contributions and Qualified Non-Elective Contributions. For 2006, 2005 and 2004, we made matching contributions of $69,000, $41,000 and $16,000 respectively.

NOTE 15 - SUBSEQUENT EVENTS

Preferred Stock Conversion

In January of 2007, three Series B shareholders converted 250 shares of preferred stock into 500,000 shares of common stock at a rate of 1 preferred share to 2,000 common shares.

In January of 2007, fourteen Series C shareholders converted 1,266 shares of preferred stock into 1,488,816 shares of common stock at a rate of 1 preferred share to 1,176 common shares.

In February of 2007, one Series B shareholder converted 220 shares of preferred stock into 440,000 shares of common stock at a rate of one preferred share to 2,000 common shares.

In February of 2007, three Series C shareholders converted 4,200 shares of preferred stock into 4,941,175 shares of common stock at a rate of one preferred share to 1,176 common shares.

At March 2, 2007, the number of Series B preferred Stock outstanding was zero and the number of Series C Preferred outstanding was two.

Note Receivable

On February 6, 2007, we signed with the direct response marketing company, the Eighth Amendment to the Private Supply and Strategic Alliance Agreement, dated August 24, 2005. The parties agreed to consolidate the terms of payment under this agreement and a Promissory Note into a single Restated Promissory Note in the amount of $3,966,000, at an annual rate of 7% payable over a period of approximately one year. The note is current with payments as scheduled.

Private Placement

On February 16, 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. 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. The warrants have a term of five years and are immediately exercisable.

Rodman & Renshaw, LLC acted as advisor and placement agent for the financing and received a 6% cash-fee based on aggregate gross proceeds received from the investors, and reasonable expenses. They also received warrants to purchase 6% of the aggregate number of shares placed in the Offering, at an exercise price per share of $3.25. The warrants have a five-year term and are immediately exercisable.

Warrants Exercised

In January of 2007, we issued 75,000 warrants to purchase common stock to one individual at an exercise price of $2.38, expiring in 3 years, vesting after March 31, 2007, and valued at $130,000. Also, five warrant holders exercised 477,547 common shares for cash in the amount of $374,000.

Also in February, 2007, 25 warrant holders exercised 2,544,412 common shares for cash in the amount of $2,975,000.

NOTE 16 - QUARTERLY FINANCIAL DATA (UNAUDITED)

NUTRACEA AND SUBSIDIARIES
Notes to Consolidated Financial Statements

	2006			
	First Quarter	**Second Quarter**	**Third Quarter**	**Fourth Quarter**
Revenues	$ 3,782,000	$ 4,166,000	$ 4,946,000	$ 5,196,000
Operating income (loss)	(254,000)	290,000	460,000	552,000
Net income (loss)	(233,000)	399,000	641,000	778,000
Basic net income (loss) per common share	0.00	0.01	0.01	0.01
Diluted net income (loss) per common share	0.00	0.01	0.01	0.01

	2005			
	First Quarter	**Second Quarter**	**Third Quarter**	**Fourth Quarter**
Revenues	$ 459,000	$ 299,000	$ 302,000	$ 4,504,000
Operating income (loss)	(643,000)	(1,658,000)	(801,000)	108,000
Net Income (loss)	(865,000)	(1,810,000)	(1,036,000)	(161,000)
Basic net income (loss) per common share	(0.02)	(0.05)	(0.03)	0.00
Diluted net income (loss) per common share	(0.02)	(0.05)	(0.03)	0.00

The quarterly presentation is made because of the 2005 fourth quarter significant event, merger with The RiceX Company. Quarter information for 2005 represent four quarterly performance for NutraCea and one quarter performance for The RiceX Company.

NOTE 17 - GEOGRAPHIC OPERATIONS

For purposes of geographic reporting, revenues are attributed to the geographic location of the sales organization. The following table presents net revenues and long-lived assets by geographic area:

Fiscal Year Ended December 31,	2006	2005	2004
Net revenue from customers:			
United States	$ 17,748,000	$ 5,545,000	$ 1,010,000
International	342,000	-	-
Total reveunes	$ 18,090,000	$ 5,545,000	$ 1,010,000
Property, plant and equipment, net:			
United States	$ 8,961,000	$ 5,493,000	$ 120,000
Other countries	-	-	-
Total property, plant and equipment	$ 8,961,000	$ 5,493,000	$ 120,000

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