

Edgar Filing: NUTRACEA - Form 10QSB

NUTRACEA
Form 10QSB
November 15, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549

FORM 10-QSB

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2004

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE
EXCHANGE ACT FOR THE TRANSITION PERIOD FROM
_____ to _____

Commission File Number 0-32565

NUTRACEA

(Exact name of small business issuer as specified in its charter)

CALIFORNIA

87-0673375

(State of other jurisdiction of
incorporation or organization)

(I.R.S. Employer Identification
Number)

1261 Hawk's Flight Court
El Dorado Hills, California

95762

(Address of Principal Executive Offices)

(Zip Code)

Issuer's telephone number:

(916) 933-7000

Indicate by check mark whether the issuer (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 issuer was required
to file such reports), and (2) has been subject to such filing requirements for
the past 90 days: Yes X No
 --- ---

The number of shares of the issuer's common stock outstanding as of November 12,
2004 was 34,332,887.

Transitional Small Business Disclosure Format (Check One): Yes No X
 --- ---

INDEX

Page

Edgar Filing: NUTRACEA - Form 10QSB

PART I - FINANCIAL INFORMATION.	2
ITEM 1. FINANCIAL STATEMENTS.	2
ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS.	14
ITEM 3. CONTROLS AND PROCEDURES.	17
PART II - OTHER INFORMATION	19
ITEM 2. CHANGES IN SECURITIES AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES.	19
ITEM 5. OTHER INFORMATION	20
ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.	20

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NUTRACEA INDEX TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Consolidated Balance Sheet as of September 30, 2004 (Unaudited)	3
Consolidated Statements of Operations for the nine and three months ended September 30, 2004 and 2003 (Unaudited)	4
Consolidated Statements of Comprehensive Loss for the nine and three months ended September 30, 2004 and 2003 (unaudited)	5
Consolidated Statements of Cash Flows for the nine months ended September 30, 2004 and 2003 (Unaudited)	6
Notes to Unaudited Consolidated Financial Statements	7

2

NUTRACEA AND SUBSIDIARIES Consolidated Balance Sheet September 30, 2004 (Unaudited)

ASSETS

CURRENT ASSETS

Cash	\$ 377,035
Accounts receivable-trade	113,808
Marketable Securities	356,167
Inventory, net	183,632
Prepaid expenses	37,991

Edgar Filing: NUTRACEA - Form 10QSB

Total current assets	1,068,633
RESTRICTED MARKETABLE SECURITIES	356,167
EQUIPMENT, net	44,526
PATENTS AND TRADEMARKS, net	331,905
GOODWILL	250,001

TOTAL ASSETS	\$ 2,051,232
	=====
LIABILITIES AND SHAREHOLDERS' EQUITY	
Accounts payable	\$ 224,699
Accrued expenses	47,390
Due to related parties	8,810
Customer deposits	106,486
Convertible, mandatorily redeemable series A preferred stock, no par value, \$1 stated value, 20,000,000 shares authorized, 130,000 shares issued and outstanding	150,473

Total current liabilities	537,858

COMMITMENTS AND CONTINGENCIES	
SHAREHOLDERS' EQUITY	
Common stock, no par value, 100,000,000 shares authorized, 34,332,887 shares issued and outstanding	45,851,881
Deferred compensation	(19,943)
Accumulated deficit	(42,650,898)
Accumulated other comprehensive income, unrealized loss on marketable securities	(1,667,666)

Total shareholders' equity	1,513,374

TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 2,051,232
	=====

3

NUTRACEA
AND SUBSIDIARIES
Consolidated Statements of Operations
(unaudited)

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2004	2003	2004	2003
	-----	-----	-----	-----
		(Restated)		(Restated)
REVENUES				
Net sales	\$ 662,910	\$ 1,206,652	\$ 249,840	\$ 631,220
COST OF GOODS SOLD	396,494	634,973	165,069	311,853
	-----	-----	-----	-----
GROSS PROFIT	266,416	571,679	84,771	319,367
OPERATING EXPENSES	21,567,575	2,434,722	1,169,691	1,136,365

Edgar Filing: NUTRACEA - Form 10QSB

LOSS FROM OPERATIONS	(21,301,159)	(1,863,043)	(1,084,920)	(816,998)
OTHER INCOME (EXPENSE)				
Interest income	4,084	-	1,027	-
Interest expense	(495)	(65,874)	-	(25,997)
Total other income (expense)	3,589	(65,874)	1,027	(25,997)
NET LOSS	(21,297,570)	(1,928,917)	(1,083,893)	(842,995)
CUMULATIVE PREFERRED DIVIDEND	(8,373)	(108,489)	-	(33,425)
NET LOSS AVAILABLE TO COMMON SHAREHOLDERS	\$ (21,305,943)	\$ (2,037,406)	\$ (1,083,893)	\$ (876,420)
BASIC AND DILUTED LOSS AVAILABLE TO COMMON SHAREHOLDERS PER SHARE	\$ (1.12)	\$ (0.78)	\$ (0.04)	\$ (0.31)
BASIC AND DILUTED WEIGHTED- AVERAGE SHARES OUTSTANDING	18,946,026	2,621,932	26,537,529	2,820,568

4

NUTRACEA
AND SUBSIDIARIES
Consolidated Statements of Comprehensive Loss
(unaudited)

	Nine Months Ended September 30,		Three Months Ended September 30,	
	2004	2003	2004	2003
		(Restated)		(Restated)
NET LOSS AVAILABLE TO COMMON SHAREHOLDERS	\$ (21,305,943)	\$ (2,037,406)	\$ (1,083,893)	\$ (876,420)
OTHER COMPREHENSIVE LOSS				
Unrealized loss on marketable securities	(1,667,666)	-	(1,667,666)	-
NET AND COMPREHENSIVE LOSS	\$ (22,973,609)	\$ (2,037,406)	\$ (2,751,559)	\$ (876,420)

NUTRACEA
AND SUBSIDIARIES
Consolidated Statements of Cash Flow
(unaudited)

	Nine months ended September 30,	
	2004	2003
		(Restated)
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	\$ (21,297,570)	\$ (1,928,917)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation and amortization	24,167	94,085
Amortization of deferred compensation	53,659	104,437
Non-cash issuances of stock options and warrants	7,782,515	218,105
Non-cash issuances of stock as compensation	11,627,484	795,790
(Increase) decrease in		
Accounts receivable	(83,355)	2,861
Inventory	(112,738)	747
Prepaid expenses	(23,134)	23,121
Accounts payable	(21,711)	(28,781)
Accrued salaries and benefits	(37,130)	(14,493)
Deferred compensation	(47,842)	63,870
Accrued expenses	10,025	243,153
Customer deposits	5,000	7,170
Due to related parties	(9,578)	(26,457)
Net cash used in operating activities	(2,130,208)	(445,309)
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of property and equipment	(35,110)	(13,580)
Purchase of patents and trademarks	(51,534)	(13,734)
Net cash used in investing activities	(86,644)	(27,314)
CASH FLOWS FROM FINANCING ACTIVITIES		
Principal payments on notes payable	-	(55,000)
Proceeds from notes payable	-	414,000
Proceeds from notes payable - related parties	-	320,422
Payments on notes payable - related parties	-	(210,000)
Proceeds from issuance of common stock	-	104,500
Proceeds from exercise of stock options	2,771,868	3,034
Common stock repurchase	(230,000)	-
Payment of preferred dividends	(48,004)	-
Net cash provided by financing activities	2,493,864	576,956
Net increase in cash	277,012	104,333
CASH, BEGINNING OF PERIOD	100,023	34,718
CASH, END OF PERIOD	\$ 377,035	\$ 139,051

SUPPLEMENTAL AND NON-CASH DISCLOSURES OF CASH FLOW INFORMATION

Edgar Filing: NUTRACEA - Form 10QSB

Interest paid \$ - \$ 4,378

6

NUTRACEA AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1-BASIS OF PRESENTATION:

The accompanying unaudited interim consolidated financial statements of NutraCea have been prepared in accordance with accounting principles generally accepted in the United States of America and the rules of the Securities and Exchange Commission ("SEC"), and should be read in conjunction with the audited financial statements and notes thereto contained in NutraCea's Annual Report filed with the SEC on Form 10-KSB. In the opinion of management, all adjustments, consisting of normal recurring adjustments, necessary for a fair presentation of financial position and the results of operations for the interim periods presented have been reflected herein. The results of operations for interim periods are not necessarily indicative of the results to be expected for the full year. Notes to the financial statements that would substantially duplicate the disclosure contained in the audited financial statements for 2003 as reported in the 10-KSB have been omitted.

NOTE 2-RESTATEMENT:

NutraCea has restated its Consolidated Financial Statements for the third quarter of 2003 to correct an error in valuation of stock-based compensation. This restatement increased operating expenses and the net loss attributable to common shareholders by \$853,395 and \$479,495, respectively, for the nine months and three months ended September 30, 2003. The following table presents the effects of the correction and restatement on a condensed basis.

	Nine months ended September 30, 2003			As previously reported	Three Months ended Septe mber 30, 2003
	As previously reported	Restatement adjustments	As restated		
Operating expenses	\$ 1,581,327	853,395	\$ 2,434,722	\$ 656,870	
Net loss available to common shareholders	\$ (1,184,011)	(853,395)	\$(2,037,406)	\$ (396,925)	
Basic and diluted loss available to common shareholders per share	\$ (0.45)	(0.33)	\$ (0.78)	\$ (0.14)	

NOTE 3-STOCK-BASED COMPENSATION:

Compensation is recorded for stock-based compensation grants based on the excess of the estimated fair value of the common stock on the measurement date over the exercise price. Additionally, for stock-based compensation grants to consultants, NutraCea recognizes as compensation expense the fair value of such grants as calculated pursuant to SFAS No. 123, recognized over the related service period. SFAS No. 148 requires companies to disclose proforma results of the estimated effect on net income and earnings per share to reflect application

Edgar Filing: NUTRACEA - Form 10QSB

of the fair value recognition provision of SFAS No. 123.

7

	For the nine months ended September 30, 2004		For the three months ended September 30, 2004	
	2003	2003	2003	2003
	(Restated)		(Restated)	
Net loss available to common shareholders:				
As reported:	\$ (21,305,943)	\$ (2,037,406)	\$ (1,083,893)	\$ (876,420)
Add: compensation expense charged to income:	7,782,515	1,133,109	21,000	722,350
Less: proforma compensation expense:	(7,784,542)	(1,138,841)	(23,027)	(724,192)
	\$ (21,307,970)	\$ (2,043,138)	\$ (1,085,920)	\$ (878,262)
Proforma net loss available to common shareholders:	\$ (21,307,970)	\$ (2,043,138)	\$ (1,085,920)	\$ (878,262)
Basic loss per common share:				
As reported:	\$ (1.12)	\$ (0.78)	\$ (0.04)	\$ (0.31)
Proforma:	\$ (1.12)	\$ (0.78)	\$ (0.04)	\$ (0.31)

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 that is actively traded on a London exchange. Per the Stock Purchase Agreement, NutraCea paid with 7,000,000 shares of its own common stock.

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 together 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 September 30, 2004, the NutraCea shares have not lost any value. However, the Langley shares are marked down to their fair market value of \$712,334, with one-half or \$356,167 shown as a current asset because they may be sold at any time, and the other one-half shown as long-term because they are held in escrow pending the 2-year review of NutraCea's stock valuation.

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.

NOTE 5 - COMMITMENTS AND CONTINGENCIES

Agreements

For all agreements where stock is awarded as partial or full consideration, the expense is valued at the fair value of the stock. Expense for stock options and warrants issued to consultants is calculated at fair value using the

Edgar Filing: NUTRACEA - Form 10QSB

Black-Scholes valuation method.

Effective January 1, 2004, NutraCea amended two executive employment contracts to reflect quarterly bonuses. Under the contract, compensation shall be \$45,000 per calendar quarter, with 250,000 shares of common stock to be granted in the event NutraCea achieves gross revenues of \$1 million or more for the quarter. In addition, a one-time stock grant of 550,000 shares of common stock will be awarded for the first quarter gross revenues equal or exceed \$5 million. This bonus agreement is effective until April 15, 2006, unless extended by the board. NutraCea also agreed to maintain an annual bonus program for members of the senior management group, including the Chief Executive Officer. The Chief Executive Officer shall be eligible to receive an annual bonus under terms otherwise governing the annual bonus program.

Effective January 1, 2004, NutraCea amended the stock options section of an executive employment contract dated April 15, 2003. The amendment changed the vesting conditions on 250,000 shares of common stock to "upon the completion of the twelfth month of employment " instead of "upon the Company achieving two successful calendar quarters of net profits from operations of the business of the Company before interest, taxes, depreciation and amortization as conclusively determined by the independent certified public accountant for the Company".

On January 12, 2004, NutraCea entered into a one-year consulting agreement with a sales and marketing company. Under the terms of the agreement, compensation shall be warrants to purchase 4,000,000 shares of common stock as follows: 300,000 shares at \$.50 per share on or before January 12, 2004; 400,000 shares at \$.50 per share on or before February 17, 2004; and 3,300,000 shares at \$.50 per share on or before April 19, 2004. Non-cash compensation expense of \$3,911,886 was recorded relating to this agreement. All of the warrants had been exercised at March 31, 2004.

On January 28, 2004, NutraCea entered into a one-year consulting agreement with a sales and marketing company. Under the terms of the agreement, compensation shall be warrants to

8

purchase 90,000 shares of common stock at an exercise price of \$.01 per share. Non-cash compensation expense of \$137,158 was recorded relating to this agreement. As of March 31, 2004, these warrants had been exercised.

On February 2, 2004, NutraCea entered into a six -month consulting agreement with a communications company. Under the terms of the agreement, compensation shall be \$2,500 per month, plus shares of common stock valued at \$6,000 issued at signing of contract. Either party may terminate the agreement with sixty days written notice. At March 31, 2004, the shares had been issued in full.

On February 23, 2004, NutraCea entered into a one-year consulting agreement with a marketing company. Under the terms of the agreement, compensation shall be monthly issuance of shares of common stock valued at \$7,500 per month. In addition, the consultant is entitled to a 3% commission on equity or debt financing introduced to NutraCea.

On March 1, 2004, NutraCea entered into a 90-day consulting agreement with a financial relations company. Compensation shall be the issuance of 100,000 shares of common stock per month. As of March 31, 2004, 100,000 shares valued at \$142,000 had been issued to the consultant.

On March 1, 2004, NutraCea entered into a one-year consulting agreement with a sales and marketing company. Compensation shall be the issuance of 25,000

Edgar Filing: NUTRACEA - Form 10QSB

shares of common stock. At March 31, 2004, these shares had been issued. Non-cash compensation expense of \$35,500 was recorded relating to this agreement.

On March 9, 2004, NutraCea entered into a one-year consulting agreement with a communications company. Under the terms of the agreement, compensation shall be issuance of shares of common stock valued at \$36,000. At March 31, 2004, these shares have been issued in full.

On March 15, 2004, NutraCea entered into a six-month consulting agreement with a sales and marketing company. Under the terms of the agreement, compensation shall be warrants to purchase 400,000 shares of common stock, at an exercise price of \$.001 and warrants to purchase up to 1,000,000 shares of common stock at an exercise price of \$1.20, to be exercised within three years. At March 31, 2004, the 400,000 warrants exercisable at \$.001 had been exercised. Non-cash compensation expense of \$2,149,598 was recorded relating to this agreement.

On March 19, 2004, NutraCea approved granting a one-time cash bonus of 2/3 of normal salary to the CEO and President. The bonus amount for both executives is \$180,000, payable April 1, 2004.

On March 25, 2004, NutraCea entered into two, two-year consulting agreements with two medical advisors. Under the terms of the agreement, compensation shall be 100,000 shares of common stock each, payable in advance, and options to purchase 100,000 shares of common stock at a price of \$.50 per share for the second year of service. The 200,000 shares of common stock are valued at \$286,000, and the options are valued at \$107,684. Expense for these amounts was recorded in April 2004 when the shares and options were issued.

On March 25, 2004, NutraCea entered into a three-year consulting agreement with a development and marketing company. Under the terms of the agreement, compensation shall be \$1 per unit (a minimum 30-day supply of NutraCea product) for up to a total accumulated payment of \$750,000, and \$.50 per unit thereafter, payable quarterly within 45 days after the end of the quarter. In addition, NutraCea will issue 100,000 shares of common stock for each probiotic formulation NutraCea markets, and options to purchase 300,000 shares of common stock at an

9

exercise price of \$1 per share with 100,000 options to be vested immediately and 50,000 shares per year thereafter. The vested options are valued at \$102,782.

On April 2, 2004, NutraCea entered into a 180-day consulting agreement with a marketing and investor relations company. The term can be extended another 180 days by mutual agreement. Under the terms of the agreement, compensation shall be 400,000 shares of common stock, and \$4,000 cash per month. Compensation shall also include an 8% cash commission on equity or debt financing introduced to NutraCea, as well as a warrant, exercisable within 3 years, for common shares to equal 10% of the gross financing proceeds. The warrant is to be priced at 110% of the closing bid price for the preceding 30 business days of the day of closing, such warrant or shares to be issued at closing.

On April 29, 2004, NutraCea entered into a one-year consulting agreement (with options to extend for four successive terms of one year each) with two retired employees of NutraCea. Under the terms of the agreements, annual compensation of \$70,000 and \$80,000 each is payable on a monthly basis. In addition, each of the consultants received warrants to purchase 50,000 shares of common stock at \$.20 a share. The 100,000 warrants are valued at \$91,370 and expire in 5 years. Either party can cancel this agreement with 30-day written notice.

Edgar Filing: NUTRACEA - Form 10QSB

On April 15, 2004, NutraCea entered into a one-year consulting agreement with a sales and marketing consultant. Under the terms of the agreement, compensation shall be warrants to purchase 50,000 shares of common stock at \$.80 per share upon the completion of certain benchmarks. The warrants are valued at \$46,758 and expire in 3 years.

On June 2, 2004, NutraCea entered into two consulting agreements with sales and marketing consultants. Under the terms of the agreements, each consultant shall be issued 150,000 restricted shares of common stock, valued at \$161,500. The agreement calls for these shares to be included in the next registration statement filed.

On July 14, 2004, NutraCea entered into a six-month consulting agreement with a business consultant to provide NutraCea with consulting services and advice pertaining to NutraCea's business affairs. Compensation shall be \$12,000 payable in cash monthly. In addition, should the consultant provide assistance to NutraCea in the raising of capital either in the form of equity or debt, NutraCea agrees to pay an additional future bonus or fee, which the consultant will receive based on the efforts expended and results obtained.

On August 1, 2004, NutraCea entered in a 90-day Independent Contractor Agreement with a contractor to prepare reports regarding investor relations, prepare advertising and marketing materials, and prepare press releases. Compensation shall be \$12,000 payable in cash monthly.

On September 2, 2004, NutraCea entered into a 90-day consulting agreement with a securities firm to serve as NutraCea's investment advisor regarding acquisitions or similar corporate transactions and to provide assistance and advice with respect to raising capital required to consummate an acquisition or similar corporate transaction. A non-reimbursable initial fee of \$50,000, to be credited again Phase I fees, was paid at execution of the agreement. Services shall be rendered as Phase I and Phase II services and shall be compensated as follows.

Phase I services: A fee of two percent of the total value of a target acquisition to be paid simultaneously with the closing of the acquisition or similar corporate transaction, to be paid 50% in cash and 50% in newly issued stock by NutraCea based on the closing values of the transaction on that day.

10

Phase II services: A cash fee of ten percent of the total amount of capital raised pursuant to sources introduced to NutraCea by the consultant. In the event NutraCea shall issue any equity or convertible securities to raise capital in connection with an acquisition or similar corporate transaction, NutraCea shall issue warrants for ten percent of the total amount of securities issued. The warrants shall have an exercise price equal to one hundred and twenty percent (120%) of the per share equity valuation established in the capital raising transaction, but in no case less than 100% of the market value of the shares on the date of the transaction, and shall be exercisable for a term of five years. A cash fee of six percent will be paid in any capital raising transaction involving unsecured debt securities.

NOTE 6 - COMMON STOCK

Common and Preferred Stock

All stock issued is valued at the fair value of the stock.

Edgar Filing: NUTRACEA - Form 10QSB

On March 25, 2004, NutraCea 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.

During the quarter ended March 31, 2004, NutraCea issued 544,965 shares of common stock to consultants for services rendered valued at \$723,381.

During the quarter ended March 31, 2004, NutraCea issued 168,095 shares of common stock to vendors in payment of accounts payable totaling \$57,111.

During the quarter ended March 31, 2004, NutraCea issued 6,490,711 shares of common stock pursuant to the exercise of stock options and warrants for cash totaling \$2,744,507.

During the quarter ended March 31, 2004, NutraCea issued 280,000 shares of common stock to two consultants in settlement of contractual agreements valued at \$477,816.

During the quarter ended March 31, 2004, NutraCea issued 5,500,000 shares of common stock, valued at \$8,360,000, to NutraCea's Chief Executive Officer for current services rendered. 175,000 of these shares replace shares owned by NutraCea's CEO and used to satisfy NutraCea obligations and the balance of the shares will be held in escrow to satisfy a deferred compensation arrangement between NutraCea and the CEO.

On April 1, 2004, NutraCea repurchased 344,956 shares of common stock valued at \$230,000 from the Chief Executive Officer of NutraCea pursuant to a repurchase agreement of that date.

During the quarter ended June 30, 2004, NutraCea issued 1,083,489 shares of common stock to consultants for services rendered valued at \$1,380,287.

During the quarter ended June 30, 2004, NutraCea issued 531 shares of common stock to a vendor in payment of accounts payable in the amount of \$833.

During the quarter ended June 30, 2004, NutraCea issued 438,612 shares of common stock pursuant to the exercise of stock options and warrants for cash totaling \$22,861.

During the quarter ended June 30, 2004, NutraCea converted 510,000 shares of preferred stock to 510,000 shares of common stock pursuant to the Mandatory Conversion paragraph of the Private Placement Memorandum dated November 9, 2001.

During the quarter ended June 30, 2004, NutraCea converted preferred dividends in the amount of \$5,986 into 5,759 shares of common stock.

11

During the quarter ended September 30, 2004, NutraCea issued 486,839 shares of common stock to consultants for services rendered valued at \$496,100.

During the quarter ended September 30, 2004, NutraCea issued 300,000 shares of restricted common stock valued at \$429,000 to officers and directors for services rendered.

During the quarter ended September 30, 2004, NutraCea issued 25,000 shares of common stock pursuant to the exercise of stock options and warrants for cash totaling \$4,500.

During the quarter ended September 30, 2004, NutraCea converted 300,000 shares of preferred stock to 120,000 shares of common stock pursuant to the Mandatory

Edgar Filing: NUTRACEA - Form 10QSB

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 the Company (i) immediately following the closing of approximately \$1,190,000 U.S.D., 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.

Stock Options & Warrants

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

During the quarter ended March 31, 2004, NutraCea issued 6,547,263 warrants with exercise prices between \$.001 and \$5.00 per share to consultants. The warrants expire at varying times between six months and five years. A total of \$7,271,060 in non-cash compensation expense was recorded relating to the issue of these warrants.

During the quarter ended June 30, 2004 NutraCea issued 451,230 warrants with exercise prices between \$.001 and \$5.00 to consultants. The warrants expire at varying times between three and five years. A total of \$490,455 in non-cash compensation expense was recorded relating to the issue of these warrants.

On July 9, 2004, NutraCea issued 25,000 stock options with an exercise price of \$.20, expiring in five years, to an employee of the Company. Non-cash compensation expense of \$21,000 was recorded relating to the issue of these options.

12

NOTE 7 - BUSINESS SEGMENTS

For internal reporting purposes, management segregates NutraCea into operating segments as follows for the nine and three months ended September 30, 2004 and 2003:

NINE MONTHS ENDED SEPTEMBER 30, 2004	NET SALES	(LOSS) FROM OPERATIONS	INTEREST EXPENSE	TOTAL ASSETS	DEPRECIAT AMORTIZA
-----	-----	-----	-----	-----	-----
NutraStar Technologies Incorporated	\$ 306,113	\$ (9,505,506)	\$ 495	\$1,914,563	\$ 2
NutraGlo Incorporated	356,797	109,200	-	136,669	
Unallocated corporate overhead	-	(11,904,853)	-	-	
-----	-----	-----	-----	-----	-----

Edgar Filing: NUTRACEA - Form 10QSB

Total, NutraCea	\$ 662,910	\$ (21,301,159)	\$ 495	\$2,051,232	\$ 2
=====					
NINE MONTHS ENDED SEPTEMBER 30, 2003 (RESTATED)	NET SALES	(LOSS) FROM OPERATIONS	INTEREST EXPENSE	TOTAL ASSETS	DEPRECIAT AMORTIZAT

NutraStar Technologies Incorporated	\$ 98,619	\$ (1,265,163)	\$ 49,358	\$ 492,208	\$ 9
NutraGlo Incorporated	1,108,033	462,178	16,516	26,286	
Unallocated corporate overhead	-	(1,060,058)	-	-	

Total, NutraCea	\$1,206,652	\$ (1,863,043)	\$ 65,874	\$ 518,494	\$ 9
=====					
THREE MONTHS ENDED SEPTEMBER 30, 2004	NET SALES	(LOSS) FROM OPERATIONS	INTEREST EXPENSE	TOTAL ASSETS	DEPRECIAT AMORTIZAT

NutraStar Technologies Incorporated	\$ 88,916	\$ 304,277	\$ -	\$1,914,563	\$ 1
NutraGlo Incorporated	160,924	49,091	-	136,669	
Unallocated corporate overhead	-	(1,438,288)	-	-	

Total, NutraCea	\$ 249,840	\$ (1,084,920)	\$ -	\$2,051,232	\$ 1
=====					
THREE MONTHS ENDED SEPTEMBER 30, 2003 (RESTATED)	NET SALES	(LOSS) FROM OPERATIONS	INTEREST EXPENSE	TOTAL ASSETS	DEPRECIAT AMORTIZAT

NutraStar Technologies Incorporated	\$ 37,403	\$ (595,027)	\$ 17,076	\$ 492,208	\$ 2
NutraGlo Incorporated	593,817	278,450	8,921	26,286	
Unallocated corporate overhead	-	(500,421)	-	-	

Total, NutraCea	\$ 631,220	\$ (816,998)	\$ 25,997	\$ 518,494	\$ 2
=====					

13

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OR PLAN OF OPERATIONS

CAUTION ABOUT FORWARD-LOOKING STATEMENTS

This Form 10-QSB includes "forward-looking" statements about future financial results, future business changes and other events that have not yet occurred. For example, statements like NutraCea "expects," "anticipates" or "believes" are forward-looking statements. Investors should be aware that actual results may differ materially from NutraCea's expressed expectations because of risks and uncertainties about the future. NutraCea does not undertake to update the information in this Form 10-QSB if any forward-looking statement later turns out to be inaccurate. Details about risks affecting various aspects of NutraCea's business are discussed throughout this Form 10-QSB and should be considered carefully.

RESULTS OF OPERATIONS

Operating Results for the Quarters Ended September 30, 2004 and 2003

The Company had revenues of \$249,840 for the quarter ended September 30, 2004 compared to revenues of \$631,220 for the quarter ended September 30, 2003. The decrease in the third quarter was due primarily to a continued decrease in purchases by a major customer of the Company's subsidiary, NutraGlo

Edgar Filing: NUTRACEA - Form 10QSB

Incorporated.

Cost of goods sold for the third quarter of 2004 was \$165,069 compared to \$311,853 for the same period of 2003. The decrease in cost of goods sold relates directly to the decrease in sales during the third quarter.

Operating expenses were \$1,169,691 for the quarter ended September 30, 2004 compared to \$1,136,365 for the quarter ended September 30, 2003. During the quarter ended September 30, 2004, non-cash stock and option awards decreased by \$185,745 to \$489,500 from \$675,245 for the quarter ended September 30, 2003. Other significant variances in operating expenses incurred during the three months ended September 30, 2004 as compared to the three months ended September 30, 2003 are as follows:

	Three months ended	
	9/30/2004	9/30/2003
	-----	-----
Commissions and finders fees	\$ -	\$ 38,115
Depreciation	10,225	29,987
Insurance	26,561	3,994
Professional fees	411,860	110,797
Promotional and marketing	19,450	350
Salaries and wages	91,286	185,362
Travel	9,721	7,366
Other	33,326	7,387
	-----	-----
	\$ 602,429	\$ 383,358
	-----	-----

14

The Company posted an operating loss of \$1,084,920 for the quarter ended September 30, 2004 compared to an operating loss of \$816,998 for the same quarter in 2003. The operating losses are due to the significant operating expenses consisting primarily of non-cash stock option and warrant awards made to certain officers and consultants of NutraCea.

Interest expense decreased to zero for the quarter ended September 30, 2004 compared to interest expense of \$25,997 for the same period in 2003. This decrease is due primarily to the elimination of interest expense on notes that were paid off or converted in 2003.

The net loss for the quarter ended September 30, 2004 was \$1,083,893 compared to a net loss of \$876,420 recorded for the quarter ended September 30, 2003. This 24% increase in net loss was due primarily to the increase in operating losses for the third quarter of 2004 offset somewhat by interest income of \$1,027.

During the quarter ended September 30, 2004 the Company entered into the following consulting agreements:

On July 14, 2004, NutraCea entered into a six-month consulting agreement with 21st Century Diversified Holdings Inc., a business consulting firm, to provide NutraCea with consulting services and advice pertaining to NutraCea's business affairs and assistance in the raising of capital either in the form of equity or debt.

On August 1, 2004, NutraCea entered in a 90-day Independent Contractor

Edgar Filing: NUTRACEA - Form 10QSB

Agreement with Margie Adelman to prepare reports regarding investor relations, prepare advertising and marketing materials, and prepare press releases.

On September 2, 2004, NutraCea entered into a 90-day consulting agreement with Sandgrain Securities Inc. to serve as NutraCea's investment advisor regarding acquisitions or similar corporate transactions and to provide assistance and advice with respect to raising capital required to consummate an acquisition or similar corporate transaction.

Operating Results for the Nine Months Ended September 30, 2004 and 2003

Revenues of NutraCea decreased by \$543,742 to \$662,910 for the nine months ended September 30, 2004 as compared to revenues of \$1,206,652 for the nine months ended September 30, 2003. The decrease in revenues is primarily attributable to decreased purchases by the major customer of the Company's subsidiary NutraGlo Incorporated.

Costs of goods sold decreased by \$238,479 to \$396,494 for the nine months ended September 30, 2004 from \$634,973 for the nine months ended September 30, 2003. The decrease in costs of goods sold generally reflects the decrease in revenues during the first nine months of 2004.

Operating expenses have increased to \$21,567,575 for the nine months ended September 30, 2004 compared to \$2,434,722 for the similar period of 2003. The substantial increase in 2004 was attributable primarily to non-cash stock and option awards which increased by \$18,396,104 to \$19,409,999 for the nine months ended September 30, 2004 compared to \$1,013,895 for the first nine months of 2003. During the first half of 2004, the Company has attempted to conserve its cash flow position by issuing options and stock for services whenever possible. Other variances in operating expense line items are as follows:

15

	Nine months ended	
	9/30/2004	9/30/2003
	-----	-----
Commissions and finders fees	\$ 209,438	\$ 38,115
Depreciation	24,167	94,085
Insurance	54,675	15,306
Professional fees	745,121	281,496
Promotional and marketing	95,479	750
Salaries and wages	539,694	513,623
Travel	74,975	9,593
Other	19,132,853	19,186,685
	-----	-----
	\$20,876,402	\$20,139,653
	-----	-----

The Company reported an operating loss of \$21,301,159 for the nine-month period ending September 30, 2004 compared to an operating loss of \$1,863,043 reported for the same period of 2003. The increase in operating loss for the first nine months of 2004 is due primarily to the substantial increase in non-cash stock and option related expenses.

Edgar Filing: NUTRACEA - Form 10QSB

Interest expense decreased by \$65,379 to \$495 for the nine months ended September 30, 2004 from \$65,874 for the nine months ended September 30, 2003. This decrease is due to the substantial reduction in the number of promissory notes outstanding.

The Company posted a net loss of \$21,297,570 for the nine-month period ended September 30, 2004 compared to \$1,928,917 for the first nine months of 2003. The substantially larger nine-month operating loss in 2004 was due primarily to the significant operating expenses incurred in the first half of 2004 relating to the issuance of the Company's common stock as compensation.

Off-Balance Sheet Arrangements

During the quarter ended September 30, 2004, the Company did not engage in any off-balance sheet arrangements as defined in Item 303 (c) of the SEC's Regulation S-B

LIQUIDITY AND SOURCES OF CAPITAL

NutraCea has incurred significant operating losses since its inception, and, as of September 30, 2004 NutraCea had an accumulated deficit of \$42,650,898. However, at September 30, 2004, NutraCea had cash and cash equivalents of \$377,035 and working capital of \$530,775.

To date, NutraCea has funded its operations, in addition to sales revenues, through a combination of short-term debt and the issuance of common and preferred stock. During the nine months ended September 30, 2004, NutraCea has issued a total of 22,559,405 shares of common stock of which approximately 8.4 million shares were issued as compensation to officers and consultants of the Company. During the nine months ended September 30, 2004, NutraCea raised a total of \$2,771,868 from the exercise of options and warrants to purchase 6,954,323 shares of common stock. NutraCea continues to

16

pursue cost cutting or expense deferral strategies in order to conserve working capital.

Based on management's financial projections, NutraCea has enough cash reserves to finance its business plan through fiscal year 2004.

Due to the Company's limited cash flow and operating losses, it is unlikely that the Company could obtain financing through commercial or banking sources. Consequently, the Company is dependent on continuous cash infusions from major investors and the exercise of outstanding warrants and options in order to fund its current operations. If these sources of capital were unwilling or unable to provide additional working capital to the Company, the Company would probably not be able to sustain its full range of operations. There is no written agreement or contractual obligation which would require the Company's past funding sources to fund the Company's future operations up to certain amounts or indeed continue to finance the Company's operations at all.

As of September 30, 2004, NutraCea's principal commitments include a lease commitment that expires in 2006 of \$ 5,358 per month for the Company's corporate offices.

Management of NutraCea believes that it will need to raise additional capital to continue to develop, promote and conduct its operations. Such additional capital may be raised through public or private financing as well as borrowing from other sources. Although the Company believes that current and/or future

Edgar Filing: NUTRACEA - Form 10QSB

investors will continue to fund the Company's expenses, there is no assurance that such investors will continue to fund the Company's ongoing operations or the terms upon which such investments will be made.

CRITICAL ACCOUNTING POLICIES

NutraCea's discussion and analysis of its financial condition and results of operations are based upon its consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of financial statements require managers to make estimates and judgments that affect the reported amounts of assets and liabilities, revenues and expenses and disclosures on the date of the financial statements. On an on-going basis, the Company's accountants' evaluate the estimates, including, but not limited to, those related to revenue recognition. The Company uses authoritative pronouncements, historical experience and other assumptions as the basis for making judgments. Actual results could differ from those estimates.

The Company has adopted the fair value based method of accounting prescribed in Financial Accounting Standards Board ("FASB") Statement No. 123, "Accounting for Stock-Based Compensation," for its employee stock option plans.

The Company has adopted SFAS No. 145, "Rescission of FASB Statements No. 4, 44 and 64, Amendment of FASB Statement No. 13 and Technical Corrections" which requires gains and losses from extinguishment of debt to be reported as part of recurring operations.

ITEM 3. CONTROLS AND PROCEDURES

The Company carried out an evaluation, under the supervision and with the participation of the Company's management, including the Company's President and Chief Executive

17

Officer along with the Company's Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-14 as of the end of the period covered by this report. Based upon that evaluation, the Company's President and Chief Executive Officer along with the Company's Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective to ensure the information required to be disclosed by the Company 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.

There have been no significant changes in the Company's internal controls over financing reporting or in other factors which occurred during the quarter covered by this report, which could materially affect or are unreasonably likely to materially affect the Company's internal controls over financing reporting.

18

PART II - OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES AND SMALL BUSINESS ISSUER PURCHASES OF EQUITY SECURITIES

SALES OF UNREGISTERED SECURITIES DURING THE QUARTER

Edgar Filing: NUTRACEA - Form 10QSB

During the quarter ended September 30, 2004, NutraCea issued 451,770 shares of restricted common stock to consultants for services rendered valued at \$473,600.

During the quarter ended September 30, 2004, NutraCea issued 300,000 shares of restricted common stock to officers and directors for services rendered valued at \$429,000.

During the third quarter, the Company issued options to an employee to purchase 25,000 shares of the Company's common stock. The options were valued at \$21,000.

During the quarter-ended September 30, 2004, NutraCea issued 25,000 shares of common stock pursuant to the exercise of stock options and warrants for cash totaling \$4,500.

All of the above issuances were made without any public solicitation, to a limited number of investors or related individuals or entities and were acquired for investment purposes only. Each of the individuals or entities had access to information about NutraCea and was deemed capable of protecting their own interests. The securities were issued pursuant to the private placement exemption provided by Section 4(2) of the Securities Act of 1933 ("1933 Act"). These are deemed to be "restricted securities" as defined in Rule 144 under the 1933 Act and bear a legend stating the restrictions on resale.

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 the Company (i) immediately following the closing of approximately \$1,190,000 U.S.D., 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.

Langley is a corporation formed outside the United States and is not deemed to be "U.S. persons" as that term is defined under Regulation S. The investor represented that it is purchasing such shares for its own account. Both the offer and the sale of the NutraCea shares were made outside the United States and are deemed to be "offshore transactions" as that term is defined under Regulation S. The share certificate contains a legend indicating that such shares can only be transferred in compliance with the provisions of Regulation S. In light of the foregoing, such sales were deemed exempt from registration pursuant to Regulation S of the Securities Act of 1933 (the "1933 Act"). The shares are deemed to be "restricted securities" as defined in Rule 144 under the 1933 Act and the certificate(s) evidencing the shares bear a legend stating the restrictions on resale.

ITEM 5. OTHER INFORMATION

On July 26, 2004, John Howell resigned as President and as a director of NutraCea. His duties as President were assumed by Patricia McPeak, NutraCea's CEO.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) The following documents are filed as exhibits to this report:

Edgar Filing: NUTRACEA - Form 10QSB

31.1 Certification by CEO pursuant to Section 302 of the Sarbanes - Oxley Act of 2002

19

31.2 Certification by CFO pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification by CEO and CFO pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K:

(i) Form 8-K filed on July 27, 2004 reporting under Item 9 the resignation of John Howell as President and as a director of NutraCea.

(ii) Form 8-K filed on September 14, 2004 reporting under Item 3.02 the sale of unregistered equity securities to Langley Park Investments PLC.

20

SIGNATURES

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

NUTRACEA

Dated: November 15, 2004

/s/ Patricia McPeak

Patricia McPeak
Chief Executive Officer

Dated: November 15, 2004

/s/ Joanna Hoover

Joanna Hoover,
Chief Financial Officer
(Principal Accounting Officer)

21