Pacific Ethanol, Inc.
Form 10-Q
August 11, 2011

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

FORM 10-Q

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2011

[_] 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: 000-21467

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	41-2170618 (I.R.S. Employer Identification No.)
400 Capitol Mall, Suite 2060, Sacramento, California (Address of principal executive offices)	95814 (zip code)

(916) 403-2123
(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 has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter periods that the registrant was required to submit and post such files). Yes |X| No | |

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

Large accelerated filer [_]	Accelerated filer [_]
Non-accelerated filer [_] (Do not check if a smaller reporting company)	Smaller reporting company [X]

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

As of August 9, 2011, there were 25,743,378 shares of Pacific Ethanol, Inc. common stock, $0.001 par value per share, outstanding.

PART I
FINANCIAL INFORMATION

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

PACIFIC ETHANOL, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands)

ASSETS	June 30, 2011 (unaudited)	December 31, 2010 *
Current Assets:		
Cash and cash equivalents	$ 9,832	$ 8,736
Accounts receivable, net (net of allowance for doubtful accounts of $108 and $287, respectively)	34,281	25,855
Inventories	20,851	17,306
Prepaid inventory	6,141	2,715
Other current assets	2,057	2,712
Total current assets	73,162	57,324
Property and equipment, net	164,483	168,976
Other Assets:		
Intangible assets, net	4,920	5,382
Other assets	2,135	2,401
Total other assets	7,055	7,783
Total Assets**	$ 244,700	$ 234,083

* Amounts derived from the audited financial statements for the year ended December 31, 2010.

** Assets of the consolidated variable interest entity that can only be used to settle obligations of that entity were $175,528 and $183,652 as of June 30, 2011 and December 31, 2010, respectively.

See accompanying notes to consolidated financial statements.

PACIFIC ETHANOL, INC.
CONSOLIDATED BALANCE SHEETS (CONTINUED)
(in thousands, except par value and shares)

LIABILITIES AND STOCKHOLDERS' EQUITY	June 30, 2011 (unaudited)	December 31, 2010 *
Current Liabilities:		
Accounts payable – trade	$9,853	$6,472
Accrued liabilities	2,783	3,251
Current portion – long-term debt (including $1,250 and $0, due to related parties, and $25,134 and $38,108 at fair value, respectively)	26,384	38,108
Total current liabilities	39,020	47,831
Long-term debt, net of current portion (including $0 and $1,250, due to related parties, respectively)	100,190	84,981
Accrued preferred dividends	6,677	6,050
Other liabilities	2,723	7,406
Total Liabilities**	148,610	146,268
Commitments and Contingencies (Notes 4, 5 and 7)		
Stockholders' Equity:		
Pacific Ethanol, Inc. Stockholders' Equity (Deficit):		
Preferred stock, $0.001 par value; 10,000,000 shares authorized; Series A: 1,684,375 shares authorized; 0 shares issued and outstanding as of June 30, 2011 and December 31, 2010;	-	-
Series B: 1,580,790 and 2,109,772 shares authorized; 926,942 and 1,455,924 shares issued and outstanding as of June 30, 2011 and December 31, 2010, respectively; liquidation preference of $24,752 as of June 30, 2011	1	1
Common stock, $0.001 par value; 300,000,000 shares authorized; 19,510,999 and 12,918,144 shares issued and outstanding as of June 30, 2011 and December 31, 2010, respectively	20	13
Additional paid-in capital	522,872	504,623
Accumulated deficit	(511,653)	(511,794)
Total Pacific Ethanol, Inc. Stockholders' Equity (Deficit)	11,240	(7,157)
Noncontrolling interest in variable interest entity	84,850	94,972
Total Stockholders' Equity	96,090	87,815
Total Liabilities and Stockholders' Equity	$244,700	$234,083

* Amounts derived from the audited financial statements for the year ended December 31, 2010.
** Liabilities of the consolidated variable interest entity for which creditors do not have recourse to the general credit of Pacific Ethanol, Inc. were $85,610 and $74,939 as of June 30, 2011 and December 31, 2010, respectively.

See accompanying notes to consolidated financial statements.

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PACIFIC ETHANOL, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS
(unaudited, in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Net sales	$214,593	$76,758	$387,741	$148,048
Cost of goods sold	213,310	79,487	383,894	153,825
Gross profit (loss)	1,283	(2,729)	3,847	(5,777)
Selling, general and administrative expenses	4,059	3,177	8,247	6,333
Loss from operations	(2,776)	(5,906)	(4,400)	(12,110)
Fair value adjustments on convertible debt and warrants	1,929	—	2,855	—
Loss on extinguishments of debt	—	(544)	—	(2,159)
Interest expense, net	(3,628)	(1,271)	(7,266)	(2,863)
Other expense, net	(200)	(421)	(543)	(466)
Loss before reorganization costs, gain from bankruptcy exit and provision for income taxes	(4,675)	(8,142)	(9,354)	(17,598)
Reorganization costs	—	(2,714)	—	(4,153)
Gain from bankruptcy exit	—	119,408	—	119,408
Provision for income taxes	—	—	—	—
Net income (loss)	(4,675)	108,552	(9,354)	97,657
Net loss attributed to noncontrolling interest in variable interest entity	(5,425)	—	(10,122)	—
Net income attributed to Pacific Ethanol	$750	$108,552	$768	$97,657
Preferred stock dividends	$(315)	$(798)	$(627)	$(1,588)
Income available to common stockholders	$435	$107,754	$141	$96,069
Net income per share, basic	$0.03	$10.95	$0.01	$10.61
Net income per share, diluted	$0.03	$10.01	$0.01	$9.71
Weighted-average shares outstanding, basic	16,768	9,842	15,183	9,057
Weighted-average shares outstanding, diluted	16,768	10,847	15,183	10,062

See accompanying notes to consolidated financial statements.

PACIFIC ETHANOL, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, in thousands)

	Six Months Ended June 30, 2011	Six Months Ended June 30, 2010
Operating Activities:		
Net income (loss)	$(9,354)	$97,657
Adjustments to reconcile net income (loss) to cash used in operating activities:		
Fair value adjustments on convertible debt and warrants	(2,855)	—
Gain on bankruptcy exit	—	(119,408)
Loss on extinguishment of debt	—	2,159
Depreciation and amortization of intangibles	6,319	5,708
Inventory valuation	—	136
Amortization of deferred financing fees	319	269
Noncash compensation	1,525	891
Derivative instruments	61	(1,206)
Bad debt expense	(140)	(214)
Equity earnings in Front Range	—	334
Changes in operating assets and liabilities:		
Accounts receivable	(8,286)	(6,653)
Inventories	(3,545)	1,554
Prepaid expenses and other assets	579	334
Prepaid inventory	(3,426)	525
Accounts payable and accrued expenses	4,804	9,956
Net cash used in operating activities	(13,999)	(7,958)
Investing Activities:		
Additions to property and equipment	(1,364)	(277)
Net cash impact of deconsolidation of Front Range	—	(10,486)
Net cash impact of bankruptcy exit	—	(1,301)
Net cash used in investing activities	(1,364)	(12,064)
Financing Activities:		
Net Proceeds from borrowings	16,459	4,452
Net cash provided by financing activities	16,459	4,452
Net increase (decrease) in cash and cash equivalents	1,096	(15,570)
Cash and cash equivalents at beginning of period	8,736	17,545
Cash and cash equivalents at end of period	$9,832	$1,975
Supplemental Information:		
Interest paid	$5,529	$3,150
Noncash financing and investing activities:		
Preferred stock dividends accrued	$627	$1,588
Debt extinguished with issuance of common stock	$14,700	$19,000

See accompanying notes to consolidated financial statements.

PACIFIC ETHANOL, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. ORGANIZATION AND BASIS OF PRESENTATION.

Organization and Business – The consolidated financial statements include the accounts of Pacific Ethanol, Inc., a Delaware corporation ("Pacific Ethanol"), and its wholly-owned subsidiaries, including Pacific Ethanol California, Inc., a California corporation, Kinergy Marketing LLC, an Oregon limited liability company ("Kinergy") and Pacific Ag. Products, LLC, a California limited liability company ("PAP") for all periods presented, and for the periods specified below, the Plant Owners (as defined below) (collectively, the "Company").

The Company is the leading marketer and producer of low carbon renewable fuels in the Western United States. The Company also sells ethanol co-products, including wet distillers grain and syrup ("WDG"), and provides transportation, storage and delivery of ethanol through third-party service providers in the Western United States, primarily in California, Nevada, Arizona, Oregon, Colorado, Idaho and Washington. The Company sells ethanol produced by the Pacific Ethanol Plants (as defined below) and unrelated third parties to gasoline refining and distribution companies and sells its WDG to dairy operators and animal feed distributors.

On May 17, 2009, five indirect wholly-owned subsidiaries of Pacific Ethanol, namely, Pacific Ethanol Madera LLC, Pacific Ethanol Columbia, LLC, Pacific Ethanol Stockton, LLC and Pacific Ethanol Magic Valley, LLC (collectively, the "Pacific Ethanol Plants") and Pacific Ethanol Holding Co. LLC (together with the Pacific Ethanol Plants, the "Plant Owners") each filed voluntary petitions for relief under chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the District of Delaware (the "Bankruptcy Court") in an effort to restructure their indebtedness (the "Chapter 11 Filings"). The Plant Owners continued to operate their businesses and manage their properties as debtors and debtors-in-possession during the pendency of the bankruptcy proceedings.

On June 29, 2010 (the "Effective Date"), the Plant Owners declared effective their amended joint plan of reorganization (the "Plan") with the Bankruptcy Court, which was structured in cooperation with certain of the Plant Owners' secured lenders. Under the Plan, on the Effective Date, 100% of the ownership interests in the Plant Owners were transferred from Pacific Ethanol to a newly-formed limited liability company, New PE Holdco, LLC ("New PE Holdco") which is wholly-owned by certain prepetition lenders, resulting in each of the Plant Owners becoming wholly-owned subsidiaries of New PE Holdco.

Under an asset management agreement, the Company manages the production and operation of the Pacific Ethanol Plants. On October 6, 2010, the Company purchased a 20% ownership interest in New PE Holdco, a variable interest entity, from a number of New PE Holdco's existing owners. At that time, the Company determined it was the primary beneficiary of New PE Holdco, and as such, has consolidated the results of New PE Holdco since that time (see Note 2).

These four facilities have an aggregate annual production capacity of up to 200 million gallons. As of June 30, 2011, three of the facilities were operating and one of the facilities was idled. If market conditions continue to improve, the Company may resume operations at the Madera, California facility, subject to the approval of New PE Holdco.

Reverse Stock Split – On June 8, 2011, the Company effected a one-for-seven reverse stock split. All share and per share information has been restated to retroactively show the effect of this stock split.

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Liquidity – The Company believes that current and future available capital resources, revenues generated from operations, and other existing sources of liquidity, including its credit facilities, will be adequate to meet its anticipated working capital and capital expenditure requirements for at least the next twelve months. If, however, the Company is unable to service the principal and/or interest payments under its outstanding senior convertible notes through the issuance of shares of its common stock, if the Company's capital requirements or cash flow vary materially from its current projections, if unforeseen circumstances occur, or if the Company requires a significant amount of cash to fund future acquisitions, the Company may require additional financing. The Company's failure to raise capital, if needed, could restrict its growth, or hinder its ability to compete.

Accounts Receivable and Allowance for Doubtful Accounts – Trade accounts receivable are presented at face value, net of the allowance for doubtful accounts. The Company sells ethanol to gasoline refining and distribution companies and sells WDG to dairy operators and animal feed distributors generally without requiring collateral.

The Company maintains an allowance for doubtful accounts for balances that appear to have specific collection issues. The collection process is based on the age of the invoice and requires attempted contacts with the customer at specified intervals. If, after a specified number of days, the Company has been unsuccessful in its collection efforts, a bad debt allowance is recorded for the balance in question. Delinquent accounts receivable are charged against the allowance for doubtful accounts once uncollectibility has been determined. The factors considered in reaching this determination are the apparent financial condition of the customer and the Company's success in contacting and negotiating with the customer. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of ability to make payments, additional allowances may be required.

Of the accounts receivable balance, approximately $28,990,000 and $20,977,000 at June 30, 2011 and December 31, 2010, respectively, were used as collateral under Kinergy's working capital line of credit. The allowance for doubtful accounts was $108,000 and $287,000 as of June 30, 2011 and December 31, 2010, respectively. The Company recorded net bad debt recoveries of $10,000 and $174,000 for the three months ended June 30, 2011 and 2010, respectively. The Company recorded net bad debt recoveries of $140,000 and $214,000 for the six months ended June 30, 2011 and 2010, respectively.

Basis of Presentation–Interim Financial Statements – The accompanying unaudited consolidated financial statements and related notes have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and the instructions to Form 10-Q and Rule 10-01 of Regulation S-X. Results for interim periods should not be considered indicative of results for a full year. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2010, filed with the Securities and Exchange Commission on March 31, 2011. The accounting policies used in preparing these consolidated financial statements are the same as those described in Note 1 to the consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2010. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair statement of the results for interim periods have been included. All significant intercompany accounts and transactions have been eliminated in consolidation.

The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States 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 revenues and expenses during the reporting period. Significant estimates are required as part of determining fair value of convertible debt and warrants, allowance for doubtful accounts, estimated lives of property and equipment and intangibles, long-lived asset impairments, valuation allowances on deferred income taxes and the potential outcome of future tax consequences of events recognized in the Company's financial statements or tax returns. Actual results and outcomes may materially differ from management's estimates and assumptions.

Reclassifications of prior year's data have been made to conform to 2011 classifications. Such classifications had no effect on net loss reported in the consolidated statements of operations.

2. VARIABLE INTEREST ENTITY.

On October 6, 2010, the Company purchased a 20% ownership interest in New PE Holdco from a number of New PE Holdco's existing equity owners. The Company concluded that upon its purchase of the 20% ownership interest in New PE Holdco, the Company became the primary beneficiary of New PE Holdco and consolidated the financial results of New PE Holdco. In making this conclusion, the Company determined that New PE Holdco was a variable interest entity and the Company, through its contractual arrangements (discussed below) had the power to direct most of its activities that most significantly impacted New PE Holdco's economic performance. Some of these activities included efficient management and operation of the Pacific Ethanol Plants, procurement of feedstock, sale of co-products and implementation of risk management strategies.

The carrying values and classification of assets that are collateral for the obligations of New PE Holdco at June 30, 2011 were as follows (in thousands):

Current assets	$12,803
Property and equipment	160,380
Other assets	2,345
Total assets	$175,528
Current liabilities	$6,220
Long-term debt	79,257
Other liabilities	133
Total liabilities	$85,610

The Company's acquisition of its ownership interest in New PE Holdco does not impact the Company's rights or obligations under any of the following agreements. Since its acquisition, the Company has not provided any additional support to New PE Holdco beyond the terms of the agreements described below. Creditors of New PE Holdco do not have recourse to Pacific Ethanol. The Company, directly or through one of its subsidiaries, has entered into the following management and marketing agreements:

Asset Management Agreement – The Company entered into an Asset Management Agreement ("AMA") with the Plant Owners under which the Company agreed to operate and maintain the Pacific Ethanol Plants on behalf of the Plant Owners. These services generally include, but are not limited to, administering the Plant Owners' compliance with their credit agreements and performing billing, collection, record keeping and other administrative and ministerial tasks. The Company agreed to supply all labor and personnel required to perform its services under the AMA, including the labor and personnel required to operate and maintain the production facilities.

The costs and expenses associated with the Company's provision of services under the AMA are prefunded by the Plant Owners under a preapproved budget. The Company's obligation to provide services is limited to the extent there are sufficient funds advanced by the Plant Owners to cover the associated costs and expenses. As compensation for providing the services under the AMA, the Company is to be paid $75,000 per month for each production facility that is operational and $40,000 per month for each production facility that is idled.

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The AMA had an initial term of six months and successive six-month renewal periods at the option of the Plant Owners. In addition to typical conditions for a party to terminate the agreement prior to its expiration, the Company may terminate the AMA, and the Plant Owners may terminate the AMA with respect to any facility, at any time by providing at least 60 days prior notice of such termination. On June 30, 2011, the AMA was amended and extended for one year.

Ethanol Marketing Agreements – Kinergy entered into separate ethanol marketing agreements with each of the three Plant Owners whose facilities are operating, which granted Kinergy the exclusive right to purchase, market and sell the ethanol produced at those facilities. Under the terms of the ethanol marketing agreements, within ten days after delivering ethanol to Kinergy, an amount is to be paid equal to (i) the estimated purchase price payable by the third-party purchaser of the ethanol, minus (ii) the estimated amount of transportation costs to be incurred by Kinergy, minus (iii) the estimated incentive fee payable to Kinergy, which equals 1% of the aggregate third-party purchase price. Each of the ethanol marketing agreements had an initial term of one year and successive one year renewal periods at the option of the individual Plant Owner. On June 30, 2011, all ethanol marketing agreements were amended and extended for one year. In addition, the price to be paid to Kinergy was amended to include a marketing fee collar of not less than $0.15 per gallon and not more than $0.225 per gallon.

Corn Procurement and Handling Agreements – PAP entered into separate corn procurement and handling agreements with each of the three Plant Owners whose facilities are operating. Under the terms of the corn procurement and handling agreements, each facility appointed PAP as its exclusive agent to solicit, negotiate, enter into and administer, on its behalf, corn supply arrangements to procure the corn necessary to operate its facility. PAP will also provide grain handling services including, but not limited to, receiving, unloading and conveying corn into the facility's storage and, in the case of whole corn delivered, processing and hammering the whole corn.

PAP was to receive a fee of $0.50 per ton of corn delivered to each facility as consideration for its procurement services and a fee of $1.50 per ton of corn delivered as consideration for its grain handling services, each payable monthly. The Company agreed to enter into an agreement guaranteeing the performance of PAP's obligations under the corn procurement and handling agreement upon the request of a Plant Owner. Each corn procurement and handling agreement had an initial term of one year and successive one year renewal periods at the option of the individual Plant Owner. On June 30, 2011, all corn procurement and handling agreements were amended and extended for one year. In addition, the corn procurement and handling fee was changed to $0.045 per bushel of corn.

Distillers Grains Marketing Agreements – PAP entered into separate distillers grains marketing agreements with each of the three Plant Owners whose facilities are operating, which granted PAP the exclusive right to market, purchase and sell the WDG produced at the facility. Under the terms of the distillers grains marketing agreements, within ten days after a Plant Owner delivers WDG to PAP, the Plant Owner is to be paid an amount equal to (i) the estimated purchase price payable by the third-party purchaser of the WDG, minus (ii) the estimated amount of transportation costs to be incurred by PAP, minus (iii) the estimated amount of fees and taxes payable to governmental authorities in connection with the tonnage of WDG produced or marketed, minus (iv) the estimated incentive fee payable to PAP, which equals the greater of (a) 5% of the aggregate third-party purchase price, and (b) $2.00 for each ton of WDG sold in the transaction. Each distillers grains marketing agreement had an initial term of one year and successive one year renewal periods at the option of the individual Plant Owner. On June 30, 2011, all distillers grains marketing agreements were amended and extended for one year. In addition, the fee to be paid to PAP was amended to include a collar of not less than $2.00 per ton and not more than $3.50 per ton.

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3. INVENTORIES.

Inventories consisted primarily of bulk ethanol, unleaded fuel and corn, and are valued at the lower-of-cost-or-market, with cost determined on a first-in, first-out basis. Inventory balances consisted of the following (in thousands):

	June 30, 2011	December 31, 2010
Finished goods	$14,045	$11,105
Work in progress	4,529	4,087
Raw materials	1,345	1,308
Other	932	806
Total	$20,851	$17,306

4. DERIVATIVES.

The business and activities of the Company expose it to a variety of market risks, including risks related to changes in commodity prices and interest rates. The Company monitors and manages these financial exposures as an integral part of its risk management program. This program recognizes the unpredictability of financial markets and seeks to reduce the potentially adverse effects that market volatility could have on operating results.

Commodity Risk – Cash Flow Hedges – The Company uses derivative instruments to protect cash flows from fluctuations caused by volatility in commodity prices for periods of up to twelve months in order to protect gross profit margins from potentially adverse effects of market and price volatility on ethanol sale and purchase commitments where the prices are set at a future date and/or if the contracts specify a floating or index-based price for ethanol. In addition, the Company hedges anticipated sales of ethanol to minimize its exposure to the potentially adverse effects of price volatility. These derivatives may be designated and documented as cash flow hedges and effectiveness is evaluated by assessing the probability of the anticipated transactions and regressing commodity futures prices against the Company’s purchase and sales prices. Ineffectiveness, which is defined as the degree to which the derivative does not offset the underlying exposure, is recognized immediately in cost of goods sold. For the three and six months ended June 30, 2011 and 2010, the Company did not designate any of its derivatives as cash flow hedges.

Commodity Risk – Non-Designated Hedges – The Company uses derivative instruments to lock in prices for certain amounts of corn and ethanol by entering into forward contracts for those commodities. These derivatives are not designated for special hedge accounting treatment. The changes in fair value of these contracts are recorded on the balance sheet and recognized immediately in cost of goods sold. The Company recognized losses of $89,000 and $0 as the change in the fair value of these contracts for the three months ended June 30, 2011 and 2010, respectively. The Company recognized losses of $61,000 and $0 as the change in the fair value of these contracts for the six months ended June 30, 2011 and 2010, respectively. The notional balances remaining on these contracts were $539,000 and $237,000 as of June 30, 2011 and December 31, 2010, respectively.

Interest Rate Risk – The Company, through the Plant Owners, uses derivative instruments to minimize significant unanticipated income fluctuations that may arise from rising variable interest rate costs associated with existing and anticipated borrowings. To meet these objectives the Company purchased interest rate caps and swaps. On the Effective Date, all interest rate caps and swaps were removed from the Company’s consolidated statement of position. For the three and six months ended June 30, 2010, the Company recognized gains from undesignated hedges of $684,000 and $1,247,000 in interest expense, net, respectively.

Non Designated Derivative Instruments – The Company classified its derivative instruments not designated as hedging instruments of $53,000 and $15,000 in accrued liabilities as of June 30, 2011 and December 31, 2010, respectively.

The classification and amounts of the Company's recognized gains (losses) for its derivatives not designated as hedging instruments are as follow (in thousands):

Type of Instrument	Statements of Operations Location	Realized Losses For the Three Months Ended June 30, 2011	2010
Commodity contracts	Cost of goods sold	$ (36)	$ —
		$ (36)	$ —

Type of Instrument	Statements of Operations Location	Unrealized Gains (Losses) For the Three Months Ended June 30, 2011	2010
Commodity contracts	Cost of goods sold	$ (53)	$ —
Interest rate contracts	Interest expense, net	—	684
		$ (53)	$ 684

Type of Instrument	Statements of Operations Location	Realized Losses For the Six Months Ended June 30, 2011	2010
Commodity contracts	Cost of goods sold	$ (23)	$ —
		$ (23)	$ —

Type of Instrument	Statements of Operations Location	Unrealized Gains (Losses) For the Six Months Ended June 30, 2011	2010
Commodity contracts	Cost of goods sold	$ (38)	$ —
Interest rate contracts	Interest expense, net	—	1,247
		$ (38)	$ 1,247

5. DEBT.

Long-term borrowings are summarized as follows (in thousands):

	June 30, 2011	December 31, 2010
Convertible notes, at fair value	$25,134	$38,108
New PE Holdco term debt	51,279	51,279
New PE Holdco operating line of credit	27,978	18,978
Kinergy operating line of credit	20,933	13,474
Notes payable to related parties	1,250	1,250
	126,574	123,089
Less short-term portion	(26,384)	(38,108)
Long-term debt	$100,190	$84,981

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Convertible Notes – On October 6, 2010, the Company raised $35,000,000 through the issuance and sale of $35,000,000 in principal amount of secured convertible notes ("Initial Notes") and warrants ("Initial Warrants") to purchase an aggregate of 2,941,178 shares of the Company's common stock. On January 7, 2011, under the terms of exchange agreements with the holders of the Initial Notes and Initial Warrants, the Company issued $35,000,000 in principal amount of secured convertible notes ("January Convertible Notes") in exchange for the Initial Notes and warrants ("Warrants") to purchase an aggregate of 2,941,178 shares of the Company's common stock in exchange for the Initial Warrants.

The transactions contemplated by the exchange agreements were entered into to, among other things, clarify previously ambiguous language in the Initial Notes and Initial Warrants, provide the Company with additional time to meet its registration obligations and to add additional flexibility to the Company's ability to incur indebtedness subordinated to the January Convertible Notes. As discussed below, the January Convertible Notes were valued at fair value, and as such, these modifications had been reflected in the fair value adjustments for the period.

On June 30, 2011, under the terms of exchange agreements with the holders of the January Convertible Notes, the Company issued $23,750,000 in principal amount, reflecting the amount then outstanding under the January Convertible Notes, of secured convertible notes ("June Convertible Notes") in exchange for the January Convertible Notes.

The transactions contemplated by the exchange agreements were entered into to, among other things, defer the August 1, 2011 Installment Payment, add one additional month to the maturity date and add a new additional conversion price option to the holders as described further below. As discussed below, the June Convertible Notes are valued at fair value, and as such, these modifications have been reflected in the fair value adjustments for the period.

On August 3, 2011, under the terms of exchange agreements with the holders of the June Convertible Notes, the Company issued approximately $17,170,000 in principal amount, reflecting the amount then outstanding under the June Convertible Notes, of secured convertible notes ("Convertible Notes") in exchange for the June Convertible Notes.

The transactions contemplated by the exchange agreements were entered into to, among other things, add three additional months to the maturity date, add a new additional conversion price option as described further below and reduced the Price Failure threshold from $1.40 to $0.60. As discussed below, the Convertible Notes are valued at fair value, and as such, these modifications will be reflected in the fair value adjustments for period ending September 30, 2011.

The Convertible Notes mature on May 6, 2012, subject to the right of the lenders to extend the date (i) if an event of default under the Convertible Notes has occurred and is continuing or any event shall have occurred and be continuing that with the passage of time and the failure to cure would result in an event of default under the Convertible Notes, and (ii) for a period of 20 business days after the consummation of specific types of transactions involving a change of control. The Convertible Notes bear interest at the rate of 8% per annum, which is compounded monthly, with any accrued interest recorded as accrued liabilities in the consolidated balance sheets. The interest rate will increase to 15% per annum upon the occurrence of an event of default. The Company had approximately $0 and $657,000 in accrued interest with respect to the Convertible Notes as of June 30, 2011 and December 31, 2010, respectively.

The Company is obligated to make amortization payments with respect to the principal amount of each Convertible Note on the first trading day of each calendar month after August 1, 2011 until the Maturity Date (collectively with the Maturity Date, the "Installment Dates").

On each Installment Date, occurring after August 1, 2011, the Company shall pay on each Convertible Note an amount equal to: (i) with respect to any Installment Date other than the Maturity Date, the lesser of (A) the product of (I) the quotient of (x) $21 million divided by (y) 9, multiplied by (II) the fraction equal to (m) the principal amount of the Initial Note on October 6, 2010 divided by (n) $35 million and (B) the principal amount under the Convertible Note as of such Installment Date, and (ii) with respect to the Maturity Date, the principal amount under the Convertible Note, together with, in each case of clauses (i) and (ii), the sum of any accrued and unpaid Interest as of such Installment Date under the Convertible Note and accrued and unpaid late charges, if any, under the Convertible Note as of such Installment Date (the "Installment Amount"). The Company may elect to pay the Installment Amount in cash or shares of its common stock, at its election, subject to the satisfaction of certain conditions.

If the Company elects to make all or part of an amortization payment in shares of its common stock, it is required to deliver to the holders of the Convertible Notes the amount of shares of the Company's common stock equal to the portion of the amount being paid in shares of the Company's common stock divided by the lesser of the then existing Conversion Price and 85% of the average of the volume weighted average prices of the 5 lowest trading days during the 20 consecutive trading day period ending on the trading day immediately prior to the applicable Installment Date.

All amounts due under the Convertible Notes are convertible at any time, in whole or in part, at the option of the holders into shares of the Company's common stock at a specified conversion price ("Conversion Price"). The Convertible Notes were initially convertible into shares of the Company's common stock at the initial Conversion Price of $5.95 per share ("Fixed Conversion Price"). The Conversion Price is not to exceed $5.95 and, unless the Company obtains a waiver, it cannot make monthly amortization and interest payments in shares of common stock if the Conversion Price is less than $0.60.

The Convertible Notes are now convertible by the holders into shares of the Company's common stock at a Conversion Price that is determined as follows:

- If the Company has elected to make an amortization payment in shares of common stock and the date of conversion occurs during the 15 calendar day period following (and including) the applicable Installment Date ("Initial Period"), the Conversion Price will equal the lesser of (i) the Fixed Conversion Price, and (ii) the average of the volume weighted average prices of the Company's common stock for each of the five lowest trading days during the 20 trading day period immediately prior to the Initial Period.

- If the Company has elected to make an amortization payment in shares of common stock and the date of conversion occurs during the period beginning on the 16th calendar day after the applicable Installment Date and ending on the day immediately prior to the next Installment Date or the maturity date, the Conversion Price will equal the lesser of (i) the Fixed Conversion Price, and (ii) the closing bid price of the Company's common stock on the trading date immediately before the date of conversion.

- The holder may, up to three times, elect a 12% discount to the closing bid price of the Company's common stock on the date immediately before the conversion.

- Four of the seven holders may, up to fifteen times, elect a 15% discount to the closing bid price of the Company's common stock on the date immediately before the conversion while the other three holders may, up to fifteen times, elect a 10% discount to the closing bid price of the Company's common stock on the date immediately before the conversion.

In addition, if an event of default has occurred and is continuing, the Conversion Price will be equal to the lesser of (i) the Fixed Conversion Price, and (ii) the closing bid price of the Company's common stock on the trading date immediately before the date of conversion.

The Fixed Conversion Price is subject to adjustment for stock splits, combinations or similar events. The Fixed Conversion Price is subject to "full ratchet" anti-dilution adjustment where if the Company was to issue or is deemed to have issued specified securities at a price lower than the then applicable Fixed Conversion Price, the Fixed Conversion Price will immediately decline to equal the price at which the Company issued or is deemed to have issued the securities. In addition, if the Company sells or issues any securities with "floating" conversion prices based on the market price of its common stock, the holder of a Convertible Note will have the right to substitute that "floating" conversion price for the Fixed Conversion Price upon conversion of all or part of the Convertible Note.

If the Company does not deliver shares of common stock due upon conversion of a Convertible Note within 3 trading days of a conversion, and, after such third trading day, the converting holder purchases shares of the Company's common stock to deliver in satisfaction of a sale by the converting holder of shares of common stock issuable upon the conversion that the converting holder anticipated receiving from the Company, upon request of the converting holder, the Company is required to either (i) pay cash to the converting holder in an amount equal to the converting holder's total purchase price for the shares of common stock so purchased (the "Buy-In Price"), at which point the Company's obligation to deliver the shares issuable upon the conversion shall terminate, or (ii) deliver shares of common stock due upon conversion and pay cash to the converting Holder in an amount equal to the excess (if any) of the Buy-In Price over the market value of the shares issuable upon conversion on the trading day immediately before the conversion date.

The Convertible Notes may not be converted if, after giving effect to the conversion, the holder together with its affiliates would beneficially own in excess of 4.99% or 9.99% (which percentage has been established at the election of each holder) of the Company's outstanding shares of common stock (the "Blocker"). The Blocker applicable to the conversion of the Convertible Notes may be raised or lowered to any other percentage not in excess of 9.99% or less than 4.99%, subject to an advance notice period, at the option of the holder.

The Company issued 1,148,000 shares of its common stock to satisfy the March 7, 2011 Installment Date payment of $3,500,000 in principal and $1,263,000 in accrued interest. The Company issued 1,396,000 shares of its common stock to satisfy the May 2, 2011 Installment Date payment of $3,500,000 in principal and $383,000 in accrued interest. The Company issued 1,563,000 shares of its common stock to satisfy the June 1, 2011 Installment Date payment of $3,350,000 in principal and $176,000 in accrued interest.

Through June 30, 2011, the Company issued an aggregate of 428,000 shares of its common stock to satisfy $900,000 in principal and $49,000 in interest in respect of additional note conversions by holders of the Convertible Notes.

The Company also elected to issue shares of its common stock to satisfy its July 1, 2011 Installment Date payment of principal and accrued interest. In accordance with the Convertible Notes, on June 6, 2011, the Company issued 1,617,000 shares of its common stock as a pre-installment payment of $3,450,000 in principal and $159,000 in accrued interest and on July 1, 2011, issued an additional 1,696,000 "true-up" shares of its common stock.

On August 3, 2011, the Company notified the holders that it would pay the Installment Amount due on the September 1, 2011 Installment Date in cash.

As of August 9, 2011, based on the current Conversion Price of $0.76, the Convertible Notes were convertible into an additional 19,800,000 shares of the Company's common stock, if it were to elect to make the remainder of the scheduled monthly payments of principal and interest in shares of its common stock.

Since the July 1, 2011 Installment Date through August 9, 2011, the Company issued an aggregate of 4,523,000 shares of its common stock to satisfy $3,572,000 in principal and $196,000 in interest in respect of additional note conversions by holders of the Convertible Notes.

The Company has elected to account for the Convertible Notes using the fair value alternative in order to simplify its accounting and reporting of the Convertible Notes. Accordingly, the Company has adjusted the carrying value of the Convertible Notes to their fair value as of June 30, 2011, as reflected in fair value adjustments on convertible debt and warrants in the statements of operations. The recorded fair value of the Convertible Notes of $25,134,000 differed from the stated unpaid principal amounts of $20,300,000 as of June 30, 2011.

The Company recorded an expense of $1,913,000 and income of $187,000 for fair value adjustments for the three and six months ended June 30, 2011, respectively, for changes in fair value, which adjustments are attributed to term shortening and reduction in the market value of the Company's common stock. There were no changes in fair value of the Convertible Notes due to a change in the estimated credit risk of the instruments. See Note 8 for the Company's fair value assumptions.

New PE Holdco Working Capital Line of Credit – For the six months ended June 30, 2011, New PE Holdco borrowed $9,000,000 on its working capital line of credit, and as of June 30, 2011 had approximately $7,000,000 in borrowing capacity under its line of credit.

Kinergy Operating Line of Credit – In May 2011, Kinergy and its lender amended and increased Kinergy's credit facility to up to $30,000,000, with an optional accordion feature for an additional $5,000,000.

Loss on Extinguishment of Debt – In 2010, the Company announced agreements designed to satisfy its indebtedness to Lyles United, LLC and Lyles Mechanical Co. (collectively, "Lyles"). Socius CG II, Ltd. ("Socius") entered into purchase agreements with Lyles under which Socius would purchase claims in respect of the Company's indebtedness in up to $5,000,000 tranches, which claims Socius would then settle in exchange for shares of the Company's common stock. Each tranche was to be settled in exchange for the Company's common stock valued at a 20% discount to the volume weighted average price of the Company's common stock over a predetermined trading period, which ranged from five to 20 trading days, immediately following the date on which the shares were first issued to Socius. Under this arrangement, the Company issued shares to Socius which settled outstanding debt previously owed to Lyles. For the three months ended June 30, 2010, the Company issued an aggregate of 16,226,000 shares with an aggregate fair value of $9,544,000 in exchange for $9,000,000 in debt extinguishment, resulting in an aggregate loss of $544,000. For the six months ended June 30, 2010, the Company issued an aggregate of 24,088,000 shares with an aggregate fair value of $21,159,000 in exchange for $19,000,000 in debt extinguishment, resulting in an aggregate loss of $2,159,000. The Company determined fair value based on the closing price of its shares on the last day of the applicable trading period, which was the date the net shares to be issued were determinable by the Company.

6. PREFERRED STOCK

For the three months ended June 30, 2011, no shares of the Company's Series B Cumulative Convertible Preferred Stock ("Series B Preferred Stock") were converted into shares of the Company's common stock. For the six months ended June 30, 2011, 528,982 shares of the Company's Series B Preferred Stock were converted into 443,589 shares of the Company's common stock.

7. COMMITMENTS AND CONTINGENCIES.

Purchase Commitments – At June 30, 2011, the Company had fixed-price purchase contracts with its suppliers to purchase $15,801,000 of ethanol. These fixed-price contracts will be satisfied throughout the remainder of 2011. At June 30, 2011, the Company had indexed-price purchase contracts with its suppliers to purchase 415,000 gallons of ethanol.

Sales Commitments – At June 30, 2011, the Company had entered into sales contracts with its major customers to sell certain quantities of ethanol and WDG. The volumes indicated in the indexed price contracts table will be sold at publicly-indexed sales prices determined by market prices in effect on their respective transaction dates (in thousands):

	Fixed-Price Contracts
Ethanol	$ 6,103
WDG	4,319
Total	$ 10,422

	Indexed-Price Contracts (Volume)
Ethanol (gallons)	145,062
WDG (tons)	15

Litigation – General – The Company is subject to legal proceedings, claims and litigation arising in the ordinary course of business. While the amounts claimed may be substantial, the ultimate liability cannot presently be determined because of considerable uncertainties that exist. Therefore, it is possible that the outcome of those legal proceedings, claims and litigation could adversely affect the Company's quarterly or annual operating results or cash flows when resolved in a future period. However, based on facts currently available, management believes that such matters will not adversely affect the Company's financial position, results of operations or cash flows.

8. FAIR VALUE MEASUREMENTS.

The fair value hierarchy prioritizes the inputs used in valuation techniques into three levels as follows:

- Level 1 – Observable inputs – unadjusted quoted prices in active markets for identical assets and liabilities;
- Level 2 – Observable inputs other than quoted prices included in Level 1 that are observable for the asset or liability through corroboration with market data; and
- Level 3 – Unobservable inputs – includes amounts derived from valuation models where one or more significant inputs are unobservable. For fair value measurements using significant unobservable inputs, a description of the inputs and the information used to develop the inputs is required along with a reconciliation of Level 3 values from the prior reporting period.

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Convertible Notes and Warrants – The Company has recorded its Convertible Notes and Warrants at fair value and designated them as Level 3.

The Convertible Notes were valued using a combination of a Monte Carlo Binomial Lattice-Based valuation methodology for the embedded conversion feature, adjusted for marketability restrictions, combined with a discounted cash flow model for the payment stream of the debt instrument. The significant assumptions used in the valuations are as follows:

Assumptions	June 30, 2011	December 31, 2010
Stock price	$1.08	$5.04
Volatility	49.5%	68.4%
Risk free interest rate	0.15%	0.29%
Term (years)	0.61	1.03
Marketability discount	15.3%	27.0%
Discount rate of debt instrument	30.0%	30.0%

Based on the above, the Company estimated the fair value of the Convertible Notes to be $25,134,000 and $38,108,000 at June 30, 2011 and December 31, 2010, respectively.

The Warrants were valued using a Monte Carlo Binomial Lattice-Based valuation methodology, adjusted for marketability restrictions. The significant assumptions used in the valuations are as follows:

Assumptions	June 30, 2011	December 31, 2010
Stock price	$1.08	$5.04
Volatility	56.7%	63.5%
Risk free interest rate	2.50%	2.71%
Term (years)	6.40	6.90
Marketability discount	40.4%	44.4%

Based on the above, the Company estimated the fair value of the Warrants to be $1,137,000 and $5,718,000 at June 30, 2011 and December 31, 2010, respectively.

Other Derivative Instruments – The Company’s other derivative instruments consist of commodity positions. The fair value of the commodity positions are based on quoted prices on the commodity exchanges and are designated as Level 1.

The following table summarizes fair value measurements by level at June 30, 2011 (in thousands):

	Level 1	Level 2	Level 3	Total
Liabilities:				
Convertible Notes	$—	$—	$25,134	$25,134
Warrants(1)	—	—	1,137	1,137
Commodity contracts(2)	53	—	—	53
Total Liabilities	$53	$---	$26,271	$26,324

(1) Included in other liabilities in the consolidated balance sheets.
(2) Included in accrued liabilities in the consolidated balance sheets.

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The following table summarizes fair value measurements by level at December 31, 2010 (in thousands):

	Level 1	Level 2	Level 3	Total
Liabilities:				
Convertible Notes	$—	$—	$38,108	$38,108
Warrants(1)	—	—	5,718	5,718
Commodity contracts(2)	15	—	—	15
Total Liabilities	$15	$---	$43,826	$43,841

(1) Included in other liabilities in the consolidated balance sheets.
(2) Included in accrued liabilities in the consolidated balance sheets.

The changes in the Company's fair value of its Level 3 inputs are as follows (in thousands):

	Convertible Notes	Warrants
Balance, December 31, 2010	$38,108	$5,718
Principal payments	(14,700)	—
Adjustments to fair value for the period	1,726	(4,581)
Balance, June 30, 2011	$25,134	$1,137

9. EARNINGS PER SHARE.

The following tables compute basic and diluted earnings per share (in thousands, except per share data):

	Three Months Ended June 30, 2011		
	Income Numerator	Shares Denominator	Per-Share Amount
Net income	$750		
Less: Preferred stock dividends	(315)		
Basic and diluted loss per share:			
Income available to common stockholders	$435	16,768	$0.03

	Three Months Ended June 30, 2010		
	Income Numerator	Shares Denominator	Per-Share Amount
Net income	$108,552		
Less: Preferred stock dividends	(798)		
Basic income per share:			
Income available to common stockholders	$107,754	9,842	$10.95
Add: Preferred stock dividends	798	1,005	
Diluted income per share:			
Income available to common stockholders	$108,552	10,847	$10.01

	Six Months Ended June 30, 2011		
	Income Numerator	Shares Denominator	Per-Share Amount
Net income	$768		
Less: Preferred stock dividends	(627)		
Basic and diluted loss per share:			
Income available to common stockholders	$141	15,183	$0.01

	Six Months Ended June 30, 2010		
	Income Numerator	Shares Denominator	Per-Share Amount
Net income	$97,657		
Less: Preferred stock dividends	(1,588)		
Basic income per share:			
Income available to common stockholders	$96,069	9,057	$10.61
Add: Preferred stock dividends	1,588	1,005	
Diluted income per share:			
Income available to common stockholders	$97,657	10,062	$9.71

There were an aggregate of 11,276,000 and 23,476,000 potentially dilutive weighted-average shares from convertible securities outstanding for the three and six months ended June 30, 2011, respectively. These convertible securities were not considered in calculating diluted net loss per share for the three and six months ended June 30, 2011, as their effect would have been anti-dilutive.

10. RELATED PARTY TRANSACTIONS.

The Company had accrued and unpaid dividends in respect of its Series B Preferred Stock of $6,677,000 and $6,050,000 as of June 30, 2011 and December 31, 2010, respectively.

The Company had notes payable to its Chairman of the Board and its Chief Executive Officer totaling $1,250,000 as of June 30, 2011 and December 31, 2010. These notes mature on March 31, 2012.

11. PLANT OWNERS' CONDENSED COMBINED FINANCIAL STATEMENTS.

Since the consolidated financial statements of the Company include entities other than the Plant Owners, the following presents the condensed combined financial statements of the Plant Owners. These condensed combined financial statements have been prepared, in all material respects, on the same basis as the consolidated financial statements of the Company. The condensed combined financial statements of the Plant Owners are as follows (unaudited, in thousands):

PACIFIC ETHANOL HOLDING CO. LLC AND SUBSIDIARIES
CONDENSED COMBINED STATEMENT OF OPERATIONS

	Three Months Ended June 30, 2010	Six Months Ended June 30, 2010
Net sales	$ 47,052	$ 89,737
Cost of goods sold	51,411	98,140
Gross loss	(4,359)	(8,403)
Selling, general and administrative expenses	843	1,829
Loss from operations	(5,202)	(10,232)
Other expense, net	(628)	(1,253)
Loss before reorganization costs and gain from bankruptcy exit	(5,830)	(11,485)
Reorganization costs	(2,714)	(4,153)
Gain from bankruptcy exit	119,408	119,408
Net income	$ 110,864	$ 103,770

PACIFIC ETHANOL HOLDING CO. LLC AND SUBSIDIARIES
CONDENSED COMBINED STATEMENT OF CASH FLOWS
Six Months Ended June 30, 2010

Operating Activities:	
Net cash used in operating activities	$(6,808)
Investing Activities:	
Net cash impact of bankruptcy exit	$(1,301)
Additions to property and equipment	(310)
Net cash used in investing activities	$(1,611)
Financing Activities:	
Proceeds from borrowings	$5,173
Net cash provided by financing activities	$5,173
Net decrease in cash and cash equivalents	(3,246)
Cash and cash equivalents at beginning of period	3,246
Cash and cash equivalents at end of period	$---

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion and analysis should be read in conjunction with our consolidated financial statements and notes to consolidated financial statements included elsewhere in this report. This report and our consolidated financial statements and notes to consolidated financial statements contain forward-looking statements, which generally include the plans and objectives of management for future operations, including plans and objectives relating to our future economic performance and our current beliefs regarding revenues we might generate and profits we might earn if we are successful in implementing our business and growth strategies. The forward-looking statements and associated risks may include, relate to or be qualified by other important factors, including:

- fluctuations in the market price of ethanol and its co-products;
- the projected growth or contraction in the ethanol and co-product markets in which we operate;
- our strategies for expanding, maintaining or contracting our presence in these markets;
- our ability to successfully manage and operate third party ethanol production facilities;
- anticipated trends in our financial condition and results of operations; and
- our ability to distinguish ourselves from our current and future competitors.

You are cautioned not to place undue reliance on any forward-looking statements, which speak only as of the date of this report, or in the case of a document incorporated by reference, as of the date of that document. We do not undertake to update, revise or correct any forward-looking statements, except as required by law.

Any of the factors described immediately above, or referenced from time to time in our filings with the Securities and Exchange Commission or in the "Risk Factors" section in our Annual Report on Form 10-K for the year ended December 31, 2010 could cause our financial results, including our net income or loss or growth in net income or loss to differ materially from prior results, which in turn could, among other things, cause the price of our common stock to fluctuate substantially.

Overview

We are the leading marketer and producer of low carbon renewable fuels in the Western United States.

Since our inception in 2005, we have conducted ethanol marketing operations through our subsidiary, Kinergy Marketing, LLC, or Kinergy, through which we market and sell ethanol produced by third parties. In 2006, we began constructing the first of our four then wholly-owned ethanol production facilities, or Pacific Ethanol Plants, and were continuously engaged in plant construction until the fourth facility was completed in 2008. We funded, and until recently directly operated, the Pacific Ethanol Plants through a subsidiary holding company and four other indirect subsidiaries, or Plant Owners.

In late 2008 and early 2009, we idled production at three of the Pacific Ethanol Plants due to adverse market conditions and lack of adequate working capital. Adverse market conditions and our financial constraints continued, resulting in an inability to meet our debt service requirements, and in May 2009, the Plant Owners each filed voluntary petitions for relief under chapter 11 of Title 11 of the United States Code, or Bankruptcy Code, in the

United States Bankruptcy Court for the District of Delaware, or Bankruptcy Court.

On June 29, 2010, or the Effective Date, the Plant Owners declared effective their amended joint plan of reorganization, or the Plan, and emerged from bankruptcy. Under the Plan, on the Effective Date, all of the ownership interests in the Plant Owners were transferred to a newly-formed holding company, New PE Holdco, LLC, or New PE Holdco, wholly-owned as of that date by some of the prepetition lenders and new lenders of the Plant Owners. As a result, the Pacific Ethanol Plants are now wholly-owned by New PE Holdco.

On October 6, 2010, we raised $35.0 million through the issuance of $35.0 million in principal amount of senior convertible notes, or Initial Convertible Notes, and warrants to purchase an aggregate of 2,941,178 shares of our common stock, or Initial Warrants. See "—Liquidity and Capital Resources—Convertible Notes." On that same date we sold our 42% interest in Front Range Energy, LLC, or Front Range, for $18.5 million in cash, paid off our outstanding indebtedness to Lyles United, LLC and Lyles Mechanical Co., or collectively Lyles, in the aggregate amount of approximately $17.0 million and purchased a 20% ownership interest, which represents the single largest interest, in New PE Holdco for an aggregate purchase price of $23.3 million.

On January 7, 2011, we issued $35.0 million in principal amount of senior convertible notes, or January Convertible Notes, in exchange for the Initial Convertible Notes and issued warrants to purchase an aggregate of 2,941,178 shares of our common stock, or Warrants, in exchange for the Initial Warrants. See "—Liquidity and Capital Resources—Convertible Notes."

On June 8, 2011, we effected a one-for-seven reverse stock split. All share and per share information has been restated to retroactively show the effect of this stock split.

On June 30, 2011, we issued $23.75 million in principal amount of senior convertible notes, or June Convertible Notes, in exchange for the January Convertible Notes. On August 3, 2011, we issued $17.17 million in principal amount of senior convertible notes, or Convertible Notes, in exchange for the June Convertible Notes. See "—Liquidity and Capital Resources—Convertible Notes."

On June 30, 2011, we amended our asset management and other agreements with New PE Holdco and the Plant Owners to extend the term for one year and make other changes effective July 1, 2011, as further described below.

We currently manage the production of ethanol at the Pacific Ethanol Plants under the terms of an asset management agreement with the Plant Owners. We also market ethanol and its co-products, including wet distillers grain and syrup, or WDG, produced by the Pacific Ethanol Plants under the terms of separate marketing agreements with the Plant Owners whose facilities are operational. We also market ethanol and its co-products to other third parties, and provide transportation, storage and delivery of ethanol through third-party service providers in the Western United States, primarily in California, Nevada, Arizona, Oregon, Colorado, Idaho and Washington.

We have extensive customer relationships throughout the Western United States and extensive supplier relationships throughout the Western and Midwestern United States. Our customers are integrated oil companies and gasoline marketers who blend ethanol into gasoline. We supply ethanol to our customers either from the Pacific Ethanol Plants located within the regions we serve, or with ethanol procured in bulk from other producers. In some cases, we have marketing agreements with ethanol producers to market all of the output of their facilities. Additionally, we have customers who purchase our co-products for animal feed and other uses.

The Pacific Ethanol Plants produce ethanol and its co-products and are comprised of the four facilities described immediately below, three of which are currently operational. If market conditions continue to improve, we may resume operations at the Madera, California facility, subject to the approval of New PE Holdco.

Facility Name	Facility Location	Estimated Annual Capacity (gallons)	Current Operating Status
Magic Valley	Burley, ID	60,000,000	Operating
Columbia	Boardman, OR	40,000,000	Operating
Stockton	Stockton, CA	60,000,000	Operating
Madera	Madera, CA	40,000,000	Idled

Under our asset management and other agreements with New PE Holdco and the Plant Owners, we manage the production and operations of the Pacific Ethanol Plants, market their ethanol and WDG and earn fees as follows. We amended the agreements and the related fee structure on June 30, 2011.

Fees effective through June 30, 2011:

- ethanol marketing fees of approximately 1% of the net sales price;
- corn procurement and handling fees of approximately $2.00 per ton;
- WDG fees of approximately the greater of 5% of the third-party purchase price or $2.00 per ton; and
- asset management fees of $75,000 per month for each operating facility and $40,000 per month for each idled facility.

Fees effective July 1, 2011:

- ethanol marketing fees of approximately 1% of the net sales price, but not less than $0.15 per gallon and not more than $0.225 per gallon;
- corn procurement and handling fees of $0.045 per bushel;
- WDG fees of 5% of the third-party purchase price, but not less than $2.00 per ton and not more than $3.50 per ton; and
- asset management fees of $75,000 per month for each operating facility and $40,000 per month for each idled facility.

We intend to maintain our position as the leading marketer and producer of low-carbon renewable fuels in the Western United States, in part by expanding our relationships with customers and third-party ethanol producers to market higher volumes of ethanol and by expanding the market for ethanol by continuing to work with state governments to encourage the adoption of policies and standards that promote ethanol as a fuel additive and transportation fuel. Further, we may seek to provide management services for other third-party ethanol production facilities in the Western United States.

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Critical Accounting Policies

The preparation of our financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America, requires us to make judgments and estimates that may have a significant impact upon the portrayal of our financial condition and results of operations. We believe that of our significant accounting policies, the following require estimates and assumptions that require complex, subjective judgments by management that can materially impact the portrayal of our financial condition and results of operations: revenue recognition; consolidation of variable interest entities; convertible notes and warrants carried at fair value; impairment of long-lived and intangible assets; and allowance for doubtful accounts. These significant accounting principles are more fully described in "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies" in our Annual Report on Form 10-K for the year ended December 31, 2010.

Results of Operations

The following selected financial information should be read in conjunction with our consolidated financial statements and notes to our consolidated financial statements included elsewhere in this report, and the other sections of "Management's Discussion and Analysis of Financial Condition and Results of Operations" contained in this report.

Certain performance metrics that we believe are important indicators of our results of operations include:

	Three Months Ended June 30,			Six Months Ended June 30,		
	2011	2010	Variance	2011	2010	Variance
Production gallons sold (in millions)	38.1	23.5	62.1%	75.0	43.2	73.6%
Third party gallons sold (in millions)	62.5	41.9	49.2%	110.1	80.9	36.1%
Total gallons sold (in millions)	100.6	65.4	53.8%	185.1	124.1	49.2%
Average sales price per gallon	$ 2.79	$ 1.67	67.1%	$ 2.67	$ 1.74	53.4%
Corn cost per bushel – CBOT equivalent (1)	$ 7.30	$ 3.55	105.6%	$ 6.96	$ 3.62	92.3%
Co-product revenues as % of delivered cost of corn	22.3%	22.7%	(1.8%)	22.5%	21.9%	2.7%
Average CBOT ethanol price per gallon	$ 2.64	$ 1.58	67.1%	$ 2.53	$ 1.65	53.3%
Average CBOT corn price per bushel	$ 7.31	$ 3.55	105.9%	$ 7.01	$ 3.62	93.6%

(1) We exclude transportation—or "basis"—costs in our corn costs to calculate a Chicago Board of Trade, or CBOT, equivalent price to compare our corn costs to average CBOT corn prices.

Net Sales, Cost of Goods Sold and Gross Profit (Loss)

The following table presents our net sales, cost of goods sold and gross profit (loss) in dollars and gross profit (loss) as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Net sales	$ 214,593	$ 76,758	$ 137,835	179.6%	$ 387,741	$ 148,048	$ 239,693	161.9%
Cost of goods sold	213,310	79,487	133,823	168.4%	383,894	153,825	230,069	149.6%
Gross profit (loss)	$ 1,283	$ (2,729)	$ 4,012	147.0%	$ 3,847	$ (5,777)	$ 9,624	166.6%
Percentage of net sales	0.6%	(3.6%)			1.0%	(3.9%)		

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Net Sales

The increase in our net sales for the three months ended June 30, 2011 as compared to the same period in 2010 was due to an increase in total gallons sold and an increase in our average sales price per gallon.

Total volume of ethanol production gallons sold increased by 14.6 million gallons, or 62%, to 38.1 million gallons for the three months ended June 31, 2011 as compared to 23.5 million gallons for the same period in 2010. The increase in production gallons sold is primarily due to the Stockton facility operating during the three months ended June 30, 2011, whereas it was not operating during the same period in 2010. Total volume of third party gallons sold increased by 20.6 million gallons, or 49%, to 62.5 million gallons for the three months ended June 30, 2011 as compared to 41.9 million gallons for the same period in 2010. The increase in third party sales volume is primarily due to additional gallons sold through third-party ethanol marketing arrangements, including from the Keyes, California production facility which opened in April 2011. We market all of that facility's ethanol.

Our average sales price per gallon increased 67% to $2.79 for the three months ended June 30, 2011 from an average sales price per gallon of $1.67 for the same period in 2010, which was in line with the increase in the average CBOT ethanol price per gallon for the comparable periods.

The increase in our net sales for the six months ended June 30, 2011 as compared to the same period in 2010 was also due to an increase in total gallons sold and an increase in our average sales price per gallon.

Total volume of ethanol production gallons sold increased by 31.8 million gallons, or 74%, to 75.0 million gallons for the six months ended June 30, 2011 as compared to 43.2 million gallons for the same period in 2010. The increase in production gallons sold is also primarily due to the Stockton facility operating during the six months ended June 30, 2011, whereas it was not operating during the same period in 2010. Total volume of third party gallons sold increased by 29.2 million gallons, or 36%, to 110.1 million gallons for the six months ended June 30, 2011 as compared to 80.9 million gallons for the same period in 2010. The increase in third party sales volume is primarily due to additional gallons sold through third-party ethanol marketing arrangements, including from the Keyes, California facility.

Our average sales price per gallon increased 53% to $2.67 for the six months ended June 30, 2011 from an average sales price per gallon of $1.74 for the same period in 2010, consistent with the increase in the average CBOT ethanol price per gallon for the comparable periods.

Cost of Goods Sold and Gross Profit (Loss)

Our gross margin increased to 0.6% for the three months ended June 30, 2011 from negative 3.6% for the same period in 2010 primarily due to increased production volumes. Our gross margin increased to 1.0% for the six months ended June 30, 2011 from negative 3.9% for the same period in 2010 primarily due to increased production volumes. Further, for the six months ended June 30, 2011, we were able to offset approximately $1.5 million of our production costs due to elevated corn prices with proceeds from the California Ethanol Producer Incentive Program, which were recorded as reductions to cost of goods sold.

Selling, General and Administrative Expenses

The following table presents our selling, general and administrative expenses, or SG&A, in dollars and as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Selling, general and administrative expenses	$ 4,059	$ 3,177	$ 882	27.8%	$ 8,247	$ 6,333	$ 1,914	30.2%
Percentage of net sales	1.9%	4.1%			2.1%	4.3%		

Our SG&A increased in absolute dollars, but decreased as a percentage of net sales for the three and six months ended June 30, 2011 as compared to the same periods in 2010.

SG&A increased $0.9 million to $4.1 million for the three months ended June 30, 2011 as compared to $3.2 million for the same period in 2010. The increase in the dollar amount of SG&A is primarily due to the following factors:

- noncash compensation expenses increased by $0.3 million due to increased grants of restricted stock awards to our employees and members of our board of directors; during the prior year period, we made fewer grants as we continued to execute on our restructuring plans;
- bad debt expense increased by $0.2 million due to a recovery in the prior year period; and
- amortization of intangibles increased by $0.1 million due to amortization of the Pacific Ethanol tradename by New PE Holdco.

SG&A increased $1.9 million to $8.2 million for the six months ended June 30, 2011 as compared to $6.3 million for the same period in 2010. The increase in the dollar amount of SG&A is primarily due to the following factors:

- noncash compensation expenses increased by $0.6 million due to increased grants of restricted stock awards to our employees and members of our board of directors; during the prior year period, we made fewer grants as we continued to execute on our restructuring plans;
- professional fees increased by $0.2 million due to organizational costs incurred by New PE Holdco; and
- amortization of intangibles increased by $0.2 million due to amortization of the Pacific Ethanol tradename by New PE Holdco.

Fair Value Adjustments on Convertible Debt and Warrants

The following table presents our fair value adjustments on convertible debt and warrants in dollars and as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Fair value adjustments on convertible debt and warrants	$ 1,929	$ —	$ 1,929	NA	$ 2,855	$ —	$ 2,855	NA
Percentage of net sales	0.9%	—%			0.7%	—%		

We issued convertible debt and warrants in the fourth quarter of 2010 for $35.0 million in cash. The convertible debt and warrants are recorded at fair value. We recorded income of $1.9 million and $2.9 million related to the subsequent fair value adjustments of these instruments for the three and six months ended June 30, 2011, respectively.

Loss on Extinguishments of Debt

The following table presents our loss on extinguishments of debt in dollars and as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Loss on extinguishments of debt	$ —	$ 544	$ (544)	(100%)	$ —	$ 2,159	$ (2,159)	(100%)
Percentage of net sales	—%	0.7%			—%	1.5%		

We were party to certain agreements designed to satisfy our outstanding debt to Lyles. Under these agreements, we issued shares to a third party which acquired outstanding debt owed to Lyles in successive transactions. Under these transactions, we issued an aggregate of 16.2 million shares and 24.1 million shares in the three and six months ended June 30, 2010, respectively, resulting in aggregate losses of $0.5 million and $2.2 million for the three and six months ended June 30, 2010, respectively. We determined fair value based on the closing price of our shares at the end of an applicable period, which was the date the net shares to be issued were determinable.

Interest Expense, net

The following table presents our interest expense, net in dollars and our interest expense, net as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent

Interest expense, net	$ 3,628	$ 1,271	$ 2,357	185.4%	$ 7,266	$ 2,863	$ 4,403	153.8%
Percentage of net sales	1.7%	1.7%			1.9%	1.9%		

Interest expense, net increased by $2.3 million to $3.6 million for the three months ended June 30, 2011 from $1.3 million for the same period in 2010. Interest expense, net increased by $4.4 million to $7.3 million for the six months ended June 30, 2011 from $2.9 million for the same period in 2010. The increase in interest expense, net for the periods is primarily due to increased average debt balances, which includes our senior convertible notes and New PE Holdco’s credit facility, neither of which were outstanding for the comparable period in 2010.

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Other Expense, net

The following table presents our other expense, net in dollars and our other expense, net as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Other expense, net	$ 200	$ 421	$ (221)	(52.5%)	$ 543	$ 466	$ 77	16.5%
Percentage of net sales	0.1%	0.5%			0.1%	0.3%		

Other expense decreased by $0.2 million to $0.2 million for the three months ended June 30, 2011 from $0.4 million for the same period in 2010. The decrease in other expense is primarily due to the reduction of equity losses from our investment in Front Range Energy, in which we owned a 42% interest in the 2010 periods, which was partially offset by increases associated with bank fees.

Reorganization Costs and Gain from Bankruptcy Exit

The following table presents our reorganization costs and gain from bankruptcy exit in dollars and as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Reorganization costs	$ —	$ 2,714	$ (2,714)	(100.0%)	$ —	$ 4,153	$ (4,153)	(100.0%)
Percentage of net sales	—%	3.5%			—%	2.8%		
Gain from bankruptcy exit	$ —	$ 119,408	$ (119,408)	(100.0%)	$ —	$ 119,408	$ (119,408)	(100.0%)
Percentage of net sales	—%	155.6%			—%	80.7%		

In accordance with the Financial Accounting Standards Board's Accounting Standards Codification 852, Reorganizations, revenues, expenses, realized gains and losses, and provisions for losses that can be directly associated with the reorganization and restructuring of a business must be reported separately as reorganization items in the statements of operations. Professional fees directly related to the reorganization include fees associated with advisors to the Plant Owners, unsecured creditors, secured creditors and administrative costs in complying with reporting rules under the Bankruptcy Code. Reorganization costs consisted of the following (in thousands):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Professional fees	$—	$2,654	$—	$4,036
Trustee fees	—	60	—	117

Total	$—	$2,714	$—	$4,153

On the Effective Date, we no longer owned the Plant Owners. As a result, we removed the net liabilities from our consolidated financial statements, resulting in a net gain from bankruptcy exit of $119.4 million.

Net Loss Attributed to Noncontrolling Interest in Variable Interest Entity

The following table presents the proportionate share of the net loss attributed to noncontrolling interest in variable interest entity, and net loss attributed to noncontrolling interest in variable interest entity as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Net loss attributed to noncontrolling interest in variable interest entity	$ 5,425	$ —	$ 5,425	NA	$ 10,122	$ —	$ 10,122	NA
Percentage of net sales	2.5%	—%			2.6%	—%		

Net loss attributed to noncontrolling interest in variable interest entity relates to our consolidated treatment of New PE Holdco, a variable interest entity, beginning October 6, 2010. For the three and six months ended June 30, 2011, we consolidated the entire income statement of New PE Holdco. However, because we owned only 20% of New PE Holdco, we reduced our net loss for the noncontrolling interest, which was the 80% ownership interest that we do not own.

Net Income Attributed to Pacific Ethanol

The following table presents our net income attributed to Pacific Ethanol, Inc. in dollars and our net income attributed to Pacific Ethanol, Inc. as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Net income attributed to Pacific Ethanol	$ 750	$ 108,552	$ (107,802)	(99.3%)	$ 768	$ 97,657	$ (96,889)	(99.2%)
Percentage of net sales	0.3%	141.4%			0.2%	66.0%		

Net income attributed to Pacific Ethanol, Inc. decreased during the three and six months ended June 30, 2011 as compared to the same period in 2010, primarily due to a gain from bankruptcy exit of $119.4 million.

Preferred Stock Dividends and Income Available to Common Stockholders

The following table presents the preferred stock dividends in dollars for our Series B Cumulative Convertible Preferred Stock, or Series B Preferred Stock, these preferred stock dividends as a percentage of net sales, and our income available to common stockholders in dollars and our loss available to common stockholders as a percentage of net sales (in thousands, except percentages):

	Three Months Ended June 30,		Variance in		Six Months Ended June 30,		Variance in	
	2011	2010	Dollars	Percent	2011	2010	Dollars	Percent
Preferred stock dividends	$ 315	$ 798	$ (483)	(60.5%)	$ 627	$ 1,588	$ (961)	(60.5%)
Percentage of net sales	0.1%	1.0%			0.2%	1.1%		
Income available to common stockholders	$ 435	$ 107,754	$ (107,319)	(99.6%)	$ 141	$ 96,069	$ (95,928)	(99.9%)
Percentage of net sales	0.2%	140.4%			0.0%	64.9%		

Shares of our Series B Preferred Stock are entitled to quarterly cumulative dividends payable in arrears in an amount equal to 7% per annum, of the purchase price per share of the Series B Preferred Stock. We have accrued dividends on our Series B Preferred Stock in the aggregate amount of $0.3 million and $0.8 million, for the three months ended June 30, 2011 and 2010, and $0.6 million and $1.6 million, for the six months ended June 30, 2011 and 2010, respectively, resulting in total accrued and unpaid dividends of $6.7 million as of June 30, 2011.

Liquidity and Capital Resources

During the three months ended June 30, 2011, we funded our operations primarily from cash provided by operations, borrowings under our credit facilities and the remaining proceeds from the issuance and sale of our senior convertible notes and Warrants. We had working capital of $34.1 million and $9.5 million as of June 30, 2011 and December 31, 2010, respectively. We had cash and cash equivalents of $9.8 million and $8.7 million as of June 30, 2011 and December 31, 2010, respectively.

Our current available capital resources consist of cash on hand and amounts available for borrowing under Kinergy's credit facility. In addition, New PE Holdco has a credit facility for use in the operations of the Pacific Ethanol Plants. We expect that our future available capital resources will consist primarily of our remaining cash balances, amounts available for borrowing, if any, under Kinergy's credit facility, cash generated from Kinergy's ethanol marketing business, fees paid under our asset management agreement relating to our operation of the Pacific Ethanol Plants, distributions, if any, in respect of our ownership interest in New PE Holdco, and the remaining proceeds of any future debt and/or equity financings.

We believe that current and future available capital resources, revenues generated from operations, and other existing sources of liquidity, including our credit facilities, will be adequate to meet our anticipated working capital and capital expenditure requirements for at least the next twelve months. If, however, we are unable to service the principal and/or interest payments under the Convertible Notes through the issuance of shares of our common stock, if our capital requirements or cash flow vary materially from our current projections, if unforeseen circumstances occur, or if we require a significant amount of cash to fund future acquisitions, we may require additional financing. Our failure to raise capital, if needed, could restrict our growth, or hinder our ability to compete.

Quantitative Quarter-End Liquidity Status

We believe that the following amounts provide insight into our liquidity and capital resources. The following selected financial information should be read in conjunction with our consolidated financial statements and notes to consolidated financial statements included elsewhere in this report, and the other sections of "Management's Discussion and Analysis of Financial Condition and Results of Operations" contained in this report (dollars in thousands):

	June 30, 2011		December 31, 2010		Variance	
Current assets	$	73,162	$	57,324	27.6	%
Total assets of variable interest entity	$	175,528	$	183,652	(4.4	)%
Current liabilities	$	39,020	$	47,831	(18.4	)%
Property and equipment, net	$	164,483	$	168,976	(2.7	)%
Notes payable, current portion	$	26,384	$	38,108	(30.8	)%
Notes payable, noncurrent portion	$	100,190	$	84,981	17.9	%
Total liabilities of variable interest entity	$	85,610	$	74,939	14.2	%
Working capital	$	34,142	$	9,493	259.7	%
Working capital ratio		1.87		1.20	55.8	%

Change in Working Capital and Cash Flows

Working capital increased to $34.1 million at June 30, 2011 from $9.5 million at December 31, 2010 as a result of increases in current assets of $15.8 million and decreases in current liabilities of $8.8 million.

Current assets increased primarily due to an increase in accounts receivable of $8.4 million and prepaid inventory of $3.4 million, as a result of higher sales volumes.

Current liabilities decreased primarily due to decreases in the current portion of our long-term debt, as a result of the issuance of shares of our common stock to pay $14.7 million in principal plus interest on our senior convertible notes, which was partially offset by an increase in accounts payable and accrued liabilities of $2.9 million related to an increase in commodity prices and sales volumes.

Cash used in operating activities of $14.0 million resulted primarily from a consolidated net loss of $9.4 million, an increase in accounts receivable of $8.3 million, an increase in inventories and prepaid inventories of $7.0 million and a gain on fair value adjustments of $2.9 million. These increases were partially offset by depreciation expense of $6.3 million, an increase in accounts payable and accrued expenses of $4.8 million and noncash compensation of $1.5 million.

Cash used in investing activities of $1.4 million resulted from additions to property and equipment.

Cash provided by financing activities of $16.5 million resulted from proceeds from borrowings under our credit facilities.

Convertible Notes

We have raised $35.0 million through the issuance and sale of $35.0 million in principal amount of senior convertible notes and warrants to purchase 2.9 million shares of our common stock.

The Convertible Notes mature on May 6, 2012, subject to the right of the lenders to extend the date (i) if an event of default under the Convertible Notes has occurred and is continuing or any event shall have occurred and be continuing that with the passage of time and the failure to cure would result in an event of default under the Convertible Notes, and (ii) for a period of 20 business days after the consummation of specific types of transactions involving a change of control. The Convertible Notes bear interest at the rate of 8% per annum, which is compounded monthly. The interest rate will increase to 15% per annum upon the occurrence of an event of default.

Interest on the Convertible Notes is payable in arrears on specified installment dates. If a holder elects to convert or redeem all or any portion of a Convertible Note prior to the maturity date, all interest that would have accrued on the amount being converted or redeemed through the maturity date will also be payable. If we elect to redeem all or any portion of a Convertible Note prior to the maturity date, all interest that would have accrued through the maturity date on the amount redeemed will also be payable.

We are obligated to make amortization payments with respect to the principal amount of each Convertible Note on the first trading day of each calendar month after August 1, 2011 until the Maturity Date, collectively with the Maturity Date, the Installment Dates.

On each Installment Date, occurring after August 1, 2011, we shall pay on each Convertible Note an amount equal to: (i) with respect to any Installment Date other than the Maturity Date, the lesser of (A) the product of (I) the quotient of (x) $21 million divided by (y) 9, multiplied by (II) the fraction equal to (m) the principal amount of the Initial Note on October 6, 2010 divided by (n) $35 million and (B) the principal amount under the Convertible Note as of such Installment Date, and (ii) with respect to the Maturity Date, the principal amount under the Convertible Note, together with, in each case of clauses (i) and (ii), the sum of any accrued and unpaid Interest as of such Installment Date under the Convertible Note and accrued and unpaid late charges, if any, under the Convertible Note as of such Installment Date, or the Installment Amount. We may elect to pay the Installment Amount and applicable interest in cash or shares of our common stock, at our election, subject to the satisfaction of certain conditions.

If we elect to make all or part of an amortization payment in shares of our common stock, we are required to deliver to the holders of the Convertible Notes the amount of shares of our common stock equal to the portion of the amount being paid in shares of our common stock divided by the lesser of the then existing Conversion Price and 85% of the average of the volume weighted average prices of the 5 lowest trading days during the 20 consecutive trading day period ending on the trading day immediately prior to the applicable Installment Date.

All amounts due under the Convertible Notes are convertible at any time, in whole or in part, at the option of the holders into shares of our common stock at a specified conversion price, or Conversion Price. The Convertible Notes were initially convertible into shares of our common stock at the initial Conversion Price of $5.95 per share, or Fixed Conversion Price. The Conversion Price is not to exceed $5.95 and, unless we obtain a waiver, we cannot make monthly amortization and interest payments in shares of common stock if the Conversion Price is less than $0.60.

The Convertible Notes are now convertible by the holders into shares of our common stock at a Conversion Price that is determined as follows:

- If we have elected to make an amortization payment in shares of common stock and the date of conversion occurs during the 15 calendar day period following (and including) the applicable Installment Date, or Initial Period, the Conversion Price will equal the lesser of (i) the Fixed Conversion Price, and (ii) the average of the volume weighted average prices of our common stock for each of the five lowest trading days during the 20 trading day period immediately prior to the Initial Period.

- If we have elected to make an amortization payment in shares of common stock and the date of conversion occurs during the period beginning on the 16th calendar day after the applicable Installment Date and ending on the day immediately prior to the next Installment Date or the maturity date, the Conversion Price will equal the lesser of (i) the Fixed Conversion Price, and (ii) the closing bid price of our common stock on the trading date immediately before the date of conversion.

- The holder may, up to three times, elect a 12% discount to the closing bid price of our common stock on the date immediately before the conversion.

- Four of the seven holders may, up to fifteen times, elect a 15% discount to the closing bid price of our common stock on the date immediately before the conversion while the other three holders may, up to fifteen times, elect a 10% discount to the closing bid price of our common stock on the date immediately before the conversion.

In addition, if an event of default has occurred and is continuing, the Conversion Price will be equal to the lesser of (i) the Fixed Conversion Price, and (ii) the closing bid price of our common stock on the trading date immediately before the date of conversion.

The Fixed Conversion Price is subject to "full ratchet" anti-dilution adjustment where if we were to issue or are deemed to have issued specified securities at a price lower than the then applicable Fixed Conversion Price, the Fixed Conversion Price will immediately decline to equal the price at which we issued or are deemed to have issued the securities. In addition, if we sell or issue any securities with "floating" conversion prices based on the market price of our common stock, the holder of a Convertible Note will have the right to substitute that "floating" conversion price for the Fixed Conversion Price upon conversion of all or part of the Convertible Note.

We have agreed to pay "buy-in" damages of the converting holder if we fail to timely deliver common stock upon conversion of the Convertible Notes.

We issued 1.1 million shares of our common stock to satisfy the March 7, 2011 Installment Date payment of $3.5 million in principal and $1.3 million in accrued interest. We issued 1.4 million shares of our common stock to satisfy the May 2, 2011 Installment Date payment of $3.5 million in principal and $0.4 million in accrued interest. We issued 1.6 million shares of our common stock to satisfy the June 1, 2011 Installment Date payment of $3.4 million in principal and $0.2 million in accrued interest.

Through June 30, 2011, we issued an aggregate of 0.4 million shares of our common stock to satisfy $0.9 million in principal and related interest in respect of additional note conversions by holders of the Convertible Notes.

We also elected to issue shares of our common stock to satisfy the July 1, 2011 Installment Date payment of principal and accrued interest. In accordance with the Convertible Notes, on June 6, 2011, we issued 1.6 million shares of our common stock as a pre-installment payment of $3.5 million in principal and $0.2 million in accrued interest and on July 1, 2011, issued additional 1.7 million "true-up" shares of our common stock.

On August 3, 2011, we notified the holders that we would pay the Installment Amount due on the September 1, 2011 Installment Date in cash.

Since the July 1 Installment Date through August 9, 2011, we have issued an aggregate of 4.5 million shares of our common stock to satisfy $3.6 million in principal and $0.2 million in interest in respect of additional note conversions by holders of the Convertible Notes.

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New PE Holdco Term Debt and Working Capital Line of Credit

On the Effective Date, approximately $294.4 million in prepetition and post petition secured indebtedness of the Plant Owners was restructured under a Credit Agreement entered into on June 25, 2010 among the Plant Owners, as borrowers, and West LB, AG, New York Branch, and other lenders. Under the Plan, the Plant Owners' existing prepetition and post petition secured indebtedness of approximately $294.4 million was restructured to consist of approximately $50.0 million in three-year term loans and a new three-year revolving credit facility of up to $35.0 million to fund working capital requirements.

Notes Payable to Related Parties

On March 31, 2009, our Chairman of the Board and our Chief Executive Officer provided funds in the aggregate amount of $2.0 million for general working capital purposes, in exchange for two unsecured promissory notes payable by us. Interest on the unpaid principal amounts accrues at a rate per annum of 8.00%. All principal and accrued and unpaid interest on the promissory notes was due and payable in March 2010. The maturity date of these notes was initially extended to January 5, 2011. On October 29, 2010, we repaid $0.8 million of principal on these notes and all accrued and unpaid interest. On November 5, 2010, we further extended the maturity date of these notes to March 31, 2012.

Kinergy Operating Line of Credit

Kinergy maintains a credit facility in the aggregate amount of up to $30.0 million. The credit facility expires on December 31, 2013. In May 2011, Kinergy and its lender amended and increased the credit facility to up to $30.0 million, with an optional accordion feature for an additional $5.0 million. Interest accrues under the credit facility at a rate equal to (i) the three-month London Interbank Offered Rate (LIBOR), plus (ii) a specified applicable margin ranging between 3.50% and 4.50%. The credit facility's monthly unused line fee is 0.50% of the amount by which the maximum credit under the facility exceeds the average daily principal balance. Kinergy is also required to pay customary fees and expenses associated with the credit facility and issuances of letters of credit. In addition, Kinergy is responsible for a $3,000 monthly servicing fee. Payments that may be made by Kinergy to Pacific Ethanol as reimbursement for management and other services provided by Pacific Ethanol to Kinergy are limited to $750,000 per fiscal quarter in 2011, $800,000 per fiscal quarter in 2012, and $850,000 per fiscal quarter in 2013. Kinergy is required to meet specified EBITDA and fixed coverage ratio financial covenants under the credit facility and is prohibited from incurring any additional indebtedness (other than specific intercompany indebtedness) or making any capital expenditures in excess of $100,000 absent the lender's prior consent. Kinergy's obligations under the credit facility are secured by a first-priority security interest in all of its assets in favor of the lender. We have guaranteed all of Kinergy's obligations under the credit facility.

Effects of Inflation

The impact of inflation was not significant to our financial condition or results of operations for the three and six months ended June 30, 2011 and 2010.

Impact of New Accounting Pronouncements

None.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not applicable.

ITEM 4. CONTROLS AND PROCEDURES.

Evaluation of Disclosure Controls and Procedures

We conducted an evaluation under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures also include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate, to allow timely decisions regarding required disclosure. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded as of June 30, 2011 that our disclosure controls and procedures were effective at a reasonable assurance level.

Changes in Internal Control over Financial Reporting

There were no changes during the most recently completed fiscal quarter that have materially affected or are reasonably likely to materially affect, our internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act.

Inherent Limitations on the Effectiveness of Controls

Management does not expect that our disclosure controls and procedures or our internal control over financial reporting will prevent or detect all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control systems are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in a cost-effective control system, no evaluation of internal control over financial reporting can provide absolute assurance that misstatements due to error or fraud will not occur or that all control issues and instances of fraud, if any, have been or will be detected.

These inherent limitations include the realities that judgments in decision-making can be faulty and that breakdowns can occur because of a simple error or mistake. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part on certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Projections of any evaluation of controls effectiveness to future periods are subject to risks. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures.

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

We are subject to legal proceedings, claims and litigation arising in the ordinary course of business. While the amounts claimed may be substantial, the ultimate liability cannot presently be determined because of considerable uncertainties that exist. Therefore, it is possible that the outcome of those legal proceedings, claims and litigation could adversely affect our quarterly or annual operating results or cash flows when resolved in a future period. However, based on facts currently available, management believes such matters will not adversely affect our financial position, results of operations or cash flows.

ITEM 1A. RISK FACTORS.

In addition to the other information set forth in this report, you should carefully consider the risk factors discussed under “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2010, as updated below, which could materially affect our business, financial condition and results of operations. The risks described in our Annual Report on Form 10-K for the year ended December 31, 2010, as updated below, are not the only risks we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and results of operations.

The United States ethanol industry is highly dependent upon myriad federal and state legislation and regulation . . .

The risk factor in our Annual Report on Form 10-K for the year ended December 31, 2010 entitled, “The United States ethanol industry is highly dependent upon myriad federal and state legislation and regulation . . .” is amended and restated in its entirety to read as follows:

The United States ethanol industry is highly dependent upon myriad federal and state legislation and regulation and any changes in legislation or regulation could have a material adverse effect on our results of operations and financial condition.

Various studies have criticized the efficiency of ethanol in general, and corn-based ethanol in particular, which could lead to the reduction or repeal of incentives and tariffs that promote the use and domestic production of ethanol or otherwise negatively impact public perception and acceptance of ethanol as an alternative fuel.

Although many trade groups, academics and governmental agencies have supported ethanol as a fuel additive that promotes a cleaner environment, others have criticized ethanol production as consuming considerably more energy and emitting more greenhouse gases than other biofuels and as potentially depleting water resources. Other studies have suggested that ethanol negatively impacts consumers by causing higher prices for dairy, meat and other foodstuffs from livestock that consume corn. If these views gain acceptance, support for existing measures promoting the use and domestic production of corn-based ethanol could decline, leading to a reduction or repeal of these measures. These views could also negatively impact public perception of the ethanol industry and acceptance of ethanol as a component for blending in transportation fuel.

Waivers or repeal of the national RFS's minimum levels of renewable fuels included in gasoline could have a material adverse effect on our results of operations.

Shortly after passage of the Energy Independence and Security Act of 2007, which increased the minimum mandated required usage of ethanol, a Congressional sub-committee held hearings on the potential impact of the national RFS on commodity prices. While no action was taken by the sub-committee towards repeal of the national RFS, any attempt by Congress to re-visit, repeal or grant waivers of the national RFS could adversely affect demand for ethanol and could have a material adverse effect on our results of operations and financial condition.

We have received a delisting notice from The NASDAQ Stock Market. . . .

The risk factor in our Annual Report on Form 10-K for the year ended December 31, 2010 entitled, "We have received a delisting notice from The NASDAQ Stock Market. . . ." is amended and restated in its entirety to read as follows:

Our common stock may be involuntarily delisted from trading on NASDAQ if we fail to maintain a minimum closing bid price of $1.00 per share for any consecutive 30 trading day period. A notification of delisting or a delisting of our common stock would reduce the liquidity of our common stock and inhibit or preclude our ability to raise additional financing and may also materially and adversely impact our credit terms with our vendors.

NASDAQ's quantitative listing standards require, among other things, that listed companies maintain a minimum closing bid price of $1.00 per share. If we fail to satisfy this threshold for any consecutive 30 trading day period, our common stock may be involuntarily delisted from trading on NASDAQ once the applicable grace period expires. Our stock price has recently declined below $1.00 per share. Given the increased market volatility and the downward trend in our stock price, the closing bid price of our common stock could remain below $1.00 per share for a consecutive 30 trading day period. A notification of delisting or delisting of our common stock would reduce the liquidity of our common stock and inhibit or preclude our ability to raise additional financing and may also materially and adversely impact our credit terms with our vendors.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

Unregistered Sales of Equity Securities

We issued 1,396,000 shares of our common stock to satisfy the May 2, 2011 Installment Date payment of $3.5 million in principal and approximately $0.4 million in accrued interest on our Convertible Notes. We issued 1,563,457 shares of our common stock to satisfy the June 1, 2011 Installment Date payment of $3.4 million in principal and approximately $0.2 million in accrued interest on our Convertible Notes. We also issued shares of our common stock to satisfy the July 1, 2011 Installment Date payment of principal and accrued interest. In accordance with the Convertible Notes, we issued 1,617,381 shares of our common stock as a pre-installment payment of $3.5 million in principal and approximately $0.2 million in accrued interest on our Convertible Notes and issued additional 1,695,533 "true-up" shares of our common stock on July 1, 2011. In addition, during the three months ended June 30, 2011, we issued 428,123 shares in connection with voluntary conversions by the holders of approximately $0.9 million in principal and $0.1 million in accrued interest.

Exemption from the registration provisions of the Securities Act of 1933 for the transactions described above is claimed under Section 4(2) of the Securities Act of 1933, among others, on the basis that such transactions did not involve any public offering and the purchasers were sophisticated or accredited with access to the kind of information registration would provide.

Dividends

For each of the three months ended June 30, 2011 and 2010, we accrued, but did not pay, an aggregate of $0.3 million and $0.6 million, and for each of the six months ended June 30, 2011, and 2010, we accrued but did not pay, an aggregate of $0.8 million and $1.6 million, respectively, in dividends on our Series B Preferred Stock. The holders of our outstanding Series B Preferred Stock are entitled to dividends of 7% per annum, payable quarterly, none of which have been paid for the years ended December 31, 2010 and 2009, for the three and six months ended June 30, 2011 or thereafter through the filing of this report. Accumulated and unpaid dividends in respect of our Series B Preferred Stock must be paid prior to the payment of any dividends in respect of our common stock.

We have never declared or paid cash dividends on our common stock and do not currently intend to pay cash dividends on our common stock in the foreseeable future. We currently anticipate that we will retain any earnings for use in the continued development of our business.

ITEMDEFAULTS UPON SENIOR SECURITIES.
3.

We accrued for dividend payments on our Series B Preferred Stock in the amount of $6.7 million as of June 30, 2011. We have not yet paid these dividends and we are therefore in breach of our obligations in respect of our Series B Preferred Stock.

ITEM(REMOVED AND RESERVED).
4.

Not applicable.

ITEMOTHER INFORMATION.
5.

None.

ITEM 6. EXHIBITS.

Exhibit Number	Description
3.1	Certificate of Amendment to the Certificate of Incorporation of Pacific Ethanol, Inc. (1)
10.1	Amendment No. 6 to Loan and Security Agreement dated April 11, 2011 by and among Kinergy Marketing LLC, Pacific Ethanol, Inc. and Wells Fargo Capital Finance, LLC, successor by merger to Wachovia Capital Finance Corporation (Western) (2)
10.2	Amendment No. 7 to Loan and Security Agreement dated May 12, 2011 by and among Kinergy Marketing LLC, Pacific Ethanol, Inc. and Wells Fargo Capital Finance, LLC, successor by merger to Wachovia Capital Finance Corporation (Western) (2)
10.3	Amendment No. 8 to Loan and Security Agreement dated June 10, 2011 by and among Kinergy Marketing LLC, Pacific Ethanol, Inc. and Wells Fargo Capital Finance, LLC, successor by merger to Wachovia Capital Finance Corporation (Western) (2)
10.4	Form of Second Amendment and Exchange Agreements dated effective June 30, 2011 between Pacific Ethanol, Inc. and each Investor (3)
10.5	Form of Senior Convertible Note issued to each Investor on June 30, 2011 (3)
10.6	Amended and Restated Asset Management Agreement (4)
10.7	Form of Amended and Restated Ethanol Marketing Agreement (4)
10.8	Form of Amended and Restated Corn Procurement and Handling Agreement (4)
10.9	Form of Amended and Restated Distillers Grains Marketing Agreement (4)
31.1	Certifications Required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (*)
31.2	Certifications Required by Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (*)
32.1	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (*)
101.INS	XBRL Instance Document (5)
101.SCH	XBRL Taxonomy Extension Schema (5)
101.CAL	XBRL Taxonomy Extension Calculation Linkbase (5)
101.DEF	XBRL Taxonomy Extension Definition Linkbase (5)
101.LAB	XBRL Taxonomy Extension Label Linkbase (5)
101.PRE	XBRL Taxonomy Extension Presentation Linkbase (5)

(*) Filed herewith.

(1) Filed as an exhibit to the Registrant’s current report on Form 8-K for June 6, 2011 filed with the Securities and Exchange Commission on June 7, 2011.

(2) Filed as an exhibit to the Registrant’s current report on Form 8-K for June 10, 2011 filed with the Securities and Exchange Commission on June 13, 2011.

(3) Filed as an exhibit to the Registrant's current report on Form 8-K for June 30, 2011 filed with the Securities and Exchange Commission on July 1, 2011.

(4) Filed as an exhibit to the Registrant's current report on Form 8-K for June 30, 2011 filed with the Securities and Exchange Commission on July 6, 2011.

(5) Pursuant to applicable securities laws and regulations, we are deemed to have complied with the reporting obligation relating to the submission of interactive data files in such exhibits and are not subject to liability under any anti-fraud provisions of the federal securities laws as long as we have made a good faith attempt to comply with the submission requirements and promptly amend the interactive data files after becoming aware that the interactive data files fail to comply with the submission requirements. Users of this data are advised that, pursuant to Rule 406T, these interactive data files are deemed not filed and otherwise are not subject to liability.

SIGNATURES

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

	PACIFIC ETHANOL, INC.	
Dated: August 11, 2011	By:	/s/ BRYON T. MCGREGOR Bryon T. McGregor Chief Financial Officer (Principal Financial and Accounting Officer)

EXHIBITS FILED WITH THIS REPORT

Exhibit Number	Description
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101.PRE	XBRL Taxonomy Extension Presentation Linkbase*

(*) Pursuant to applicable securities laws and regulations, we are deemed to have complied with the reporting obligation relating to the submission of interactive data files in such exhibits and are not subject to liability under any anti-fraud provisions of the federal securities laws as long as we have made a good faith attempt to comply with the submission requirements and promptly amend the interactive data files after becoming aware that the interactive data files fail to comply with the submission requirements. Users of this data are advised that, pursuant to Rule 406T, these interactive data files are deemed not filed and otherwise are not subject to liability.